MALVERN BANCORP, INC.
Form 10-K
December 14, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended: September 30, 2018

or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to

Commission File Number: 000-54835

MALVERN BANCORP, INC.

(Exact name of Registrant as specified in its charter)

Pennsylvania (State or Other Jurisdiction of Incorporation or Organization)	45-5307782 (I.R.S. Employer Identification Number)
42 E. Lancaster Avenue, Paoli, Pennsylvania (Address of Principal Executive Offices)	19301 (Zip Code)

Registrant s telephone number, including area code: (610) 644-9400

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $.01 par value per share	The NASDAQ Stock Market, LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES NO

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant s knowledge in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates was approximately $155.2 million, based on the last sale price on the NASDAQ Stock Market for the last business day of the Registrant s most recently completed second fiscal quarter.

The number of shares of the Issuer s common stock, par value $0.01 per share, outstanding as of December 14, 2018 was 7,771,356.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 2019 Annual Meeting of Shareholders are incorporated by reference into Part III, Items 10-14 of this Form 10-K.

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Information included in or incorporated by reference in this Annual Report on Form 10-K, other filings with the Securities and Exchange Commission, the Company s press releases or other public statements, contain or may contain forward looking statements. Please refer to a discussion of the Corporation s forward looking statements and associated risks in Item 1 Business and Item 1A Risk factors in this Annual Report on Form 10-K.

PART I.

This report, in Item 1, Item 7 and elsewhere, includes forward-looking statements within the meaning of Sections 27A of the Securities Act of 1933, as amended, and 21E of the Securities Exchange Act of 1934, as amended, that involve inherent risks and uncertainties. This report contains certain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance and business of Malvern Bancorp, Inc. and its subsidiaries, including statements preceded by, followed by or that include words or phrases such as believes, expects, anticipates, plans, trend, objective, continue, remain, pattern or similar expressions or future or conditional verbs such as will, would, should, could, might, can, may or similar expressions. There are a number of important factors that could cause future results to differ materially from historical performance and these forward-looking statements. Factors that might cause such a difference include, but are not limited to: (1) competitive pressures among depository institutions may increase significantly; (2) changes in the interest rate environment may reduce interest margins; (3) prepayment speeds, loan origination and sale volumes, charge-offs and loan loss provisions may vary substantially from period to period; (4) general economic conditions may be less favorable than expected; (5) political developments, wars or other hostilities may disrupt or increase volatility in securities markets or other economic conditions; (6) legislative or regulatory changes or actions may adversely affect the businesses in which Malvern Bancorp, Inc. is engaged; (7) changes and trends in the securities markets may adversely impact Malvern Bancorp, Inc.; (8) difficulties in integrating any businesses that we may acquire, which may increase our expenses and delay the achievement of any benefits that we may expect from such acquisitions; (9) the impact of reputation risk created by the developments discussed above on such matters as business generation and retention, funding and liquidity could be significant; and (10) the outcome of any regulatory or legal investigations and proceedings may not be anticipated. Further information on other factors that could affect the financial results of Malvern Bancorp, Inc. are included in Item 1A of this Annual Report on Form 10-K and in Malvern Bancorp s other filings with the Securities and Exchange Commission. These documents are available free of charge at the Commission s website at http://www.sec.gov and/or from Malvern Bancorp, Inc. Malvern Bancorp, Inc. assumes no obligation to update forward-looking statements at any time.

Item 1. Business

General

Malvern Bancorp, Inc. (the Company or Malvern Bancorp), a Pennsylvania corporation, is a registered bank holding company under the Bank Holding Company Act of 1956, as amended (the Holding Company Act). Malvern Bancorp is the holding company for Malvern Bank, National Association (Malvern Bank or the Bank), a national bank that was originally organized in 1887 as a federally-chartered savings bank. Malvern Bank now serves as one of the oldest banks headquartered on the Philadelphia Main Line. For more than a century, the Bank has been committed to helping people build prosperous communities as a trusted financial partner, forging lasting relationships through teamwork, respect and integrity. Effective February 12, 2018, the Bank converted from a federal savings bank charter to a national bank charter and Malvern Bancorp converted from a savings and loan holding company to a bank holding company. As previously disclosed in the Company s Form 8-K filed on October 9, 2018, the Company closed an underwritten public offering of shares of our common stock for gross proceeds of $25.0 million and net proceeds of approximately $23.4 million (after deducting the underwriting discount and other estimated offering expenses).

The Bank conducts business from its headquarters in Paoli, Pennsylvania, a suburb of Philadelphia, and through its nine other banking locations in Chester, Delaware and Bucks counties, Pennsylvania, Palm Beach, Florida, and Morristown, New Jersey, its New Jersey regional headquarters. The Bank also maintains a representative office in Montchanin, Delaware. The Bank s primary market niche is providing personalized service to its client base.

The Bank, through its Private Banking division and strategic partnership with Bell Rock Capital in Rehoboth Beach, Delaware, provides personalized wealth management and advisory services to high net worth individuals and families. Those services include banking, liquidity management, investment services, 401(k) accounts and planning, custody, tailored lending, wealth planning, trust and fiduciary services, family wealth advisory services and philanthropic advisory services. The Bank offers insurance services though Malvern Insurance Associates, LLC, which provides clients a rich array of financial services, including commercial and personal insurance and commercial and personal lending.

The Bank s principal business consists of attracting deposits from businesses and the general public and investing those deposits, together with borrowings and funds generated from operations, in one- to four-family residential real estate loans, construction and development loans, commercial and multi-family real estate loans, commercial business loans, home equity loans and lines of credit and other consumer loans, as well as investing in investment securities. In addition to the Pennsylvania counties referred to above, the Bank also serves client needs in the New Jersey, New York, Delaware, and greater Philadelphia market area.

The Bank s revenues are derived principally from interest on loans and investment securities, loan commitment and customer service fees and our mortgage banking operation. Our primary sources of funds are deposits, borrowings and principal and interest payments on loans and securities, as well as the sale of residential loans in the secondary market. The Bank s primary expenses are interest expense on deposits and borrowings, provisions for loan losses and general operating expenses.

The Bank owns 100% of Malvern Insurance Associates, LLC (Malvern Associates), a Pennsylvania limited liability company. Malvern Associates is a licensed insurance broker under Pennsylvania and New Jersey law.

The Bank owns a 10% non-controlling interest in Bell Rock Capital, LLC (Bell Rock), a Delaware limited liability company and investment advisor registered with the SEC, and headquartered in Rehoboth Beach, Delaware.

Certain mortgage-backed securities of the Bank are held through Delaware statutory trusts, 5% of which are owned by the Bank and 95% of which are owned by Coastal Asset Management Co., a Delaware corporation which is wholly owned by the Bank.

The Bank owns a 3.39% interest in Bankers Settlement Services Capital Region, LLC, a Pennsylvania limited liability company which acts as a title insurance agent or agency.

The Bank has a representative office which is not a branch, in Montchanin, Delaware.

SEC Reports and Corporate Governance

The Company makes its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and amendments thereto available on its website at *ir.malvernbancorp.com* without charge as soon as reasonably practicable after filing or furnishing them to the SEC. Also available on the website are the Company s corporate code of ethics that applies to all of the Company s employees, including principal officers and directors, and charters for the Audit Committee, Compensation Committee and Nominating Committee.

Additionally, the Company will provide without charge, a copy of its Annual Report on Form 10-K to any shareholder by mail, upon request. Requests should be sent to Malvern Bancorp, Inc., Attention: Shareholder Relations, 42 East Lancaster Avenue, Paoli, Pennsylvania, 19301. Our telephone number is (610) 644-9400.

Market Area and Competition

The banking business is highly competitive. We face substantial immediate competition and potential future competition both in attracting deposits and in originating loans. We compete with numerous commercial banks, savings banks and savings and loan associations, many of which have assets, capital and lending limits larger than those that we have. Other competitors include money market mutual funds, mortgage bankers, insurance companies, stock brokerage firms, regulated small loan companies, credit unions and issuers of commercial paper and other securities.

Our larger competitors have greater financial resources to finance wide-ranging advertising campaigns.

Additionally, we endeavor to compete for business by providing high quality, personal service to customers, customer access to our decision-makers and competitive interest rates and fees. We seek to hire and retain quality employees who desire greater responsibility than may be available working for a larger employer. Additionally, the local real estate and other business activities of the members of our Board of Directors help us develop business relationships by increasing our profile in our communities.

Products and Services

We derive substantially all of our income from our net interest income (i.e., the difference between the interest we receive on our loans and securities and the interest we pay on deposits and other borrowings). We offer a broad range of deposit and loan products. In addition, to attract the business of consumer and business customers, we also provide a broad array of other banking services. Products and services provided include personal and business checking accounts, retirement accounts, money market accounts, time and savings accounts, credit cards, wire transfers, access to automated teller services, internet banking, ACH origination, telephone banking, and mobile banking by phone. In addition, we offer safe deposit boxes. The Bank also offers remote deposit capture banking for business customers, providing the ability to electronically scan and transmit checks for deposit, reducing time and cost. In addition, the Bank offers mobile remote deposit capture banking for both retail and business customers, providing the convenience to deposit on the go.

Checking account products consist of both retail and business demand deposit products. Retail products include free checking and, for businesses, both interest-bearing accounts, which require a minimum balance, and non-interest-bearing accounts. NOW accounts consist of both retail and business interest-bearing transaction accounts that have minimum balance requirements. Money market accounts consist of products that provide a market rate of interest to depositors but have limited check writing capabilities. Our savings accounts consist of statement type accounts. Time deposits consist of certificates of deposit, including those held in IRA accounts. CDARS/ICS Reciprocal deposits are offered through the Bank s participation in Promontory Interfinancial Network, LLC. Customers who are FDIC insurance sensitive are able to place large dollar deposits with the Company and the Company uses CDARS to place those funds into certificates of deposit issued by other banks in the Network. This occurs in increments of less than the FDIC insurance limits so that both the principal and interest are eligible for complete FDIC insurance coverage. The FDIC currently considers these funds as brokered deposits.

The Bank, through its partnership with Bell Rock, offers through its wealth management division personalized wealth management and advisory services to high net worth individuals and families. Services provided include liquidity management, investment services, custody, wealth planning, trust and fiduciary services, insurance and 401(k) services.

The Bank, through its wholly-owned subsidiary, Malvern Associates, offers insurance services.

Deposits serve as the primary source of funding for our interest-earning assets, but also generate non-interest revenue through insufficient funds fees, stop payment fees, safe deposit rental fees, card income,

including credit and debit card interchange fees, gift card fees, and other miscellaneous fees. In addition, the Bank generates additional non-interest revenue associated with residential loan origination and sale, loan servicing, late fees and merchant services.

We offer personal and commercial business loans on a secured and unsecured basis, revolving lines of credit, commercial mortgage loans, and residential mortgages on both primary and secondary residences, home equity loans, bridge loans and other personal purpose loans. However, we are not and have not historically been a participant in the sub-prime lending market.

Commercial loans are loans made for business purposes and are primarily secured by collateral such as cash balances with the Bank, marketable securities held by or under the control of the Bank, business assets including accounts receivable, inventory and equipment, and liens on commercial and residential real estate.

Commercial construction loans are loans to finance the construction of commercial or residential properties secured by first liens on such properties. Commercial real estate loans include loans secured by first liens on completed commercial properties, including multi-family properties, to purchase or refinance such properties. Residential mortgages include loans secured by first liens on residential real estate, and are generally made to existing customers of the Bank to purchase or refinance primary and secondary residences. Home equity loans and lines of credit include loans secured by first or second liens on residential real estate for primary or secondary residences.

Consumer loans are made to individuals who qualify for auto loans, cash reserve, credit cards and installment loans.

The Bank s lending policies generally provide for lending inside of our primary market area. However, the Bank will make loans to persons outside of our primary market area when we deem it prudent to do so. In an effort to promote a high degree of asset quality, the Bank focuses primarily upon offering secured loans. However, the Bank does make unsecured loans to borrowers with high net worth and income profiles. The Bank generally requires loan customers to maintain deposit accounts with the Bank. In addition, the Bank generally provides for a minimum required rate of interest in its variable rate loans. We believe that having senior management on-site allows for an enhanced local presence and rapid decision-making that attracts borrowers.

As a national bank, the Bank s lending limit to any one borrower is 15% of the Bank s capital and surplus (defined as Tier 1 and Tier 2 capital calculated under the risk-based capital standards applicable to the Bank plus the allowance for loan losses (ALLL , allowance) not included in the Bank s Tier 2 capital) for most loans ($21.1 million) and 25% of the Bank s capital and surplus for loans secured by readily marketable collateral ($35.2 million). At September 30, 2018, the Bank s largest committed relationship totaled $18.5 million.

Our business model includes using industry best practices for community banks, including personalized service, state-of-the-art technology and extended hours. We believe that this will generate deposit accounts with larger average balances than we might attract otherwise. We also use pricing techniques in our efforts to attract banking relationships having larger than average balances.

Supervision and Regulation

The banking industry is highly regulated. Earnings of the Company are affected by state and federal laws and regulations and by policies of various regulatory authorities. Changes in applicable law or in the policies of various regulatory authorities could affect materially the business and prospects of the Company and the Bank. The following discussion of supervision and regulation is qualified in its entirety by reference to the statutory and regulatory provisions discussed.

Regulation of Malvern Bancorp, Inc.

Malvern Bancorp is a bank holding company within the meaning of the Holding Company Act. As a bank holding company, Malvern Bancorp is supervised by the Federal Reserve Board (the FRB) and is required to file reports with the FRB and provide such additional information as the FRB may require.

The Holding Company Act prohibits Malvern Bancorp, with certain exceptions, from acquiring direct or indirect ownership or control of more than five percent of the voting shares of any company which is not a bank and from engaging in any business other than that of banking, managing and controlling banks or furnishing services to subsidiary banks, except that it may, upon application, engage in, and may own shares of companies engaged in, certain businesses found by the FRB to be so closely related to banking as to be a proper incident thereto. The Holding Company Act requires prior approval by the FRB of the acquisition by Malvern Bancorp of more than five percent of the voting stock of any other bank. Satisfactory capital ratios, Community Reinvestment Act ratings, and anti-money laundering policies are generally prerequisites to obtaining federal regulatory approval to make acquisitions. The policy of the FRB provides that a bank holding company is expected to act as a source of financial strength to its subsidiary bank and to commit resources to support its subsidiary bank in circumstances in which it might not do so absent that policy. Acquisitions by Malvern Bank require approval of the Office of the Comptroller of the Currency (the OCC).

The Holding Company Act does not place territorial restrictions on the activities of non-bank subsidiaries of bank holding companies.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 enables bank holding companies to acquire banks in states other than the bank holding company s home state and to open branches in other states, subject to certain restrictions. The Dodd-Frank Act, discussed below, authorized interstate *de novo* branching regardless of state law.

Regulation of Malvern Bank

As a national bank, Malvern Bank is subject to the supervision of, and to regular examination by the OCC. Various laws and the regulations promulgated thereunder applicable to Malvern Bancorp and Malvern Bank impose restrictions and requirements in many areas, including capital requirements, the maintenance of reserves, establishment of new offices, the making of loans and investments, consumer protection, employment practices, bank acquisitions and entry into new types of business. There are various legal limitations, including Sections 23A and 23B of the Federal Reserve Act, which govern the extent to which a bank subsidiary may finance or otherwise supply funds to its holding company or its holding company s non-bank subsidiaries. Under federal law, no bank subsidiary may, subject to certain limited exceptions, make loans or extensions of credit to, or investments in the securities of, its parent or the non-bank subsidiaries of its parent (other than direct subsidiaries of such bank which are not financial subsidiaries) or take their securities as collateral for loans to any borrower. Each bank subsidiary is also subject to collateral security requirements for any loans or extensions of credit permitted by such exceptions.

Capital Requirements

Pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), each federal banking agency has promulgated regulations, specifying the levels at which a financial institution would be considered well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, or critically undercapitalized, to take certain mandatory and discretionary supervisory actions based on the capital level of the institution.

In July 2013, the FRB and the OCC published final rules establishing a new comprehensive capital framework for U.S. banking organizations, referred to as the Basel III rules. The Basel III rules implement the

Basel Committee s December 2010 framework, commonly referred to as Basel III, for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. Basel III substantially revised the risk-based capital requirements applicable to bank holding companies and depository institutions, including Malvern Bancorp and Malvern Bank. Basel III became effective for us on January 1, 2015 (subject to phase-in periods for certain components).

Basel III (i) introduced a new capital measure called Common Equity Tier 1, or CET1, (ii) specified that Tier 1 capital consists of CET1 and Additional Tier 1 capital instruments meeting specified requirements, (iii) applied most deductions/adjustments to regulatory capital measures to CET1 and not to the other components of capital, thus potentially requiring higher levels of CET1 in order to meet minimum ratios, and (iv) expanded the scope of the reductions/adjustments from capital as compared to existing regulations.

Under Basel III, the minimum capital ratios for Malvern Bancorp and Malvern Bank are as follows:

- 4.5 percent CET1 to risk-weighted assets.
- 6.0 percent Tier 1 capital (i.e., CET1 plus Additional Tier 1) to risk-weighted assets.
- 8.0 percent Total capital (i.e., Tier 1 plus Tier 2) to risk-weighted assets.
- 4.0 percent Tier 1 capital to average consolidated assets as reported on consolidated financial statements (known as the leverage ratio).

When fully phased in on January 1, 2019, Basel III also requires Malvern Bancorp and Malvern Bank to maintain a 2.5 percent capital conservation buffer , composed entirely of CET1, on top of the minimum risk-weighted asset ratios, effectively resulting in minimum ratios of (i) CET1 to risk-weighted assets of at least 7.0 percent, (ii) Tier 1 capital to risk-weighted assets of at least 8.5 percent, and (iii) total capital to risk-weighted assets of at least 10.5 percent. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of (i) CET1 to risk-weighted assets, (ii) Tier 1 capital to risk-weighted assets or (iii) total capital to risk-weighted assets above the respective minimum but below the capital conservation buffer will face constraints on dividends, equity repurchases and discretionary bonus payments to executive officers based on the amount of the shortfall. The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625 percent level and will increase by 0.625 percent on each subsequent January 1st, until it reaches 2.5 percent on January 1, 2019. As of September 30, 2018, Malvern Bancorp and Malvern Bank were required to maintain a capital conservation buffer of 1.875% percent.

Basel III provides for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets dependent upon future taxable income and significant investments in common equity issued by nonconsolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10 percent of CET1 or all such categories in the aggregate exceed 15 percent of CET1. The deductions and other adjustments to CET1 were being phased in incrementally between January 1, 2015 and January 1, 2018. However, in November 2017, banking regulators announced that the phase in of certain of these adjustments for non-advanced approaches banking organizations, such as Malvern Bank, was frozen.

Under current capital standards, the effects of accumulated other comprehensive income items included in capital are excluded for the purposes of determining regulatory capital ratios. Under Basel III, the effects of certain accumulated other comprehensive items are not excluded; however, non-advanced approaches banking organizations, including Malvern Bancorp and Malvern Bank, were permitted to make a one-time permanent election to continue to exclude these items effective as of January 1, 2015. We made this one-time election in the applicable bank regulatory reports as of March 31, 2015.

With respect to Malvern Bank, Basel III also revised the prompt corrective action regulations pursuant to Section 38 of FDICIA, by (i) introducing a CET1 ratio requirement at each capital quality level (other than

critically undercapitalized); (ii) increasing the minimum Tier 1 capital ratio requirement for each category; and (iii) requiring a leverage ratio of 5 percent to be well-capitalized. The OCC s regulations implementing these provisions of FDICIA provide that an institution will be classified as well capitalized if it (i) has a total risk-based capital ratio of at least 10.0 percent, (ii) has a Tier 1 risk-based capital ratio of at least 8.0 percent, (iii) has a CET1 ratio of at least 6.5 percent, (iv) has a Tier 1 leverage ratio of at least 5.0 percent, and (v) meets certain other requirements. An institution will be classified as adequately capitalized if it meets the aforementioned minimum capital ratios under Basel III. An institution will be classified as undercapitalized if it (i) has a total risk-based capital ratio of less than 8.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 6.0 percent, (iii) has a CET1 ratio of less than 4.5 percent or (iv) has Tier 1 leverage ratio of less than 4.0 percent. An institution will be classified as significantly undercapitalized if it (i) has a total risk-based capital ratio of less than 6.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 4.0 percent, (iii) has a CET1 ratio of less than 3.0 percent or (iv) has a Tier 1 leverage ratio of less than 3.0 percent. An institution will be classified as critically undercapitalized if it has a tangible equity to total assets ratio that is equal to or less than 2.0 percent. An insured depository institution may be deemed to be in a lower capitalization category if it receives an unsatisfactory examination rating. Similar categories apply to bank holding companies. When the capital conservation buffer is fully phased in, the capital ratios applicable to depository institutions under Basel III will exceed the ratios to be considered well-capitalized under the prompt corrective action regulations.

Basel III prescribes a standardized approach for calculating risk-weighted assets that expand the risk-weighting categories from the four Basel I-derived categories (0 percent, 20 percent, 50 percent and 100 percent) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets.

As indicated in the following tables, the capital ratios of Malvern Bank and Malvern Bancorp met all regulatory requirements as of September 30, 2018. In addition, we believe that as of September 30, 2018, Malvern Bancorp and Malvern Bank would meet all capital adequacy requirements under Basel III on a fully phased-in basis if such requirements were currently effective.

Malvern Bank s capital ratios as of September 30, 2018 are as follows:

	Actual		**Required for Capital Adequacy Purposes**		**To Be Well Capitalized Under Prompt Corrective Action Provisions**		**Excess Over Well-Capitalized Provision**	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
	(Dollars in thousands)							
Tier 1 leverage capital (to adjusted tangible assets)	$ 131,746	12.71%	$ 41,450	4.00%	$ 51,812	5.00%	$ 79,934	7.71%
Common equity Tier 1 (to risk-weighted assets)	$ 131,746	15.09	39,293	4.50	56,756	6.50	74,990	8.59
Tier 1 risk-based capital (to risk-weighted assets)	$ 131,746	15.09	52,390	6.00	69,853	8.00	61,893	7.09
Total risk-based capital (to risk-weighted assets)	$ 140,833	16.13	69,853	8.00	87,317	10.00	53,516	6.13

Failure to meet any of the capital requirements could result in enforcement actions by the regulators, including a capital directive, a cease and desist order, civil money penalties, the establishment of restrictions on the institution s operations, termination of federal deposit insurance and the appointment of a conservator or receiver.

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Malvern Bancorp s capital ratios as of September 30, 2018 are as follows:

	Actual		Required for Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions		Excess Over Well-Capitalized Provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)							
Tier 1 leverage capital (to adjusted tangible assets)	$ 110,239	10.63%	$ 41,491	4.00%	$ 51,864	5.00%	$ 58,375	5.63%
Common equity Tier 1 (to risk-weighted assets)	$ 110,239	12.62	39,322	4.50	56,799	6.50	53,440	6.12
Tier 1 risk-based capital (to risk-weighted assets)	$ 110,239	12.62	52,430	6.00	69,906	8.00	40,333	4.62
Total risk-based capital (to risk-weighted assets)	$ 143,787	16.45	69,906	8.00	87,383	10.00	56,404	6.45

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

On July 21, 2010, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The Dodd-Frank Act has significantly changed the bank regulatory structure and significantly impacted the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies have been given significant discretion in drafting the implementing rules and regulations. The discussion below generally discusses the material provisions of the Dodd-Frank Act applicable to the Company and the Bank and is not complete or meant to be an exhaustive discussion.

The following aspects of the Dodd-Frank Act are related to the operations of the Bank:

A new independent consumer financial protection bureau was established within the Federal Reserve Board, empowered to exercise broad regulatory, supervisory and enforcement authority with respect to both new and existing consumer financial protection laws. Financial institutions with assets of $10 billion or less, such as the Bank, are subject to the supervision and enforcement of their primary federal banking regulator with respect to the federal consumer financial protection laws.

Tier 1 capital treatment for hybrid capital items like trust preferred securities was eliminated subject to various grandfathering and transition rules.

The prohibition on payment of interest on demand deposits was repealed.

State consumer financial law is preempted only if it would have a discriminatory effect on a national bank, prevents or significantly interferes with the exercise by a national bank of its powers or is preempted by any other federal law. The OCC must make a preemption determination on a case-by-case basis with respect to a particular state law or another state law with substantively equivalent terms.

Deposit insurance has been permanently increased to $250,000.

The deposit insurance assessment base calculation equals the depository institution s total assets minus the sum of its average tangible equity during the assessment period.

The minimum reserve ratio of the Deposit Insurance Fund increased to 1.35 percent of estimated annual insured deposits or assessment base; however, the Federal Deposit Insurance Corporation (the FDIC) was directed to offset the effect of the increased reserve ratio for insured depository institutions with total consolidated assets of less than $10 billion.

The following aspects of the Dodd-Frank Act are related to the operations of the Company:

The Federal Deposit Insurance Act was amended to direct federal regulators to require depository institution holding companies to serve as a source of strength for their depository institution subsidiaries.

Public companies are required to provide their shareholders with a non-binding vote: (i) at least once every three years on the compensation paid to executive officers, and (ii) at least once every six years on whether they should have a say on pay vote every one, two or three years.

A separate, non-binding shareholder vote is required regarding golden parachutes for named executive officers when a shareholder vote takes place on mergers, acquisitions, dispositions or other transactions that would trigger the parachute payments.

Securities exchanges are required to prohibit brokers from using their own discretion to vote shares not beneficially owned by them for certain significant matters, which include votes on the election of directors, executive compensation matters, and any other matter determined to be significant.

Stock exchanges, which includes The NASDAQ Stock Market, LLC (NASDAQ), will be prohibited from listing the securities of any issuer that does not have a policy providing for (i) disclosure of its policy on incentive compensation payable on the basis of financial information reportable under the securities laws, and (ii) the recovery from current or former executive officers, following an accounting restatement triggered by material noncompliance with securities law reporting requirements, of any incentive compensation paid erroneously during the three-year period preceding the date on which the restatement was required that exceeds the amount that would have been paid on the basis of the restated financial information. See Incentive Compensation below.

Disclosure in annual proxy materials will be required concerning the relationship between the executive compensation paid and the financial performance of the issuer.

Item 402 of Regulation S-K has been amended to require companies to disclose the ratio of the Chief Executive Officer s annual total compensation to the median annual total compensation of all other employees. This information must be reported for the first time for the first full fiscal year beginning on or after January 1, 2017; accordingly, this information will be included in the Company s proxy statement for its 2019 annual meeting of shareholders.

Volcker Rule Regulations

Regulations adopted by the federal banking agencies to implement the provisions of the Dodd Frank Act commonly referred to as the Volcker Rule contain prohibitions and restrictions on the ability of financial institution holding companies and their affiliates to engage in proprietary trading and to hold certain interests in, or to have certain relationships with, various types of investment funds, including hedge funds and private equity funds. The Company

is in compliance with the various provisions of the Volcker Rule regulations.

Incentive Compensation

The Dodd-Frank Act requires the federal bank regulatory agencies and the SEC to establish joint regulations or guidelines prohibiting incentive-based payment arrangements at specified regulated entities with at least $1 billion in total assets, such as Malvern Bancorp and the Bank, that encourage inappropriate risks by providing an executive officer, employee, director or principal shareholder with excessive compensation, fees, or benefits or that could lead to material financial loss to the entity. In addition, these agencies must establish regulations or guidelines requiring enhanced disclosure to regulators of incentive-based compensation arrangements. The agencies proposed such regulations in April 2011 and subsequently proposed revised regulations in May 2016, but the revised regulations have not been finalized. If the revised regulations are adopted in the form proposed, they will impose limitations on the manner in which Malvern Bancorp may structure compensation for its executives and employees.

In 2010, the FRB, OCC and FDIC issued comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization s incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization s ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization s board of directors. These three principles are incorporated into the proposed joint compensation regulations under the Dodd-Frank Act.

The FRB will review, as part of its regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as Malvern Bancorp, that are not large, complex banking organizations. These reviews will be tailored to each organization based on the scope and complexity of the organization s activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization s supervisory ratings, which can affect the organization s ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization s safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

Dividend Limitations

Malvern Bancorp is a legal entity separate and distinct from its subsidiaries. Malvern Bancorp s revenues (on a parent company only basis) result in substantial part from dividends paid by the Bank. The Bank s dividend payments, without prior regulatory approval, are subject to regulatory limitations. Under the National Bank Act, dividends may be declared only if, after payment thereof, capital would be unimpaired and remaining surplus would equal 100 percent of capital. Moreover, a national bank may declare, in any one year, dividends only in an amount aggregating not more than the sum of its net profits for such year and its retained net profits for the preceding two years. However, declared dividends in excess of net profits in either of the preceding two years can be offset by retained net profits in the third and fourth years preceding the current year when determining the Bank s dividend limitation. In addition, the bank regulatory agencies have the authority to prohibit the Bank from paying dividends or otherwise supplying funds to Malvern Bancorp if the supervising agency determines that such payment would constitute an unsafe or unsound banking practice.

Loans to Related Parties

Malvern Bank s authority to extend credit to its directors, executive officers and 10 percent shareholders, as well as to entities controlled by such persons, is currently governed by the requirements of the National Bank Act, Sarbanes-Oxley Act and Regulation O of the FRB thereunder. Among other things, these provisions require that extensions of credit to insiders (i) be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features and (ii) not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the Bank s capital. In addition, extensions of credit in excess of certain limits must be approved by the Bank s Board of Directors. Under the Sarbanes-Oxley Act, Malvern Bancorp and its subsidiaries, other than the Bank under the authority of Regulation O, may not extend or arrange for any personal loans to its directors and executive officers.

Community Reinvestment

Under the Community Reinvestment Act (CRA), as implemented by OCC regulations, a national bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of

its entire community, including low and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution s discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA requires the OCC, in connection with its examination of a national bank, to assess the association s record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such association. The CRA also requires all institutions to make public disclosure of their CRA ratings. Malvern Bank received an overall satisfactory CRA rating in its most recent examination. A bank which does not have a CRA program that is deemed satisfactory by its regulator will be prevented from making acquisitions.

Corporate Governance

The Sarbanes-Oxley Act of 2002 added new legal requirements for public companies affecting corporate governance, accounting and corporate reporting, to increase corporate responsibility and to protect investors. Among other things, the Sarbanes-Oxley Act of 2002:

- required our management to evaluate our disclosure controls and procedures and our internal control over financial reporting, and required our auditors to issue a report on our internal control over financial reporting;

- imposed on our chief executive officer and chief financial officer additional responsibilities with respect to our external financial statements, including certification of financial statements within the Annual Report on Form 10-K and Quarterly Reports on Form 10-Q by the chief executive officer and the chief financial officer;

- established independence requirements for audit committee members and outside auditors;

- created the Public Company Accounting Oversight Board which oversees public accounting firms; and

- increased various criminal penalties for violations of securities laws.

NASDAQ, where Malvern Bancorp s common stock is listed, has corporate governance listing standards, including rules strengthening director independence requirements for boards, as well as the audit committee and the compensation committee, and requiring the adoption of charters for the nominating, corporate governance, compensation and audit committees.

USA PATRIOT Act

As part of the USA PATRIOT Act, Congress adopted the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (the Anti Money Laundering Act). The Anti Money Laundering Act authorizes the Secretary of the U.S. Treasury, in consultation with the heads of other government agencies, to adopt special measures applicable to financial institutions such as banks, bank holding companies, broker-dealers and insurance companies. Among its other provisions, the Anti Money Laundering Act requires each financial institution: (i) to establish an anti-money laundering program; (ii) to establish due diligence policies, procedures and controls that are reasonably

designed to detect and report instances of money laundering in United States private banking accounts and correspondent accounts maintained for non-United States persons or their representatives; and (iii) to avoid establishing, maintaining, administering, or managing correspondent accounts in the United States for, or on behalf of, a foreign shell bank that does not have a physical presence in any country.

Regulations implementing the due diligence requirements require minimum standards to verify customer identity and maintain accurate records, encourage cooperation among financial institutions, federal banking agencies, and law enforcement authorities regarding possible money laundering or terrorist activities, prohibit the anonymous use of concentration accounts, and require all covered financial institutions to have in place an anti-money laundering compliance program.

The OCC, along with other banking agencies, have strictly enforced various anti-money laundering and suspicious activity reporting requirements using formal and informal enforcement tools to cause banks to comply with these provisions.

A bank which is issued a formal or informal enforcement requirement with respect to its Anti Money Laundering program will be prevented from making acquisitions.

Insurance of Accounts

The deposits of the Bank are insured to the maximum extent permitted by the Deposit Insurance Fund and are backed by the full faith and credit of the U.S. Government. As insurer, the FDIC is authorized to conduct examinations of, and to require reporting by, insured institutions. It also may prohibit any insured institution from engaging in any activity determined by regulation or order to pose a serious threat to the FDIC. The FDIC also has the authority to initiate enforcement actions against national banks, after giving the OCC an opportunity to take such action.

The FDIC s risk-based premium system provides for quarterly assessments. Each insured institution is placed in one of four risk categories depending on supervisory and capital considerations. Within its risk category, an institution is assigned to an initial base assessment rate which is then adjusted to determine its final assessment rate based on its brokered deposits, secured liabilities and unsecured debt. To implement the Dodd Frank Act, the FDIC amended its deposit insurance regulations (1) to change the assessment base for insurance from domestic deposits to average assets minus average tangible equity and (2) to lower overall assessment rates. The revised assessments rates are between 2.5 to 9 basis points for banks in the lowest risk category and between 30 to 45 basis points for banks in the highest risk category.

In addition, all institutions with deposits insured by the FDIC are required to pay assessments to fund interest payments on bonds issued by the Financing Corporation, or FICO, a mixed-ownership government corporation established to recapitalize the predecessor to the Deposit Insurance Fund. These assessments will continue until the Financing Corporation bonds mature in 2019.

The FDIC may terminate the deposit insurance of any insured depository institution, including the Bank, if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, order or any condition imposed by an agreement with the FDIC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance, if the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC. Management is not aware of any existing circumstances which could result in termination of the Bank s deposit insurance.

As noted above, the Dodd Frank Act raises the minimum reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35% and requires the FDIC to offset the effect of this increase on insured institutions with assets of less than $10 billion (small institutions). The FDIC has adopted a rule to accomplish this by imposing a surcharge on larger institutions commencing when the reserve ratio reaches 1.15% and ending when it reaches 1.35%. The reserve ratio reached 1.15% on June 30, 2016. Accordingly, surcharges began on July 1, 2016. Small institutions will receive credits for the portion of their regular assessments that contributed to growth in the reserve ratio between 1.15% and 1.35%. The credits will apply for each quarter the reserve ratio is above 1.38%, in amounts as determined by the FDIC.

Federal Home Loan Bank System.

Malvern Bank is a member of the Federal Home Loan Bank of Pittsburgh, which is one of 12 regional Federal Home Loan Banks (FHLB). Each FHLB serves as a reserve or central bank for its members within its

assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the board of directors of the FHLB. At September 30, 2018, the Bank had $118.0 million of FHLB advances and $150.0 million available on its line of credit with the FHLB.

As a member, the Bank is required to purchase and maintain stock in the FHLB of Pittsburgh in an amount equal to at least 1.0% of its aggregate unpaid residential mortgage loans or similar obligations at the beginning of each year. At September 30, 2018, Malvern Bank had $6.1 million in FHLB stock, which was in compliance with this requirement.

Federal Reserve System. The FRB, requires all depository institutions to maintain reserves against their transaction accounts (primarily NOW and Super NOW checking accounts) and non-personal time deposits. Because required reserves must be maintained in the form of vault cash or a noninterest-bearing account at a Federal Reserve Bank, the effect of this reserve requirement is to reduce an institution s earning assets. At September 30, 2018, the Bank had met its reserve requirement.

Federal Securities Laws. Malvern Bancorp has registered its common stock with the Securities and Exchange Commission (the SEC) under Section 12(b) of the Securities Exchange Act of 1934 (the Exchange Act). Accordingly, Malvern Bancorp is subject to the proxy and tender offer rules, insider trading reporting requirements and restrictions, and certain other requirements under the Exchange Act.

Employees

As of September 30, 2018, we had a total of 85 full-time equivalent employees. No employees are represented by a collective bargaining group, and we believe that our relationship with our employees is excellent.

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Item 1A. Risk Factors.

In analyzing whether to make or to continue an investment in our securities, investors should consider, among other factors, the following risk factors.

We are subject to credit risk in connection with our lending activities, and our financial condition and results of operations may be negatively impacted by economic conditions and other factors that adversely affect our borrowers.

Our financial condition and results of operations are affected by the ability of our borrowers to repay their loans, and in a timely manner. Lending money is a significant part of the banking business. Borrowers, however, do not always repay their loans. The risk of non-payment is assessed through our underwriting and loan review procedures based on several factors including credit risks of a particular borrower, changes in economic conditions, the duration of the loan and in the case of a collateralized loan, uncertainties as to the future value of the collateral and other factors. Despite our efforts, we do and will experience loan losses, and our financial condition and results of operations will be adversely affected. Our non-performing assets were approximately $3.1 million at September 30, 2018. Our allowance for loan losses was approximately $9.0 million at September 30, 2018. Our loans between thirty and eighty-nine days delinquent totaled $9.2 million at September 30, 2018.

Our results of operations and financial condition may be adversely affected by changing economic conditions.

While the economy and real estate market conditions have significantly improved in recent years, a return to a recessionary period could adversely affect our customers in a manner that would adversely affect our results of operations and financial condition. Volatility in the housing markets, real estate values and unemployment levels, and the deterioration of economic conditions in our market area, could affect our customers ability to repay loans and adversely affect our results of operations and future growth potential in the following ways:

- Loan delinquencies may increase;
- Problem assets and foreclosures may increase;
- Demand for our products and services may decline;
- The carrying value of our other real estate owned may decline further; and
- Collateral for loans made by us, especially real estate, may continue to decline in value, in turn reducing a customer s borrowing power, and reducing the value of assets and collateral associated with our loans.

Changes in interest rates could adversely affect our financial condition and results of operation.

Our net income depends primarily upon our net interest income. Net interest income is the difference between interest income earned on loans, investments and other interest-earning assets and the interest expense incurred on deposits

and borrowed funds. The level of net interest income is primarily a function of the average balance of our interest-earning assets, the average balance of our interest-bearing liabilities, and the spread between the yield on such assets and the cost of such liabilities. These factors are influenced by both the pricing and mix of our interest-earning assets and our interest-bearing liabilities which, in turn, are impacted by such external factors as the local economy, competition for loans and deposits, the monetary policy of the Federal Open Market Committee of the Federal Reserve Board of Governors (the FOMC), and market interest rates.

Different types of assets and liabilities may react differently, and at different times, to changes in market interest rates. We expect that we will periodically experience gaps in the interest rate sensitivities of our assets and liabilities. That means either our interest-bearing liabilities will be more sensitive to changes in market

interest rates than our interest-earning assets, or vice versa. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets, an increase in market rates of interest could reduce our net interest income. Likewise, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could reduce our net interest income. We are unable to predict changes in market interest rates, which are affected by many factors beyond our control, including inflation, deflation, recession, unemployment, money supply, domestic and international events and changes in the United States and other financial markets.

We also attempt to manage risk from changes in market interest rates, in part, by controlling the mix of interest rate sensitive assets and interest rate sensitive liabilities. However, interest rate risk management techniques are not exact. A rapid increase or decrease in interest rates could adversely affect our results of operations and financial performance.

Our high concentration of commercial real estate loans exposes us to increased lending risk.

As of September 30, 2018, the primary composition of our total loan portfolio was as follows:

- commercial real estate loans of $493.9 million, or 54.2% of total loans;
- construction and development loans of $46.7 million, or 5.1% of total loans;
- commercial and industrial loans of $137.2 million, or 15.1% of total loans;
- residential real estate loans of $197.2 million, or 21.7% of total loans and
- consumer loans of $35.6 million, or 3.9% of total loans

Commercial real estate loans, which comprised 54.2% of our total loan portfolio as of September 30, 2018, expose us to a greater risk of loss than do residential mortgage loans. Commercial real estate loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to residential loans. Consequently, an adverse development with respect to one commercial loan or one credit relationship exposes us to a significantly greater risk of loss compared to an adverse development with respect to one residential mortgage loan. Any significant failure to pay on time by our customers or a significant default by our customers would materially and adversely affect us.

Although the economy in our market area generally, and the real estate market in particular, is improving, we can give you no assurance that it will continue to grow or that the rate of growth will accelerate to historic levels. Many factors could reduce or halt growth in our local economy and real estate market. Accordingly, it may be more difficult for commercial real estate borrowers to repay their loans in a timely manner in the current economic climate, as commercial real estate borrowers ability to repay their loans frequently depends on the successful development of their properties. The deterioration of one or a few of our commercial real estate loans could cause a material increase in our level of nonperforming loans, which would result in a loss of revenue from these loans and could result in an increase in the provision for loan and lease losses and/or an increase in charge-offs, all of which could have a material adverse impact on our net income. We also may incur losses on commercial real estate loans due to declines in occupancy rates and rental rates, which may decrease property values and may decrease the likelihood that a borrower

may find permanent financing alternatives. Given the continued weaknesses in the commercial real estate market in general, there may be loans where the value of our collateral has been negatively impacted. Any weakening of the commercial real estate market may increase the likelihood of default of these loans, which could negatively impact our loan portfolio s performance and asset quality. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, we could incur material losses. Any of these events could increase our costs, require management time and attention, and materially and adversely affect us.

If our allowance for loan losses is not sufficient to cover actual loan losses, our earnings will decrease.

Like all financial institutions, we maintain an allowance for loan losses to provide for loan defaults and nonperformance. In determining the amount of the allowance for loan losses, we review our loans and our loss and delinquency experience, and we evaluate economic conditions. If our assumptions are incorrect, our allowance for loan losses may not be sufficient to cover losses inherent in our loan portfolio.

In addition, bank regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities might have a material adverse effect on our financial condition and results of operations.

A new accounting standard will likely require us to increase our allowance for loan losses and may have a material adverse effect on our financial condition and results of operations.

The Financial Accounting Standards Board has adopted a new accounting standard that will be effective for the Company and the Bank for fiscal years beginning after December 15, 2019. This standard, referred to as Current Expected Credit Loss, or CECL, will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances for loan losses. This will change the current method of providing allowances for loan losses that are probable, which would likely require us to increase our allowance for loan losses, and to greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for loan losses. Any increase in our allowance for loan losses or expenses incurred to determine the appropriate level of the allowance for loan losses may have a material adverse effect on our financial condition and results of operations.

Failure to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act could have a material adverse effect on our business and stock price.

Section 404 of the Sarbanes-Oxley Act requires us to evaluate periodically the effectiveness of our internal controls over financial reporting and to include a management report assessing the effectiveness of our internal controls over financial reporting in our Annual Report on Form 10-K. Section 404 also requires our independent registered public accounting firm to report on our internal controls over financial reporting. If we fail to maintain the adequacy of our internal controls, we cannot assure you that we will be able to conclude in the future that we have effective internal controls over financial reporting. If we fail to maintain effective internal controls, we might be subject to sanctions or investigation by regulatory authorities, such as the SEC or NASDAQ. Any such action could adversely affect our financial results and the market price of our common stock and may also result in delayed filings with the SEC.

Strong competition within our market area could hurt our profits and slow growth.

The banking and financial services industry in our market area is highly competitive. We may not be able to compete effectively in our markets, which could adversely affect our results of operations. The increasingly competitive environment is a result of changes in regulation, changes in technology and product delivery systems, and consolidation among financial service providers. Larger institutions have greater access to capital markets, with higher lending limits and a broader array of services. Competition may require increases in deposit rates and decreases in loan rates, and adversely impact our net interest margin.

We operate in a highly regulated environment and we may be adversely affected by changes in laws and regulations.

We are subject to extensive regulation, supervision and examination by the FRB, our primary federal regulator, the OCC, the Bank s primary federal regulator, and by the FDIC, as insurer of the Bank s deposits.

Such regulation and supervision governs the activities in which an institution and its holding company may engage and are intended primarily for the protection of the insurance fund and the depositors and borrowers of the Bank rather than for holders of our common stock. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of our assets and determination of the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our operations.

The fair value of our investment securities can fluctuate due to market conditions outside of our control.

As of September 30, 2018, the fair value of our investment securities portfolio was approximately $54.4 million. We have historically taken a conservative investment strategy, with concentrations of securities that are backed by government sponsored enterprises. Factors beyond our control can significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. These factors include, but are not limited to, rating agency actions in respect of the securities, defaults by the issuer or with respect to the underlying securities, and changes in market interest rates and continued instability in the capital markets. Any of these factors, among others, could cause other-than-temporary impairments and realized and/or unrealized losses in future periods and declines in other comprehensive income, which could have a material adverse effect on us. The process for determining whether impairment of a security is other-than-temporary usually requires complex, subjective judgments about the future financial performance and liquidity of the issuer and any collateral underlying the security in order to assess the probability of receiving all contractual principal and interest payments on the security.

Our growth-oriented business strategy could be adversely affected if we are not able to attract and retain skilled employees or if we lose the services of our senior management team.

Our ability to manage growth will depend upon our ability to continue to attract, hire and retain skilled employees. The loss of members of our senior management team, including those officers named in the summary compensation table of our proxy statement, could have a material adverse effect on our results of operations and ability to execute our strategic goals. Our success will also depend on the ability of our officers and key employees to continue to implement and improve our operational and other systems, to manage multiple, concurrent customer relationships and to hire, train and manage our employees.

We are dependent on our information technology and telecommunications systems and third-party servicers, and cyber-attacks, systems failures, interruptions or breaches of security could have a material adverse effect on us.

Information technology systems are critical to our business. We use various technology systems to manage our customer relationships, general ledger, securities, deposits, and loans. We have established policies and procedures to prevent or limit the impact of system failures, interruptions, and security breaches (including privacy breaches), but such events may still occur and may not be adequately addressed if they do occur. In addition any compromise of our systems could deter customers from using our products and services. Although we rely on security systems to provide security and authentication necessary to effect the secure transmission of data, these precautions may not protect our systems from compromises or breaches of security.

In addition, we outsource a majority of our data processing to certain third-party providers. If these third-party providers encounter difficulties, or if we have difficulty communicating with them, our ability to adequately process and account for transactions could be affected, and our business operations could be adversely affected. Threats to

information security also exist in the processing of customer information through various other vendors and their personnel.

The occurrence of any system failures, interruption, or breach of security could damage our reputation and result in a loss of customers and business thereby subjecting us to additional regulatory scrutiny, or could expose

us to litigation and possible financial liability. Furthermore, we may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures arising from operational and security risks. Any of these events could have a material adverse effect on our financial condition and results of operations.

The effects of the Tax Cuts and Jobs Act on our business have not yet been fully analyzed and could have an adverse effect on our net income.

On December 22, 2017, the Tax Cuts and Jobs Act (the Tax Act) was signed into law. As a result of the Tax Act, during the first quarter of fiscal 2018, the Company revised its estimated annual effective rate to reflect a change in the federal statutory rate from 34% to 21%. The rate change was administratively effective at the beginning of our fiscal year, using a blended rate for the annual period. As a result, the blended statutory tax rate for the 2018 fiscal year is 24.25%. Net deferred income taxes decreased $3.5 million to $3.2 million at September 30, 2018 compared to $6.7 million at September 30, 2017.

The Company recorded $4.3 million in income tax expense in fiscal 2018 compared to $2.9 million in income tax expense in fiscal 2017. Included in the income tax expense for the current fiscal year is a provisional amount of $2.0 million related to adjusting our deferred tax balance to reflect the new corporate tax rate. The effective tax rates for the Company for the years ended September 30, 2018 and 2017 were 36.9 percent and 33.4 percent, respectively.

Given the significant changes resulting from and complexities associated with the Tax Act, the financial impacts are provisional and subject to further analysis, interpretation and clarification of the Tax Act, which could result in changes to these estimates during fiscal 2019.

Recent New Jersey legislative changes may increase our tax expense.

In connection with adopting the 2019 fiscal year budget, the New Jersey legislature adopted, and the Governor signed, legislation that imposes a temporary surtax on corporations earning New Jersey allocated income in excess of $1 million of 2.5% for tax years beginning on or after January 1, 2018 through December 31, 2019, and of 1.5% for tax years beginning on or after January 1, 2020 through December 31, 2021. The legislation also requires combined filing for members of an affiliated group for tax privilege periods ending on or after July 31, 2019, changing New Jersey s current status as a separate return state, and limits the deductibility of dividends received. These changes are not temporary. Regulations implementing the legislative changes have not yet been issued, and the Company cannot yet fully evaluate the impact of the legislation on overall tax expense or the valuation of the deferred tax asset. It is likely that the Company will lose benefits of various tax management strategies, and as a result, the total tax expense will increase.

Our ability to pay cash dividends is limited, and we may be unable to pay future dividends even if we desire to do so.

We are a legal entity separate and distinct from our banking and other subsidiaries. Our principal source of cash flow, including cash flow to pay dividends to our shareholders if we desire to do so in the future, and to pay the principal of and interest on our outstanding debt, is dividends from the Bank. There are various regulations that limit the Bank s ability to pay dividends to us, and our ability to pay dividends to shareholders. In particular, the prior approval of the FRB and OCC may be required in certain circumstances prior to the payment of dividends by us or the Bank. There can be no assurances that we would receive such approval, if it were required.

In addition, the OCC has the authority to prohibit a national bank from paying dividends if such payment is deemed to be an unsafe or unsound practice. The FRB and the FDIC also have the authority to prohibit or to limit the payment of dividends by a banking organization under its jurisdiction if, in the regulator s opinion, the organization is engaged in or is about to engage in an unsafe or unsound practice. Depending on the financial condition of the Bank, we may be deemed to be engaged in an unsafe or unsound practice if the Bank were to pay dividends.

Payment of dividends could also be subject to regulatory limitations if the Bank became under-capitalized for purposes of the prompt corrective action regulations of the federal bank regulatory agencies.

No assurances can be given that the Bank will, in any particular circumstances, pay dividends to us. If the Bank fails to make dividend payments to us, and sufficient cash or liquidity is not otherwise available, we may not be able to make principal and interest payments on our outstanding debt, or dividend payments on our common stock even if we desire to pay cash dividends in the future.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

At September 30, 2018, the Bank owns and maintains the premises in which the headquarters and six full-service financial centers are located, and leases a financial center in Glen Mills, Pennsylvania and in Villanova, Pennsylvania and private banking offices in Morristown, New Jersey and Palm Beach, Florida. The Bank also leases a representative office in Montchanin, Delaware. The location of each of the offices is as follows:

Paoli Headquarters	42 East Lancaster Avenue, Paoli, PA 19301
Paoli Financial Center	34 East Lancaster Avenue, Paoli, PA 19301
Malvern Financial Center	100 West King Street, Malvern, PA 19355
Coventry Financial Center	1000 Ridge Road, Pottstown, PA 19465
Berwyn Financial Center	650 Lancaster Avenue, Berwyn, PA 19312
Lionville Financial Center	537 West Uwchlan Avenue, Downingtown, PA 19335
Glen Mills Financial Center	940 Baltimore Pike, Glen Mills, PA 19342
Palm Beach Private Banking Office	205 Worth Avenue, Suite 308, Palm Beach, Florida 33480
Villanova Private Banking Office	801 East Lancaster Avenue, Villanova, PA 19085
Morristown Private Banking Office	163 Madison Avenue, 3rd Floor, Morristown, NJ 07960
Montchanin Representative Office	16 W. Rockland Road, Montchanin, Delaware 19710

Item 3. Legal Proceedings.

The Company and its subsidiaries are subject to various legal actions arising in the normal course of business. In the opinion of management, the resolution of these legal actions is not expected to have a material adverse effect on the Company s financial condition or results of operations.

Item 4. Mine Safety Disclosures.

Not Applicable.

PART II.

Item 5. Market for the Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

The common stock of the Company is traded on the NASDAQ Global Select Market under the symbol MLVF . As of September 30, 2018, the Company had 405 stockholders of record, not including the number of persons or entities whose stock is held in nominee or street name through various brokerage firms and banks. On September 28, 2018, the closing sale price was $23.95.

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The following table sets forth the high and low closing sales price of a share of the Company s common stock for the years ended September 30, 2018 and 2017.

	Year Ended September 30,			
	2018		2017	
	High	Low	High	Low
First Quarter	$ 28.20	$ 24.75	$ 21.25	$ 16.36
Second Quarter	$ 26.83	$ 21.00	$ 22.00	$ 19.35
Third Quarter	$ 27.25	$ 23.57	$ 24.60	$ 21.10
Fourth Quarter	$ 25.65	$ 22.78	$ 26.95	$ 22.50

For the years ended September 30, 2018 and 2017, no cash dividends per share of common stock were declared by the Company.

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Stockholders Return Comparison

Set forth below is a line graph presentation comparing the cumulative stockholder return on the Company s common stock, on a dividend reinvested basis, against the cumulative total returns of the Standard & Poor s Composite, the SNL Mid-Atlantic Bank Index and the SNL Mid-Atlantic Thrift Index for the period from October 1, 2013 through September 30, 2018. Effective February 12, 2018, the bank converted from a federal savings bank charter to a national bank charter.

Malvern Bancorp, Inc.

	Period Ending					
Index	**09/30/13**	**09/30/14**	**09/30/15**	**09/30/16**	**09/30/17**	**09/30/18**
Malvern Bancorp, Inc.	100.00	89.40	122.84	128.73	209.97	187.99
S&P 500 Index	100.00	119.73	119.00	137.36	162.92	192.10
SNL Mid-Atlantic U.S. Bank Index	100.00	114.66	117.45	124.02	181.73	198.92
SNL Mid-Atlantic U.S. Thrift Index	100.00	110.63	129.84	130.06	151.39	145.83

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Item 6. Selected Financial Data.

The following tables set forth selected consolidated financial data as of the dates and for the periods presented. The selected consolidated statement of financial condition data as of September 30, 2018 and 2017 and the selected consolidated summary of operating data for the years ended September 30, 2018, 2017 and 2016 have been derived from our audited consolidated financial statements and related notes that we have included elsewhere in this Annual Report. The selected consolidated statement of financial condition data as of September 30, 2016, 2015 and 2014 and the selected consolidated summary of operating data for the years ended September 30, 2015 and 2014 have been derived from audited consolidated financial statements that are not presented in this Annual Report.

The selected historical consolidated financial data as of any date and for any period are not necessarily indicative of the results that may be achieved as of any future date or for any future period. You should read the following selected statistical and financial data in conjunction with the more detailed information contained in Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes that we have presented elsewhere in this Annual Report.

	At September 30,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Summary of Operating Data:					
Total interest and dividend income	$ 40,030	$ 33,782	$ 25,244	$ 20,462	$ 20,167
Total interest expense	12,995	9,446	6,732	5,248	5,071
Net interest income	27,035	24,336	18,512	15,214	15,096
Provision for loan losses	954	2,791	947	90	263
Net interest income after provision for loan losses	26,081	21,545	17,565	15,124	14,833
Total other income	3,304	2,341	2,333	2,535	2,155
Total other expenses	17,803	15,147	13,922	13,961	16,644
Income tax expense (benefit)	4,276	2,922	(6,174)	(970)	(367)
Net income	$ 7,306	$ 5,817	$ 12,150	$ 4,668	$ 711
Earnings per share	$ 1.13	$ 0.90	$ 1.90	$ 0.73	$ 0.11
Statement of Financial Condition Data					
Securities available for sale	$ 24,298	$ 14,587	$ 66,387	$ 128,354	$ 100,943
Securities held to maturity	30,092	34,915	40,551	57,221	
Loans receivable, net	902,136	834,331	574,160	391,307	386,074
Total assets	1,033,951	1,046,012	821,272	655,690	542,264
Deposits	774,163	790,396	602,046	465,522	412,953
FHLB borrowings	118,000	118,000	118,000	103,000	48,000
Other short-term borrowing	2,500	5,000			
Shareholders equity	110,823	102,520	96,157	82,749	77,160
Allowance for loan losses	9,021	8,405	5,434	4,667	4,589
Non-accrual loans in portfolio	2,687	1,038	1,617	1,399	2,391
Non-performing assets in portfolio	3,061	1,211	2,313	2,567	4,355
Performing troubled debt restructurings in portfolio	18,640	2,238	2,039	1,091	1,009

Non-performing assets and performing troubled debt restructurings in portfolio	21,701	3,449	4,352	3,658	5,364

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	At September 30,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Performance Ratios:					
Return on average assets	0.69%	0.62%	1.61%	0.75%	0.12%
Return on average equity	6.88	5.93	14.07	5.79	0.94
Interest rate spread(1)	2.48	2.57	2.53	2.48	2.59
Net interest margin(2)	2.66	2.72	2.65	2.62	2.74
Non-interest expenses to average total assets	1.69	1.62	1.85	2.25	2.84
Efficiency ratio(3)	57.88	56.82	67.22	76.48	96.63
Asset Quality Ratios:					
Non-accrual loans as a percent of gross loans	0.30	0.12	0.28	0.35	0.62
Non-performing assets as a percent of total assets	0.30	0.12	0.28	0.39	0.80
Non-performing assets and performing troubled debt restructurings as a percent of total assets	2.10	0.33	0.53	0.56	0.99
Allowance for loan losses as a percent of gross loans	0.99	1.00	0.94	1.18	1.18
Allowance for loan losses as a percent of non-performing loans	293.65	694.04	234.93	333.60	191.93
Net (recovery) charge-offs to average loans outstanding	0.04	(0.02)	0.04		0.19
Capital Ratios(4):					
Total risk-based capital to risk weighted assets	16.13	15.78	15.42	17.30	20.87
Tier 1 risk-based capital to risk weighted assets	15.09	14.75	14.50	16.21	19.62
Tangible capital to tangible assets	N/A	N/A	N/A	N/A	12.17
Tier 1 leverage (core) capital to adjustable tangible assets	12.71	12.02	10.98	11.01	12.17
Shareholders equity to total assets	10.72	9.80	11.71	12.62	14.23

(1) Represents the difference between the weighted average yield on interest earning assets and the weighted average cost of interest bearing liabilities.

(2) Net interest income divided by average interest earning assets.

(3) Efficiency ratio, which is a non-GAAP financial measure, is computed by dividing other expense, less non-core items, by net interest income on a tax equivalent basis plus other income, excluding net securities gains (losses). Included in non-core items are costs which include expenses related to the Company s corporate restructuring initiatives. The Company believes these adjustments are necessary to provide the most accurate measure of core operating results as a means to evaluate comparative results. See table below for the calculation of the efficiency ratio.

(4) Other than shareholders equity to total assets, all capital ratios are for the Bank only.

The following table presents the calculation of efficiency ratio.

	At September 30,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Other expense	$ 17,803	$ 15,147	$ 13,922	$ 13,961	$ 16,644
Less: non-core items	844	159	111	639	

Other expense, excluding non-core items	16,959	14,988	13,811	13,322	16,644
Net interest income (tax-equivalent basis)	27,183	24,498	18,777	15,400	15,152
Other income, excluding net investment securities gains and gains on sale of real estate (Non-GAAP)	2,118	1,878	1,768	2,020	2,072
Total	29,301	26,376	20,545	17,420	17,224
Efficiency ratio (Non-GAAP)	57.88%	56.82%	67.22%	76.48%	96.63%

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Item 7. Management s Discussion and Analysis (MD&A) of Financial Condition and Results of Operations.

The purpose of this analysis is to provide the reader with information relevant to understanding and assessing the Company s results of operations for each of the past three years and financial condition for each of the past two years. To fully appreciate this analysis, the reader is encouraged to review the consolidated financial statements and accompanying notes thereto appearing under Item 8 of this report, and statistical data presented in this document.

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

See the first page of this Annual Report on Form 10-K for information regarding forward-looking statements.

Critical Accounting Policies and Estimates

Management s Discussion and Analysis of Financial Condition and Results of Operations is based on our consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. Note 2 to our audited consolidated financial statements contains a summary of our significant accounting policies. Management believes our policy with respect to the methodology for the determination of the allowance for loan losses involves more complexity and requires management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could materially impact results of operations. This critical policy and its application are periodically reviewed with the Audit Committee and our Board of Directors.

Allowance for Loan Losses

The allowance for loan losses represents management s estimate of probable loan losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the Company s Consolidated Statements of Financial Condition.

The evaluation of the adequacy of the allowance for loan losses includes, among other factors, an analysis of historical loss rates by loan category applied to current loan totals and qualitative factors. However, actual loan losses may be higher or lower than historical trends, which vary. Actual losses on specified problem loans, which also are provided for in the evaluation, may vary from estimated loss percentages, which are established based upon a limited number of potential loss classifications. The allowance for loan losses is established through a provision for loan losses charged to expense. Management believes that the current allowance for loan losses will be adequate to absorb loan losses on existing loans that may become uncollectible based on the evaluation of known and inherent risks in the loan portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the portfolio, overall portfolio quality, and specific problem loans and current economic conditions which may affect our borrowers ability to pay.

The evaluation also details historical losses by loan category and the resulting loan loss rates which are projected for current loan total amounts. Loss estimates for specified problem loans are also detailed. In addition, OCC, as an integral part of their examination process, periodically review our allowance for loan losses. The OCC may require us to make additional provisions for loan losses based upon information available to them at

the time of their examination. All of the factors considered in the analysis of the adequacy of the allowance for loan losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required that could materially adversely impact earnings in future periods.

Qualitative or environmental factors that may result in further adjustments to the quantitative analyses include items such as changes in lending policies and procedures, economic and business conditions, nature and volume of the portfolio, changes in delinquency, concentration of credit trends, and value of underlying collateral. The total net adjustments due to all qualitative factors increased the allowance for loan losses by approximately $6.2 million and $4.6 million at September 30, 2018 and September 30, 2017, respectively.

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

Other Real Estate Owned

Assets acquired through foreclosure consist of other real estate owned and financial assets acquired from debtors. Other real estate owned is carried at the lower of cost or fair value, less estimated selling costs. The fair value of other real estate owned is determined using current market appraisals obtained from approved independent appraisers, agreements of sale, and comparable market analysis from real estate brokers, where applicable. Changes in the fair value of assets acquired through foreclosure at future reporting dates or at the time of disposition will result in an adjustment in assets acquired through foreclosure expense or net gain (loss) on sale of assets acquired through foreclosure, respectively.

Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets to determine fair value disclosures. Investment and mortgage-backed securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans, real estate owned and certain other assets. These nonrecurring fair value adjustments typically involve application of lower-of-cost-or-market accounting or write-downs of individual assets.

Under the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, Fair Value Measurements, the Company groups its assets at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value. These levels are:

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

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

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

market participants would use in pricing the asset.

Under FASB ASC Topic 820, the Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is our policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements, in accordance with the fair value hierarchy in FASB ASC Topic 820.

Fair value measurements for assets where there exists limited or no observable market data and, therefore, are based primarily upon the Company s or other third-party s estimates, are often calculated based on the characteristics of the asset, the economic and competitive environment and other such factors. Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset. Additionally, there may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, that could significantly affect the results of current or future valuations. At September 30, 2018, the Company had $15.6 million of assets that were measured at fair value on a non-recurring basis using Level 3 measurements.

Income Taxes

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

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

Realization of a deferred tax asset requires us to exercise significant judgment and is inherently uncertain because it requires the prediction of future occurrences. Our net deferred tax asset amounted to $3.2 million and $6.7 million at September 30, 2018 and at September 30, 2017, respectively. As a result of the previously disclosed enactment of the Tax Act, our total deferred tax assets decreased to $3.7 million at September 30, 2018 compared to $7.0 million at September 30, 2017. In accordance with ASC Topic 740, the Company evaluates on a quarterly basis, all evidence, both positive and negative, to determine whether, based on the weight of that evidence, a valuation allowance for DTAs is needed. In conducting this evaluation, management explores all possible sources of taxable income available under existing tax laws to realize the net deferred tax asset beginning with the most objectively verifiable evidence first, including available carry back claims and viable tax planning strategies. If needed, management will look to future taxable income as a potential source. Management reviews the Company s current financial position and its results of operations for the current and preceding years. That historical information is supplemented by all currently available information about future years. The Company understands that projections about future performance are subjective. The Company did not have a DTA valuation allowance as of September 30, 2018 and September 30, 2017.

Due to the improvement in the Company s earnings performance, both on a book (GAAP) and taxable income basis, the Company achieved five consecutive fiscal years of positive book (GAAP) income for the fiscal year ended September 30, 2018.

Other-Than-Temporary Impairment of Securities

Securities are evaluated on a quarterly basis, and more frequently when market conditions warrant such an evaluation, to determine whether declines in their value are other-than-temporary. To determine whether a loss in value is other-than-temporary, management utilizes criteria such as the reasons underlying the decline, the

magnitude and duration of the decline and whether management intends to sell or expects that it is more likely than not that it will be required to sell the security prior to an anticipated recovery of the fair value. The term other-than-temporary is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value for a debt security is determined to be other-than-temporary, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

Derivatives

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

Interest rate swaps are valued by a third party, using models that primarily use market observable inputs, such as yield curves, and are validated by comparison with valuations provided by the respective counterparties. The credit risk associated with derivative financial instruments that are subject to master netting agreements is measured on a net basis by counterparty portfolio. The significant assumptions used in the models, which include assumptions for interest rates, are independently verified against observable market data where possible. Where observable market data is not available, the estimate of fair value becomes more subjective and involves a high degree of judgment. In this circumstance, fair value is estimated based on management s judgment regarding the value that market participants would assign to the asset or liability. This valuation process takes into consideration factors such as market illiquidity. Imprecision in estimating these factors can impact the amount recorded on the balance sheet for an asset or liability with related impacts to earnings or other comprehensive income.

Overview and Strategy

Our business strategy is to operate as a well-capitalized and profitable financial institution dedicated to providing exceptional personal service to our individual and business customers. Highlights of our business strategy are discussed below:

Improving Core Earnings. With interest rates steadily increasing and the FRB signaling additional interest rate hikes, the Bank is focusing on pricing its loan growth at floating rates or rate resets within 5 years. This focus throughout fiscal year-end 2018, partially impacted by higher deposit betas and borrowing costs, have allowed for an expansion in the Banks net interest margin. In an effort to continue consistent sustainable earnings, i.e. improve the net interest margin, we are implementing specific product and pricing strategies designed to increase the yield on loans and control the cost of funding. We are focused on increasing our core deposits, which we define as all deposit accounts other than certificates of deposit. At September 30, 2018, our core deposits amounted to 69.9% of total deposits ($541.2 million), compared to 65.6% of total deposits ($518.6 million) at September 30, 2017. We have continued our promotional efforts to increase core deposits. We review our deposit products on an ongoing basis and

we are considering additional deposit products and are currently offering more flexible delivery options, such as mobile banking, as part of our efforts to increase core

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deposits. We expect to increase our commercial checking and business accounts and we plan to enhance our cross-marketing as part of our efforts to gain additional deposit relationships with our loan customers and private banking clients.

Maintain Low Levels of Problem Assets. We are continuing our efforts to maintain low levels of problem assets. At September 30, 2018, our total non-performing assets in portfolio were $3.1 million or 0.30% of total assets, reflecting a reduction of $1.3 million, or 29.5%, compared to $4.4 million of total non-performing assets at September 30, 2014 (when total non-performing assets amounted to 0.80% of total assets).

Growing Our Loan Portfolio and Resuming Commercial Real Estate and Construction and Development Lending. While commercial real estate loans and construction and development loans were the primary component of the portfolio in fiscal 2018, the Bank is focused on diversification of the mix moving into our fiscal 2019 year. That diversification will include owner occupied, C&I and 1-4 family loans. These loans are being underwritten in accordance with our strengthened loan underwriting standards and our enhanced credit review and administration procedures. With the continued improvements in economic conditions and real estate values, we believe that the continued lending strategy in a planned, deliberative fashion with the loan underwriting and administrative enhancements that we have implemented in recent periods, will increase our interest income and our returns in future periods.

Increasing Market Share Penetration. The Company continued to move forward with momentum in expanding our presence in key markets in fiscal 2018. We continue to execute on our business plans and are positioning the Company to take advantage of the growth activity we are achieving in our markets, which included our new representative office in Montchanin, Delaware. With the recent entry into Florida and Delaware markets, we are working to solidify and expand the service relationship with our new and existing customers. We remain excited by the potential to create incremental shareholder value from our strategic growth. We believe that our earnings performance demonstrates the Company s commitment to achieving meaningful growth, an essential component of providing consistent and favorable long-term returns to our shareholders. However, while we continue to see an improvement in balance sheet strength and core earnings performance, we remain cautious about the credit stability of the broader markets. We operate in a competitive market area for banking products and services. In recent years, we have been working to increase our deposit share in Chester and Delaware counties and we increased our marketing and promotional efforts. In our effort to increase market share as well as non-interest income, we plan to evaluate increasing our business in non-traditional products, such as wealth management and insurance services.

Continuing to Provide Exceptional Customer Service. As a community-oriented bank, we take pride in providing exceptional customer service as a means to attract and retain customers. We deliver personalized service to our customers that distinguish us from the large regional banks operating in our market area. Our management team has strong ties to and deep roots in, the local community. We believe that we know our customers banking needs and can respond quickly to address them.

Introduction

The following sections discuss the Company s Results of Operations, Asset and Liability Management, Liquidity and Capital Resources.

Results of Operations

Net income for the year ended September 30, 2018 was $7.3 million as compared to $5.8 million earned in fiscal 2017 and $12.2 million earned in fiscal 2016. Our net income for fiscal 2018 increased by 25.6 percent compared to fiscal

2017. For fiscal 2018, the fully diluted earnings per common share was $1.13 as compared with $0.90 per share in fiscal 2017 and $1.90 per share in fiscal 2016. Net income prior to income tax expense was $11.6 million for 2018 and $8.7 million for 2017, an increase of $2.8 million or 32.5%.

For the year ended September 30, 2018, the Company s return on average shareholders equity (ROE) was 6.88 percent and its return on average assets (ROA) was 0.69 percent. The comparable ratios for the year ended September 30, 2017 were ROE of 5.93 percent and ROA of 0.62 percent.

Earnings for fiscal 2018 benefitted from an increase in net interest income, as well as an increase in non-interest income. The increase in non-interest income was primarily a result of an increase in service charges and other fees, rental income, and a net gain on the sale of real estate, which were partially offset by a decrease in net gain on sale of investments, earnings on bank owned life insurance and net gain on sale of loans. The increase in non-interest expenses was due to increases in salaries and benefits, occupancy expenses, FDIC insurance, professional fees and other operating expenses. The increase was offset by decreases in advertising expenses, and data processing expense.

Use of Non-GAAP Disclosures

Reported amounts are presented in accordance with U.S. GAAP. The Company s management believes that the supplemental non-GAAP information contained herein, including the efficiency ratio, are utilized by regulators and market analysts to evaluate a company s financial condition and therefore, such information is useful to investors. These disclosures should not be viewed as a substitute for financial results determined in accordance with U.S. GAAP, nor are they necessarily comparable to non-GAAP performance measures which may be presented by other companies.

Net Interest Income and Margin on a Fully Tax-Equivalent Basis, Non-GAAP Financial Measure

Net interest income is the difference between the interest earned on the portfolio of earning assets (principally loans and investments) and the interest paid for deposits and borrowings, which support these assets. Net interest income is presented on a fully tax-equivalent basis, a non-GAAP financial measure, by adjusting tax-exempt income (primarily interest earned on obligations of state and political subdivisions) by the amount of income tax which would have been paid had the assets been invested in taxable issues. We believe this to be the preferred measurement of net interest income as it provides a relevant comparison between taxable and non-taxable amounts.

The following table shows the Company s calculation of Net Interest Income and Margin on a Fully Tax-Equivalent Basis, non-GAAP financial measure.

	Year Ended September 30,		
(Dollars in thousands)	**2018**	**2017**	**2016**
Net interest income	$ 27,035	$ 24,336	$ 18,512
Tax-equivalent adjustment, investment income(1)	55	153	255
Tax-equivalent adjustment, loan interest(1)	93	9	10
Net interest income on a fully tax-equivalent Basis (Non-GAAP)	$ 27,183	$ 24,498	$ 18,777

(1) Computed using a federal income tax rate of 24.25 percent for the year ended September 30, 2018 and 34 percent for the years ended September 30, 2017 and 2016.

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The following table presents the components of net interest income on a fully tax-equivalent basis, a non-GAAP measure, for the periods indicated, together with a reconciliation of net interest income as reported under GAAP.

	Year Ended September 30,								
	2018			2017			2016		
(Dollars in thousands)	Amount	Increase (Decrease) from Prior Year	Percent Change	Amount	Increase (Decrease) from Prior Year	Percent Change	Amount	Increase (Decrease) from Prior Year	Percent Change
Interest income:									
Loans, including fees	$ 36,955	$ 6,105	19.79	$ 30,850	$ 9,634	45.41	$ 21,216	$ 4,724	28.64
Investment securities	1,400	(806)	(36.54)	2,206	(1,624)	(42.40)	3,830	57	1.51
Dividends, restricted stock	467	210	81.71	257	7	2.80	250	(61)	(19.61)
Interest-bearing cash accounts	1,356	725	114.90	631	418	196.24	213	141	195.83
Total interest income	40,178	6,234	18.37	33,944	8,435	33.07	25,509	4,861	23.54
Interest expense:									
Deposits	9,200	2,964	47.53	6,236	1,699	37.45	4,537	1,106	32.24
Short-term borrowings	68	34	100.00	34	34	100.00			
Long-term borrowings	2,200	24	1.10	2,176	(19)	(0.87)	2,195	378	20.80
Subordinated debt	1,527	527	52.70	1,000	1,000	100.00			
Total interest expense	12,995	3,549	37.57	9,446	2,714	40.31	6,732	1,484	28.28
Net interest income on a fully tax-equivalent basis	27,183	2,685	10.96	24,498	5,721	30.47	18,777	3,377	21.93
Tax-equivalent adjustment[1]	(148)	14	8.64	(162)	103	38.87	(265)	(79)	42.47
Net interest income, as reported under GAAP	$ 27,035	$ 2,699	11.09	$ 24,336	$ 5,824	31.46	$ 18,512	$ 3,298	21.68

(1)

Computed using a federal income tax rate of 24.25 percent for the year ended September 30, 2018. Computed using a federal income tax rate of 34 percent for the years ended September 30, 2017 and 2016.

Net interest income is directly affected by changes in the volume and mix of interest-earning assets and interest-bearing liabilities, which support those assets, as well as changes in the rates earned and paid. Net interest income is presented in this financial review on a tax equivalent basis by adjusting tax-exempt income (primarily interest earned on various obligations of state and political subdivisions) by the amount of income tax which would have been paid had the assets been invested in taxable issues, and then in accordance with the Company s consolidated financial statements. Accordingly, the net interest income data presented in this financial review differ from the Company s net interest income components of the Consolidated Financial Statements presented elsewhere in this report.

Net interest income on a fully tax-equivalent basis, a non-GAAP financial measure, for the year ended September 30, 2018 increased $2.7 million, or 11.0 percent, to $27.2 million, from $24.5 million for fiscal 2017. The Company s net interest margin decreased six basis points to 2.66 percent in fiscal 2018 from 2.72 percent for the fiscal year ended September 30, 2017. From fiscal 2016 to fiscal 2017, net interest income on a tax equivalent basis increased by $5.7 million and the net interest margin increased by seven basis points. During fiscal 2018, our net interest margin was impacted by decreases in the yield on investments, as well as an increase in the cost of deposits and borrowings.

The increase in net interest income during fiscal 2018 was attributable in part to the slight increase in short-term interest rates that continued to increase throughout 2018. The Company experienced a slight decrease of

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$444,000 in non-interest bearing deposits during fiscal 2018 and an increase of $14.9 million in interest-bearing demand, savings, money market and time deposits under $100,000 during fiscal 2018. During the twelve months ended September 30, 2018, the Company s net interest spread decreased by nine basis points reflecting a 16 basis points increase in the average yield on interest-earning assets as well as a 25 basis points increase in the average interest rates paid on interest-bearing liabilities.

For the year ended September 30, 2018, average interest-earning assets increased by $121.5 million to $1,022.2 million, as compared with the year ended September 30, 2017. The fiscal 2018 change in average interest-earning asset volume was primarily due to increased loan volume. Average interest-bearing liabilities increased by $108.2 million in fiscal 2018 compared to fiscal 2017, due primarily to an increase in average interest-bearing deposits of $98.8 million and a $9.4 million increase in average borrowings.

For the year ended September 30, 2017, average interest-earning assets increased by $191.3 million to $900.7 million, as compared with the year ended September 30, 2016. The fiscal 2017 change in average interest-earning asset volume was primarily due to increased loan volume. Average interest-bearing liabilities increased by $158.5 million in fiscal 2017 compared to fiscal 2016, due primarily to an increase in average interest-bearing deposits of $137.2 million and a $21.3 million increase in average borrowings.

The factors underlying the year-to-year changes in net interest income on a tax-equivalent basis, a non-GAAP financial measure, are reflected in the tables presented on page 30, each of which have been presented on a tax-equivalent basis (assuming a 24.25 percent tax rate for fiscal 2018, and a 34 percent tax rate for 2017 and 2016). The table on page 32 (Average Statements of Condition with Interest and Average Rates) shows the Company s consolidated average balance of assets, liabilities and shareholders equity, the amount of income produced from interest-earning assets and the amount of expense incurred from interest-bearing liabilities, and net interest income as a percentage of average interest-earning assets.

Net Interest Margin on a Fully Tax-Equivalent Basis, Non-GAAP Financial Measure

The following table quantifies the impact on net interest income on a fully tax-equivalent basis, a non-GAAP financial measure, resulting from changes in average balances and average rates over the past three years. Any change in interest income or expense attributable to both changes in volume and changes in rate has been allocated in proportion to the relationship of the absolute dollar amount of change in each category.

Analysis of Variance in Net Interest Income Due to Volume and Rates

	Fiscal 2018/2017 Increase (Decrease) Due to Change in:			Fiscal 2017/2016 Increase (Decrease) Due to Change in:		
(In thousands)	Average Volume	Average Rate	Net Change	Average Volume	Average Rate	Net Change
Interest-earning assets:						
Loans, including fees	$ 4,914	$ 1,191	$ 6,105	$ 9,628	$ 6	$ 9,634
Investment securities	(403)	(403)	(806)	(1,656)	32	(1,624)
Interest-bearing cash accounts	154	571	725	116	302	418
Dividends, restricted stock	91	119	210	9	(3)	6
Total interest-earning assets	4,756	1,478	6,234	8,097	337	8,434
Interest-bearing liabilities:						
Money market deposits	381	1,137	1,518	599	597	1,196
Savings deposits	1	(2)	(1)	(1)	6	5
Certificates of deposit	(329)	620	291	440	(72)	368
Other interest-bearing deposits	203	953	1,156	20	110	130
Total interest-bearing deposits	256	2,708	2,964	1,058	641	1,699
Borrowings	219	366	585	403	611	1,014
Total interest-bearing liabilities	475	3,074	3,549	1,461	1,252	2,713
Change in net interest income	$ 4,281	$ (1,596)	$ 2,685	$ 6,636	$ (915)	$ 5,721

Interest income on a fully tax-equivalent basis, a non-GAAP financial measure, for the year ended September 30, 2018 increased by approximately $6.2 million or 18.4 percent as compared with the year ended September 30, 2017. This increase was due primarily to increases in the balances of the Company s loans. Interest income on a fully tax-equivalent basis, a non-GAAP financial measure, for the year ended September 30, 2017 increased by approximately $8.4 million or 33.1 percent as compared with the year ended September 30, 2016. This increase was due primarily to increases in the balances of the Company s loans.

The average balance of the Company s loan portfolio increased $117.6 million in fiscal 2018 to $856.1 million from $738.5 million in fiscal 2017, primarily driven by an increase in commercial real estate loans.

The average loan portfolio represented approximately 83.7 percent of the Company s interest-earning assets (on average) during fiscal 2018 and 82.0 percent for fiscal 2017. Average investment securities decreased during fiscal 2018 by $15.5 million compared to fiscal 2017. The average yield on interest-earning assets increased from 3.77 percent in fiscal 2017 to 3.93 percent in fiscal 2018.

Interest expense for the year ended September 30, 2018 was principally impacted by rate related factors. The changes resulted in increased expense of $3.5 million primarily due to an increase in rate paid on interest bearing liabilities and to a lesser degree, the $108.2 million increase in interest -bearing liabilities from fiscal 2017 to fiscal 2018. For the

year ended September 30, 2017, interest expense increased $2.7 million as compared with fiscal 2016, principally reflecting an increase in deposits and borrowings. Average interest-bearing liabilities increased $158.5 million from fiscal 2016 to fiscal 2017.

The Company s net interest spread on a fully tax-equivalent basis, a non-GAAP financial measure, (i.e., the average yield on average interest-earning assets, calculated on a tax equivalent basis, minus the average rate paid on interest-bearing liabilities) decreased nine basis points to 2.48 percent in fiscal 2018 from 2.57 percent for the year ended September 30, 2017. The decrease in fiscal 2018 reflected a spread decrease between yields earned on investments and an increase in overall cost of funds. The net interest spread increased four basis points in fiscal

2017 as compared with fiscal 2016, primarily as a result of an increase of spreads between yields earned on investments and interest-bearing cash accounts and rates paid for supporting funds.

The cost of total average interest-bearing liabilities increased to 1.45 percent, an increase of 25 basis points, for the year ended September 30, 2018, from 1.20 percent for the year ended September 30, 2017, which followed an increase of thirteen basis points from 1.07 percent for the year ended September 30, 2016.

The following table, Average Statements of Condition with Interest and Average Rates , on a tax-equivalent basis presents for the years ended September 30, 2018, 2017 and 2016, the Company s average assets, liabilities and shareholders equity. The Company s net interest income, net interest spreads and net interest income as a percentage of interest-earning assets (net interest margin) are also reflected.

	Year Ended September 30,								
	2018			2017			2016		
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)								
ASSETS									
Interest earning assets:									
Loans receivable(1)	$ 856,066	$ 36,955	4.32%	$ 738,496	$ 30,850	4.18%	$ 507,973	$ 21,216	4.18%
Investment securities	69,485	1,400	2.01	85,030	2,206	2.59	149,812	3,830	2.56
Deposits in other banks	89,304	1,356	1.52	71,754	631	0.88	46,429	213	0.46
FHLB stock	7,359	467	6.35	5,436	257	4.72	5,243	250	4.77
Total interest earning assets(1)	1,022,214	40,178	3.93	900,716	33,944	3.77	709,457	25,509	3.60
Non-interest earning assets									
Cash and due from banks	1,524			1,789			15,585		
Bank owned life insurance	19,173			18,683			18,165		
Other assets	18,668			20,151			14,177		
Allowance for loan losses	(8,629)			(6,930)			(4,968)		
Total non-interest earning assets	30,736			33,693			42,959		

Total assets	$ 1,052,950	$ 934,409	$ 752,416

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	Year Ended September 30,								
	2018			2017			2016		
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)								
LIABILITIES AND SHAREHOLDERS EQUITY									
Interest bearing liabilities:									
Money Market accounts	$ 277,449	$ 3,587	1.29%	$ 234,204	$ 2,069	0.88%	$ 138,997	$ 874	0.63%
Savings accounts	44,357	36	0.08	43,937	37	0.08	45,060	32	0.07
Certificate accounts	247,029	4,152	1.68	270,054	3,861	1.43	239,810	3,492	1.46
Other interest-bearing deposits	181,087	1,425	0.79	102,936	269	0.26	90,054	139	0.15
Total deposits	749,922	9,200	1.23	651,131	6,236	0.96	513,921	4,537	0.88
Borrowed funds	146,245	3,795	2.59	136,885	3,210	2.34	115,598	2,195	1.90
Total interest-bearing liabilities	896,167	12,995	1.45	788,016	9,446	1.20	629,519	6,732	1.07
Non-interest bearing liabilities									
Demand deposits	42,821			40,759			31,263		
Other liabilities	7,723			6,044			5,262		
Total non-interest-bearing liabilities	50,544			46,803			36,525		
Shareholders equity	106,239			99,590			86,372		
Total liabilities and shareholders equity	$ 1,052,950			$ 934,409			$ 752,416		
Net interest income (tax-equivalent basis)		$ 27,183			$ 24,498			$ 18,777	
Net interest spread			2.48%			2.57%			2.53%
Net interest margin			2.66%			2.72%			2.65%
Tax-equivalent adjustment[2]		(148)			(162)			(265)	
Net Interest income		$ 27,035			$ 24,336			$ 18,512	

(1) Includes non-accrual loans during the respective periods. Calculated net of deferred loan fees and loan discounts.
(2) The tax-equivalent adjustment was computed based on a statutory Federal income tax rate of 24.25 percent for fiscal years 2018.The tax-equivalent adjustment was computed based on a statutory Federal income tax rate of 34 percent for fiscal years 2017 and 2016.

Investment Portfolio

For the year ended September 30, 2018, the average volume of investment securities decreased by $15.5 million to approximately $69.5 million or 6.8 percent of average interest-earning assets, from $85.0 million on average, or 9.4 percent of average interest-earning assets, in fiscal 2017. At September 30, 2018, the total investment portfolio amounted to $54.4 million, an increase of $4.9 million from September 30, 2017. The increase in the investment portfolio was primarily due to the purchase of U.S. Treasury notes during the first quarter of fiscal 2018. At September 30, 2018, the principal components of the investment portfolio were government Treasury notes, government agency obligations, federal agency obligations including

mortgage-backed securities, obligations of U.S. states and political subdivision, corporate bonds and notes, and equity securities.

During the year ended September 30, 2018, volume related factors and rate related factors each decreased investment revenue by $403,000. The tax-equivalent yield on investments decreased by 58 basis points to 2.01 percent from a yield of 2.59 percent during the year ended September 30, 2017. The decrease in the investment portfolio was attributed to the sales, amortization, and calls recorded during fiscal 2018. The yield on the portfolio decreased in fiscal 2018 compared to fiscal 2017 due primarily to lower rates earned on taxable securities.

As of September 30, 2018, the estimated fair value of the available-for-sale securities disclosed below was primarily dependent upon the movement in market interest rates, particularly given the negligible inherent credit risk associated with these securities. These investment securities are comprised of securities that are rated investment grade by at least one bond credit rating service. Although the fair value will fluctuate as the market interest rates move, management believes that these fair values will recover as the underlying portfolios mature and are reinvested in market rate yielding investments. As of September 30, 2018, the Company held one U.S. government treasury note, two U.S. government agency securities, seventeen municipal bonds, four corporate securities, thirty-seven mortgage-backed securities, and one single issuer trust preferred security which were in an unrealized loss position. The Company does not intend to sell and expects that it is not more likely than not that it will be required to sell these securities until such time as the value recovers or the securities mature. Management does not believe any individual unrealized loss as of September 30, 2018 represents other-than-temporary impairment.

Securities available-for-sale are a part of the Company s interest rate risk management strategy and may be sold in response to changes in interest rates, changes in prepayment risk, liquidity management and other factors. The Company continues to reposition the investment portfolio as part of an overall corporate-wide strategy to produce reasonable and consistent margins where feasible, while attempting to limit risks inherent in the Company s balance sheet.

For fiscal 2018, no available-for-sale investment securities were sold. For fiscal 2017, proceeds of investment securities sold amounted to approximately $51.1 million. Gross realized gains on investment securities sold amounted to approximately $464,000, while gross realized losses amounted to approximately $1,000, for the period. For fiscal 2016, proceeds of investment securities sold amounted to approximately $62.8 million. Gross realized gains on investment securities sold amounted to approximately $595,000, while gross realized losses amounted to approximately $30,000, for the period.

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

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The table below illustrates the maturity distribution and weighted average yield on a tax-equivalent basis for investment securities at September 30, 2018 on a contractual maturity basis.

	One year or less		More than One Year through Five Years		More than Five Years through Ten Years		More than Ten Years		Total		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
	(Dollars in thousands)										
Available for Sale Securities:											
U.S. treasury notes	$ 9,996	1.61%	$	%	$	%	$	%	$ 9,996	$ 9.986	1.61%
State and municipal obligations	1,004	1.98	4,050	2.49	1,444	2.19	455	3.40	$ 6,953	6,887	2.54
Single issuer trust preferred security					1,000	2.97			1,000	921	2.97
Corporate debt securities			3,105	3.01	3,500	2.77			6,605	6,254	2.89
Mutual fund			250	2.00					250	250	2.00
Total	$ 11,000	1.80%	$ 7,405	2.34%	$ 5,944	2.66%	$ 455	3.40%	$ 24,804	$ 24,298	2.13%
Held to Maturity Securities:											
U.S. government agencies and obligations	$ 1,000	1.21%	$ 999	1.37%	$	%	$	%	$ 1,999	1,979	1.29%
State and municipal obligations					1,863	2.24	6,318	1.49	8,181	8,115	1.66
Corporate debt securities					3,715	3.82			3,715	3,666	3.82
					806	1.86	15,391	1.76	16,197	15,208	1.76

Mortgage-backed securities											
Total	$ 1,000	1.21%	$ 999	1.37%	$ 6,384	2.97%	$ 21,709	1.70%	$ 30,092	$ 28,968	2.41%
Total Investment Securities	$ 12,000	1.59%	$ 8,404	2.21%	$ 12,328	2.89%	$ 22,164	1.80%	$ 54,896	$ 53,266	2.07%

For information regarding the carrying value of the investment portfolio, see Note 5 and Note 11 of the Notes to the Consolidated Financial Statements.

The following table sets forth the carrying value of the Company s investment securities, as of September 30, for each of the last three years.

(In thousands)	**2018**	**2017**	**2016**
Investment Securities Available-for-Sale:			
U.S. treasury notes	$ 9,986	$	$
State and municipal obligations	6,887	7,029	25,307
Single issuer trust preferred security	921	934	878
Corporate debt securities	6,254	6,374	40,202
Mutual Fund	250	250	
Total available-for-sale	$ 24,298	$ 14,587	$ 66,387
Investment Securities Held-to-Maturity:			
U.S. government agencies	$ 1,999	$ 1,999	$ 2,999
State and municipal obligations	8,181	9,574	9,826
Corporate debt securities	3,715	3,818	3,916
Mortgage-backed securities:			
Collateralized mortgage obligations, fixed- rate	16,197	19,524	23,810
Total held-to-maturity	$ 30,092	$ 34,915	$ 40,551
Total investment securities	$ 54,390	$ 49,502	$ 106,938

For information regarding the Company s investment portfolio, see Note 5 and Note 11 of the Notes to the Consolidated Financial Statements.

Loan Portfolio

Lending is one of the Company s primary business activities. The Company s loan portfolio consists of residential, construction and development, commercial and consumer loans, serving the diverse customer base in its market area. The composition of the Company s portfolio continues to change due to the local economy. Factors such as the economic climate, interest rates, real estate values and employment all contribute to these changes. Growth is generated through business development efforts, repeat customer requests for new financings, penetration into existing markets and entry into new markets.

The Company seeks to create growth in commercial lending by offering customer-focused products and competitive pricing and by capitalizing on the positive trends in its market area. Products offered are designed to meet the financial requirements of the Company s customers. It is the objective of the Company s credit policies to diversify the commercial loan portfolio to limit concentrations in any single industry.

At September 30, 2018, total gross loans amounted to $910.6 million, an increase of $68.4 million or 8.1 percent as compared to September 30, 2017. For the year ended September 30, 2018, growth of $77.0 million in commercial loans and $4.7 million in residential mortgage loans were partially offset by decreases of $7.3 million in construction and development loans and $6.0 million in total consumer loans. Even though the Company continues to be challenged by the competition for lending relationships that exists within its market, growth in volume has been achieved through successful lending sales efforts to build on continued customer relationships.

The average balance of our total loans increased $117.6 million or 15.9 percent for the year ended September 30, 2018 as compared to September 30, 2017, while the average yield on loans increased 14 basis points to 4.32% in fiscal 2018 from 4.18% in fiscal 2017. The increase in average total loan volume was due primarily to the volume of new loan originations. During fiscal 2018 compared to fiscal 2017, the volume-related factors during the period contributed to an increase of interest income on loans of $4.9 million, while the rate-related changes increased interest income by $1.2 million.

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The following table presents information regarding the components of the Company s loan portfolio on the dates indicated.

	September 30,				
	2018	2017	2016	2015	2014
	(In thousands)				
Residential mortgage	$ 197,219	$ 192,500	$ 209,186	$ 214,958	$ 231,324
Construction and Development:					
Residential and commercial	37,433	35,622	18,579	5,677	5,964
Land	9,221	18,377	10,013	2,142	1,033
Total construction and development	46,654	53,999	28,592	7,819	6,997
Commercial:					
Commercial real estate	493,929	437,760	231,439	87,686	71,579
Multi-family	45,102	39,768	19,515	7,444	1,032
Farmland	12,066	1,723			
Other	80,059	74,837	38,779	13,380	5,480
Total commercial	631,156	554,088	289,733	108,510	78,091
Consumer:					
Home equity lines of credit	14,884	16,509	19,757	22,919	22,292
Second mortgages	18,363	22,480	29,204	37,633	47,034
Other	2,315	2,570	1,914	2,359	2,839
Total consumer	35,562	41,559	50,875	62,911	72,165
Total loans	910,591	842,146	578,386	394,198	388,577
Deferred loan fees and costs, net	566	590	1,208	1,776	2,086
Allowance for loan losses	(9,021)	(8,405)	(5,434)	(4,667)	(4,589)
Loans receivable, net	$ 902,136	$ 834,331	$ 574,160	$ 391,307	$ 386,074

At September 30, 2018, our net loan portfolio totaled $902.1 million or 87.3% of total assets. Our principal lending activity has been the origination of commercial and commercial real estate loans. Through our loan policy strict underwriting guidelines maintain low average loan-to-value (LTV) ratios, maximum gross debt ratios and minimum debt coverage ratios. We have invested in software which facilitates our ability to internally review and grade loans in our portfolio and to monitor loan performance. Our Credit Department s primary focus has been to review and maintain the loan portfolio, along with the review of underwriting of all new credits.

In prior years, the Company purchased single-family residential mortgage loans and consumer loans from a network of mortgage brokers.

The types of loans that we originate are subject to federal and state law and regulations. Interest rates charged by us on loans are affected principally by the demand for such loans and the supply of money available for lending purposes and the rates offered by our competitors. These factors are, in turn, affected by general and economic conditions, the monetary policy of the federal government, including the Federal Reserve Board, legislative tax policies and

governmental budgetary matters.

The loans receivable portfolio is segmented into residential mortgage loans, construction and development loans, commercial loans and consumer loans. The residential mortgage loan segment has one class, one- to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial construction loans and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built and occupied by the home-owner. Commercial construction loans are made for the purpose of acquiring, developing and constructing a commercial use structure and for acquisition, development and construction of

residential properties by residential developers. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

Residential Lending. Residential mortgage originations are secured primarily by properties located in the Company s primary market area and surrounding areas. At September 30, 2018, $197.2 million, or 21.7%, of our total loans in portfolio consisted of single-family residential mortgage loans. During fiscal 2018, we had $60,000 of charge-offs of residential loans, as compared to zero charge-offs at fiscal 2017.

Our single-family residential mortgage loans generally are underwritten on terms and documentation conforming to guidelines issued by Freddie Mac and Fannie Mae. Applications for one- to four-family residential mortgage loans are taken by our loan origination officers and are accepted at any of our banking offices and are then referred to the lending department at our Morristown office in order to process the loan, which consists primarily of obtaining all documents required by Freddie Mac and Fannie Mae underwriting standards, and completing the underwriting, which includes making a determination whether the loan meets our underwriting standards such that the Bank can extend a loan commitment to the customer. We generally have retained for portfolio a substantial portion of the single-family residential mortgage loans that we originate. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 10 to 30 years. We also offer adjustable rate mortgage (ARM) loans where the interest rate either adjusts on an annual basis or is fixed for the initial one, three, five or seven years and then adjusts annually. However, due to the low interest rate environment and demand for fixed rate products, we have not originated a significant amount of ARM loans in recent years. At September 30, 2018, $57.6 million, or 29.2%, of our one- to four-family residential mortgage loans consisted of ARM loans.

We underwrite one- to four-family residential mortgage loans with loan-to-value ratios of up to 95%, provided that the borrower obtains private mortgage insurance on loans that exceed 80% of the appraised value or sales price, whichever is less, of the secured property. We also require that title insurance, hazard insurance and, if appropriate, flood insurance be maintained on all properties securing real estate loans. We require that a licensed appraiser from our list of approved appraisers perform and submit to us an appraisal on all properties secured by a first mortgage on one- to four-family first mortgage loans. Our mortgage loans generally include due-on-sale clauses which provide us with the contractual right to deem the loan immediately due and payable in the event the borrower transfers ownership of the property. Due-on-sale clauses are an important means of adjusting the yields of fixed-rate mortgage loans in portfolio and we generally exercise our rights under these clauses.

Construction and Development Loans. The amount of our outstanding construction and development loans in portfolio decreased to $46.7 million or 5.1% of gross loans at September 30, 2018 from $54.0 million or 6.4% of total loans as of September 30, 2017. From October 2009 through September 30, 2013, we ceased originating any new construction and development loans, with certain limited exceptions. We generally limit construction loans to builders and developers with whom we have an established relationship, or who are otherwise known to officers of the Bank. Our construction loans also include single-family residential construction loans which may if approved convert to permanent, long-term mortgage loans upon completion of construction (construction/perm loans). During the initial or construction phase, these construction/perm loans require payment of interest only, which generally is tied to prime rate, as the home is being constructed. On residential construction to perm loans the interest rate is as approved. Upon the earlier of the completion of construction or one year, these loans if approved by the appropriate approving authority convert to long-term (generally 30 years), amortizing, fixed-rate single-family mortgage loans.

Our current portfolio of construction loans generally have a maximum term as approved based upon the underwriting (for individual, owner-occupied dwellings), and loan-to-value ratios less than 80%. Residential

construction loans to developers are made on either a pre-sold or speculative (unsold) basis. Limits are placed on the number of units that can be built on a speculative basis based upon the reputation and financial position of the builder, his/her present obligations, the location of the property and prior sales in the development and the surrounding area. Generally, a limit of two unsold homes (one model home and one speculative home) is placed per project.

Prior to committing to a construction loan, we require that an independent appraiser prepare an appraisal of the property. Each project also is reviewed and inspected at its inception and prior to every disbursement of loan proceeds. Disbursements are made after inspections based upon a percentage of project completion and monthly payment of interest is required on all construction loans.

Our construction loans also include loans for the acquisition and development of land for sale (i.e. roads, sewer and water lines). We typically make these loans only in conjunction with a commitment for a construction loan for the units to be built on the site. These loans are secured by a lien on the property and are limited to a loan-to-value ratio not exceeding 75% of the appraised value at the time of origination. The loans have a variable rate of interest and require monthly payments of interest. The principal of the loan is repaid as units are sold and released. We limit loans of this type to our market area and to developers with whom we have established relationships. In most cases, we also obtain personal guarantees from the borrowers.

Our loan portfolio included six loans secured by unimproved real estate and lots (land loan), with an outstanding balance of $9.2 million, constituting 1.0% of total loans, at September 30, 2018.

In order to mitigate some of the risks inherent to construction lending, we inspect properties under construction, review construction progress prior to advancing funds, work with builders with whom we have established relationships, require annual updating of tax returns and other financial data of developers and obtain personal guarantees from the principals. At September 30, 2018, $442,000, or 4.9 percent, of our allowance for loan losses was attributed to construction and development loans. We had no loans in non-performing construction and development loans in portfolio at September 30, 2018 and at September 30, 2017. At September 30, 2018 and 2017, we had $76,000 and $94,000, respectively, in construction and development loans that were performing troubled debt restructurings.

Commercial Lending. At September 30, 2018, our loans in portfolio secured by commercial real estate amounted to $493.9 million and constituted 54.2 percent of our gross loans at such date. During the year ended September 30, 2018, the commercial real estate loan portfolio increased by $56.2 million, or 12.8 percent. During fiscal 2018, we had $276,000 of charge-offs of commercial real estate loans and $45,000 of charge-offs of other commercial loans, as compared to zero charge-offs for fiscal 2017.

Our commercial real estate loan portfolio consists primarily of loans secured by office buildings, retail and industrial use buildings, strip shopping centers, mixed-use and other properties used for commercial purposes located in our market area.

Although terms for commercial real estate and multi-family loans vary, our underwriting standards generally allow for terms up to 10 years with the interest rate being reset in the fifth year and with amortization typically not greater than 25 years and loan-to-value ratios of not more than 80%. Interest rates are either fixed or adjustable, based upon the index rate plus a margin, and fees ranging from 0.5% to 1.50% are charged to the borrower at the origination of the loan. Prepayment fees are charged on most loans in the event of early repayment. Generally, we obtain personal guarantees of the principals as additional collateral for commercial real estate and multi-family real estate loans.

Commercial and multi-family real estate loans generally present a higher level of risk than loans secured by one- to four-family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing

properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced (for example, if leases are not obtained or renewed, a bankruptcy court modifies a lease term, or a major tenant is unable to fulfill its lease obligations), the borrower s ability to repay the loan may be impaired. As of September 30, 2018, we had one non-accruing commercial real estate mortgage loan with an outstanding balance of approximately $520,000 and an aggregate of $18.7 million of our commercial real estate loans at such date were classified for regulatory reporting purposes as substandard. As of September 30, 2018, $4.4 million, or 48.6% of our allowance for loan losses was allocated to commercial real estate mortgage loans. In addition, at September 30, 2018 and 2017, we had no real estate owned which were acquired from foreclosures, or our acceptance of a deed-in-lieu of foreclosure, on commercial real estate loans. As of September 30, 2018, our commercial real estate loans held in portfolio that were deemed performing troubled debt restructurings increased to $16.9 million from $554,000 at September 30, 2017 primarily due to two commercial real estate loans with an aggregate outstanding balance of approximately $16.4 million moving to performing troubled debt restructured (TDR) status in the second fiscal quarter of 2018. In November 2018, one TDR with an aggregate outstanding balance of approximately $7.0 million ceased to perform under modified terms and as a result the Company is in the process of accepting a deed in lieu.

At September 30, 2018, our loan portfolio included 14 loans with an aggregate book value of $45.1 million secured by multi-family (more than four units) properties, constituting 5.0% of our gross loans at such date. As of September 30, 2018, we had no non-accruing multi-family loans.

At September 30, 2018, we had $80.1 million in commercial business loans (8.8% of gross loans outstanding) in portfolio. Our commercial business loans generally have been made to small to mid-sized businesses located in our market area. The commercial business loans in our portfolio assist us in our asset/liability management since they generally provide shorter maturities and/or adjustable rates of interest in addition to generally having higher rates of return which are designed to compensate for the additional credit risk associated with these loans. The commercial business loans which we have originated may be either a revolving line of credit or for a fixed term of generally 10 years or less. Interest rates are adjustable, indexed to a published prime rate of interest, or fixed. Generally, equipment, machinery, real property or other corporate assets secure such loans. Personal guarantees from the business principals are generally obtained as additional collateral.

Generally, commercial business loans (other commercial loans) are characterized as having higher risks associated with them than single-family residential mortgage loans. As of September 30, 2018, we had no non-accruing other commercial loans in our loan portfolio. At such date, $467,000 or 5.2% of the allowance for loan losses was allocated to other commercial loans. At September 30, 2018 and 2017, we held no other commercial loans in portfolio that were deemed performing troubled debt restructurings.

In our underwriting procedures, consideration is given to the stability of the property s cash flow history, future operating projections, current and projected occupancy levels, location and physical condition. Generally, our practice in recent periods is to impose a debt service ratio (the ratio of net cash flows from operations before the payment of debt service to debt service) of not less than 120%. We also evaluate the credit and financial condition of the borrower, and if applicable, the guarantor. Appraisal reports prepared by independent appraisers are obtained on each loan to substantiate the property s market value, and are reviewed by us prior to the closing of the loan.

Consumer Lending. In our efforts to provide a full range of financial services to our customers, we offer various types of consumer loans. Our consumer loans amounted to $35.6 million or 3.9% of our total loan portfolio at September 30, 2018. The largest components of our consumer loans are loans secured by second mortgages, consisting primarily of home equity loans, which amounted to $18.4 million at September 30, 2018, and home equity

lines of credit, which amounted to $14.9 million at such date. Our consumer loans also include automobile loans, unsecured personal loans and loans secured by deposits. Consumer loans are originated primarily through existing and walk-in customers and direct advertising.

Our home equity lines of credit are variable rate loans tied to the prime rate. Our second mortgages may have fixed or variable rates, although they generally have had fixed rates in recent periods. Our second mortgages have a maximum term to maturity of 15 years. Both our second mortgages and our home equity lines of credit generally are secured by the borrower s primary residence. However, our security generally consists of a second lien on the property. Our lending policy provides that the maximum loan-to-value ratio on our home equity lines of credit is 80%, when Malvern Bank has the first mortgage. However, the maximum loan-to-value ratio on our home equity lines of credit is reduced to 75%, when the Bank does not have the first mortgage. At September 30, 2018, the unused portion of our home equity lines of credit was $26.5 million.

Consumer loans generally have higher interest rates and shorter terms than residential loans; however, they have additional credit risk due to the type of collateral securing the loan or in some cases the absence of collateral. In the year ended September 30, 2018, we charged-off $90,000 of consumer loans mostly consisting of second mortgage loans, as compared to $223,000 of charge-offs at fiscal 2017. We are continuing to evaluate and monitor the credit conditions of our consumer loan borrowers and the real estate values of the properties securing our second mortgage loans as part of our on-going efforts to assess the overall credit quality of the portfolio in connection with our review of the allowance for loan losses. As of September 30, 2018, we had an aggregate of $324,000 of non-accruing second mortgage loans and home equity lines of credit, representing an increase of $112,000 over the amount of non-accruing second mortgage loans and home equity lines of credit at September 30, 2017. At September 30, 2018, $1.1 million of our consumer loans were classified as substandard consumer loans. At September 30, 2018, an aggregate of $408,000 of our allowance for loan losses was allocated to second mortgages and home equity lines of credit.

The following table presents the contractual maturity of our loans held in portfolio at September 30, 2018. The table does not include the effect of prepayments or scheduled principal amortization. Loans having no stated repayment schedule or maturity and overdraft loans are reported as being due in one year or less.

	At September 30, 2018, Maturing			
	In One Year or Less	**After One Years Through Five Years**	**After Five Years**	**Total**
	(In thousands)			
Residential mortgage	$ 111	$ 5,905	$ 191,203	$ 197,219
Construction and Development:				
Residential and commercial	33,141	4,292		37,433
Land	6,310	2,463	448	9,221
Total construction and development	39,451	6,755	448	46,654
Commercial:				
Commercial real estate	56,761	77,388	359,780	493,929
Farmland		10,391	1,675	12,066
Multi-family	13,857	13,226	18,019	45,102
Other	33,978	33,293	12,788	80,059
Total commercial	104,596	134,298	392,262	631,156
Consumer:				
Home equity lines of credit			14,884	14,884
Second mortgages	25	3,776	14,562	18,363
Other	35	1,926	354	2,315
Total consumer	60	5,702	29,800	35,562
Total	$ 144,218	$ 152,660	$ 613,713	$ 910,591
Loans with:				
Fixed rates	$ 5,926	$ 24,659	$ 264,886	$ 295,471
Variable rates	138,292	128,001	348,827	615,120
Total	$ 144,218	$ 152,660	$ 613,713	$ 910,591

For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

Allowance for Loan Losses and Related Provision

The purpose of the allowance for loan losses is to absorb the impact of probable losses inherent in the loan portfolio. Additions to the allowance are made through provisions charged against current operations and through recoveries

made on loans previously charged-off. The allowance for loan losses is maintained at an amount considered adequate by management to provide for potential credit losses based upon a periodic evaluation of the risk characteristics of the loan portfolio. In establishing an appropriate allowance, an assessment of the individual borrowers, a determination of the value of the underlying collateral, a review of historical loss experience and an analysis of the levels and trends of loan categories, delinquencies and problem loans are considered. Such qualitative factors as changes in lending policies and procedures, economic and business conditions, nature and volume of the portfolio, changes in delinquency, concentration of credit trends, value of underlying collateral, the level and trend of interest rates, and peer group statistics are also reviewed. At fiscal 2018 year-end, the level of the allowance was $9.0 million as compared to a level of $8.4 million at September 30, 2017. The Company made loan loss provisions of $954,000 in fiscal 2018 compared with $2.8 million in fiscal 2017 and $947,000 in fiscal 2016. The level of the allowance during the respective annual fiscal periods of 2018, 2017 and 2016 reflects the change in average volume, credit quality within the loan portfolio, the level of charge-offs, loan

volume recorded during the periods and the Company s focus on the changing composition of the commercial and residential real estate loan portfolios.

At September 30, 2018, the allowance for loan losses amounted to 0.99 percent of total loans. In management s view, the level of the allowance at September 30, 2018 is adequate to cover losses inherent in the loan portfolio. Management s judgment regarding the adequacy of the allowance constitutes a Forward Looking Statement under the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from management s analysis, based principally upon the factors considered by management in establishing the allowance.

Although management uses the best information available, the level of the allowance for loan losses remains an estimate, which is subject to significant judgment and short-term change. Various regulatory agencies, as an integral part of their examination process, periodically review the Company s allowance for loan losses. Such agencies may require the Company to increase the allowance based on their analysis of information available to them at the time of their examination. Furthermore, the majority of the Company s loans are secured by real estate in the State of Pennsylvania. Future adjustments to the allowance may be necessary due to economic factors impacting Pennsylvania real estate and a further deterioration of the economic climate, as well as, operating, regulatory and other conditions beyond the Company s control. The allowance for loan losses as a percentage of total loans amounted to 0.99 percent, 1.00 percent and 0.94 percent at September 30, 2018, 2017 and 2016, respectively. Provision expense was added throughout the fiscal year commensurate with loan growth.

Net charge-offs were $338,000 in fiscal 2018, compared to net recoveries of $180,000 in fiscal 2017 and net charge-offs of $180,000 in fiscal 2016. During fiscal 2018, the Company experienced an increase in charge-offs and a decrease in recoveries compared to fiscal 2017. Charge-offs were higher in most of the portfolio segments in fiscal 2018 than in fiscal 2017. Charge-offs related to residential mortgage loans, commercial real estate loans, and other commercial loans increased $60,000, $276,000, and $45,000, respectively in fiscal 2018 compared to fiscal 2017.

Five-Year Statistical Allowance for Loan Losses

The following table reflects the relationship of loan volume, the provision and allowance for loan losses and net charge-offs for the past five years.

			September 30,		
	2018	2017	2016	2015	2014
			(Dollars in thousands)		
Average loans outstanding	$ 856,066	$ 738,496	$ 507,973	$ 384,125	$ 407,169
Total loans at end of period	$ 910,591	$ 842,146	$ 578,386	$ 394,198	$ 388,577
Analysis of the Allowance of Loan Losses					
Balance at beginning of year	$ 8,405	$ 5,434	$ 4,667	$ 4,589	$ 5,090
Charge-offs:					
Residential mortgage	60		9		83
Construction and Development:					
Residential and commercial			91	1	37
Commercial:					
Commercial real estate	276		99	48	183
Other	45				
Consumer:					
Home equity lines of credit					14
Second mortgages	88	218	291	138	618
Other	2	5	70	34	6
Total charge-offs	471	223	560	221	941
Recoveries:					
Residential mortgage	58	2	17	17	23
Construction and Development:					
Residential and commercial		90	243	98	1
Commercial:					
Commercial real estate	11	40	3	9	9
Other	4	9	3	3	3
Consumer:					
Home equity lines of credit	1	18	1	2	1
Second mortgages	52	232	100	69	136
Other	7	12	13	11	4
Total recoveries	133	403	380	209	177
Net charge-offs (recoveries)	338	(180)	180	12	764
Provision for loan losses	954	2,791	947	90	263
Balance at end of year	$ 9,021	$ 8,405	$ 5,434	$ 4,667	$ 4,589

Ratio of net charge-offs (recoveries) during the year to average loans outstanding during the year	0.04%	(0.02)%	0.04%	0.00%	0.19%
Allowance for loan losses as a percentage of total loans at end of year	0.99%	1.00%	0.94%	1.18%	1.18%

For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

Implicit in the lending function is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan being made, the creditworthiness of the borrower and prevailing economic conditions.

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The allowance for loan losses has been allocated in the table below according to the estimated amount deemed to be reasonably necessary to provide for the possibility of losses being incurred within the following categories of loans at September 30, for each of the past five years.

The table below shows, for three types of loans, the amounts of the allowance allocable to such loans and the percentage of such loans to total loans.

	September 30,									
	2018		2017		2016		2015		2014	
	Amount	Loans to Total Loans	Amount	Loans to Total Loans	Amount	Loans to Total Loans	Amount	Loans to Total Loans	Amount	Loans to Total Loans
	(Dollars in thousands)									
Residential mortgage	$ 1,062	21.7%	$ 1,004	22.8%	$ 1,201	36.2%	$ 1,486	54.5%	$ 1,672	59.5%
Construction and Development:										
Residential and commercial	393	4.1	523	4.2	199	3.2	30	1.5	291	1.5
Land loans	49	1.0	132	2.2	97	1.7	35	0.5	13	0.3
Commercial:										
Commercial real estate	5,031	54.2	3,581	52.0	1,874	40.0	1,235	22.2	1,248	18.4
Farmland	66	1.3	9	0.2						
Multi-family	232	5.0	224	4.7	109	3.4	104	1.9	29	0.3
Other	467	8.8	541	8.9	158	6.7	108	3.4	50	1.4
Consumer:										
Home equity lines of credit	82	1.6	90	2.0	116	3.4	139	5.8	168	5.8
Second mortgages	326	2.0	402	2.7	467	5.0	761	9.6	1,033	12.1
Other	51	0.3	27	0.3	34	0.4	24	0.6	23	0.7
Total allocated	7,759	100.0	6,533	100.0	4,255	100.0	3,922	100.0	4,527	100.0
Unallocated	1,262		1,872		1,179		745		62	
Balance at end of period	$ 9,021	100.0%	$ 8,405	100.0%	$ 5,434	100.0%	$ 4,667	100.0%	$ 4,589	100.0%

In assessing the adequacy of the ALLL, it is recognized that the process, methodology and underlying assumptions require a significant degree of judgment. The estimation of credit losses is not precise; the range of factors considered is wide and is significantly dependent upon management s judgment, including the outlook and potential changes in the economic environment. At present, components of the commercial loan segments of the portfolio are new originations and the associated volumes continue to see increased growth. At the same time, historical loss levels have decreased as factors in assessing the portfolio. Any unallocated portion of the allowance reflects management s estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions,

delays in obtaining information, including unfavorable information about a borrower s financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors.

Asset Quality

The Company manages asset quality and credit risk by maintaining diversification in its loan portfolio and through review processes that include analysis of credit requests and ongoing examination of outstanding loans and delinquencies, with particular attention to portfolio dynamics and mix. The Company strives to identify loans experiencing difficulty early enough to correct the problems, to record charge-offs promptly based on realistic assessments of current collateral values, and to maintain an adequate allowance for loan losses at all times.

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It is generally the Company s policy to discontinue interest accruals once a loan is past due as to interest or principal payments for a period of ninety days. When a loan is placed on non-accrual status, interest accruals cease and uncollected accrued interest is reversed and charged against current income. Payments received on non-accrual loans are applied against principal. A loan may only be restored to an accruing basis when it again becomes well secured and in the process of collection or all past due amounts have been collected and a satisfactory period of ongoing repayment exists. Accruing loans past due 90 days or more are generally well secured and in the process of collection. For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

Non-Performing and Past Due Loans and OREO

Non-performing loans include non-accrual loans and accruing loans which are contractually past due 90 days or more. Non-accrual loans represent loans on which interest accruals have been suspended. It is the Company s general policy to consider the charge-off of loans at the point they become past due in excess of 90 days, with the exception of loans that are both well-secured and in the process of collection. Troubled debt restructurings represent loans on which a concession was granted to a borrower, such as a reduction in interest rate to a rate lower than the current market rate for new debt with similar risks, and which are currently performing in accordance with the modified terms. For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

The following table sets forth, as of the dates indicated, the amount of the Company s non-accrual loans, accruing loans past due 90 days or more, other real estate owned (OREO) and troubled debt restructurings.

	At September 30,				
	2018	**2017**	**2016**	**2015**	**2014**
	(In thousands)				
Non-accrual loans	$ 2,687	$ 1,038	$ 1,617	$ 1,399	$ 2,391
Accruing loans past due 90 days or more	374	173	696		
Total non-performing loans	3,061	1,211	2,313	1,399	2,391
Other real estate owned				1,168	1,964
Total non-performing assets	$ 3,061	$ 1,211	$ 2,313	$ 2,567	$ 4,355
Troubled debt restructured loans performing	$ 18,640	$ 2,238	$ 2,039	$ 1,091	$ 1,009

At September 30, 2018, non-performing assets totaled $3.1 million, or 0.30% of total assets, as compared with $1.2 million, or 0.12%, at September 30, 2017. The increase in non-performing assets at September 30, 2018 compared to September 30, 2017 was primarily due to the addition of eight residential mortgage loans with an aggregate outstanding balance of approximately $1.3 million, one commercial loan with an outstanding balance of approximately $520,000 and ten consumer loans with an aggregate outstanding balance of approximately $306,000 moving into non-accrual status and a $308,000 increase in residential mortgage loans receivable greater than 90 days and accruing.

TDR loans, totaled $18.9 million and $2.3 million at September 30, 2018 and at September 30, 2017, respectively. A total of $18.6 million and $2.2 million of troubled debt restructured loans were performing pursuant to the terms of their respective modifications at September 30, 2018 and September 30, 2017, respectively. At September 30, 2018, three troubled debt restructured loans with an outstanding balance of approximately $289,000, were deemed

non-performing, while one troubled debt restructured loan with an outstanding balance of approximately $22,000 was deemed non-performing at September 30, 2017. The performing troubled debt restructured loans increased by $16.4 million at September 30, 2018 compared to September 30, 2017 primarily due to two commercial real estate loans with an aggregate outstanding balance of approximately $16.4 million moving to performing TDR status in the second fiscal quarter of 2018. In November 2018, one TDR with an aggregate outstanding balance of approximately $7.0 million ceased to perform under modified terms and as a result the Company is in the process of accepting a deed in lieu.

Total non-performing assets decreased $1.1 million from September 30, 2016 to September 30, 2017. The reduction in non-performing assets from September 30, 2016 was attributable to four loans with an outstanding balance of approximately $435,000 at September 30, 2016 which were returned to accruing status during fiscal 2017, as well as, an aggregate balance of $413,000 of paid-offs loans, principal payments of $180,000, offset in part by the addition of three single residential loans (totaling approximately $318,000) and two consumer loans (totaling approximately $151,000) into non-accrual status.

Other Income

The following table presents the principal categories of non-interest income for each of the years in the three-year period ended September 30, 2018.

	Year Ended September 30,							
	2018	2017	Increase (Decrease)	% Change	2017	2016	Increase (Decrease	% Change
	(Dollars in thousands)							
Service charges and other fees	$ 1,268	$ 992	$ 276	27.82%	$ 992	$ 923	$ 69	7.48%
Rental income-other	268	227	41	18.06	227	211	16	7.58
Net gains on sale of investments		463	(463)	(100.00)	463	565	(102)	(18.05)
Net gains on sale of loans	102	154	(52)	(33.77)	154	116	38	32.76
Net gains on sale of real estate	1,186		1,186	100.00		1	(1)	(100.00)
Earnings on bank-owned life insurance	480	505	(25)	(4.95)	505	517	(12)	(2.32)
Total other income	$ 3,304	$ 2,341	$ 963	41.14%	$ 2,341	$ 2,333	$ 8	0.34%

For the year ended September 30, 2018, total other income increased $963,000 compared to fiscal 2017. This was primarily as a result of a $1.2 million net gain on the sale of the Exton, Pennsylvania branch location, an increase of $276,000 in other fees and service charges and a $41,000 increase in rental income partially offset by a $463,000 decrease in net gains on sales of investment securities, a $52,000 decrease in net gains on sale of loans, and a $25,000 decrease in earnings on bank-owned insurance.

Excluding net investment securities gains and losses and net gains on sale of real estate, a non-GAAP measure, the Company recorded other income of $2.1 million for the twelve months ended September 30, 2018 compared to $1.9 million for the comparable period in fiscal 2017, an increase of $240,000, or 12.8 percent.

For fiscal 2017, total other income increased $8,000 compared to fiscal 2016. This was primarily a result of a $69,000 increase in service charges, a $16,000 increase in rental income, and an increase of $38,000 in net gain on sale of loans, partially offset by a decrease of $102,000 in net gains on sales of investment securities and a decrease in earnings on bank-owned insurance of $12,000.

Excluding net securities gains and losses, a non-GAAP measure, the Company recorded other income of $1.9 million for the twelve months ended September 30, 2017 compared to $1.8 million for the comparable period in fiscal 2016,

an increase of $110,000, or 6.2 percent.

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The Company s other income is presented in the table below excluding net investment security gains and gains on sale of real estate.

	For the Year Ended September 30, 2018	2017	2016
		(In thousands)	
Other income (GAAP basis)	$ 3,304	$ 2,341	$ 2,333
Less: Net investment securities gains and gains on sale of real estate	1,186	463	565
Other income, excluding net investment securities gains and gains on sale of real estate (Non-GAAP)	$ 2,118	$ 1,878	$ 1,768

Other Expense

The following table presents the principal categories of other expense for each of the years in the three-year period ended September 30, 2018.

	Year Ended September 30,							
	2018	2017	Increase (Decrease)	% Change	2017	2016	Increase (Decrease)	% Change
	(Dollars in thousands)							
Salaries and employee benefits	$ 8,193	$ 7,114	$ 1,079	15.17%	$ 7,114	$ 6,290	$ 824	13.10%
Occupancy expense	2,295	2,084	211	10.12	2,084	1,820	264	14.51
Federal deposit insurance premium	298	244	54	22.13	244	579	(335)	(57.86)
Advertising	152	216	(64)	(29.63)	216	131	85	64.89
Data processing	1,098	1,195	(97)	(8.12)	1,195	1,128	67	5.94
Professional fees	2,891	1,894	997	52.64	1,894	1,683	211	12.54
Other operating expense	2,876	2,400	476	19.83	2,400	2,291	109	4.76
Total other expense	$ 17,803	$ 15,147	$ 2,656	17.53%	$ 15,147	$ 13,922	$ 1,225	8.80%

Total other expense increased $2.7 million, or 17.5 percent, in fiscal 2018 from fiscal 2017 as compared with an increase of $1.2 million, or 8.8 percent, from fiscal 2016 to fiscal 2017. The increase from fiscal 2017 to fiscal 2018 was primarily reflected increases in salaries and employee benefits of $1.1 million, a $997,000 increase in professional fees, a $476,000 increase in other operating expense, a $211,000 increase in occupancy expense, and a $54,000 increase in the federal deposit insurance premium. The increase was partially offset by a $97,000 decrease in data processing expense and a $64,000 decrease in advertising expense.

Prudent management of operating expenses has been and will continue to be a key objective of management in an effort to improve earnings performance. The Company s ratio of other expenses to average assets increased slightly to 1.69 percent in fiscal 2018 compared to 1.62 percent in fiscal 2017 and was 1.85 percent in fiscal 2016.

Salaries and employee benefits increased $1.1 million or 15.2 percent in fiscal 2018 compared to fiscal 2017 and increased $824,000 or 13.1 percent from fiscal 2016 to fiscal 2017. The increase in salaries and employee benefits during fiscal 2018 primarily reflects higher compensation to officers and employees to support overall franchise growth. Salaries and employee benefits accounted for 46.0 percent of total non-interest expense in fiscal 2018, as compared to 47.0 percent and 45.2 percent in fiscal 2017 and fiscal 2016, respectively.

Occupancy expense for fiscal 2018 increased by $211,000 or 10.1 percent, over fiscal 2017. Occupancy expense for fiscal 2017 increased by $264,000 or 14.5 percent, compared to fiscal 2016. The increase in occupancy expense during fiscal 2018 was primarily due to an increase in rent expense of $141,000, a $61,000 increase in depreciation expense, and a $16,000 increase in building and equipment maintenance expense.

Federal deposit insurance premium for fiscal 2018 increased $54,000, or 22.1 percent, compared to fiscal 2017. The increase in the federal deposit insurance premium is due to adjustments in fiscal 2018 as a result of the new regulatory calculation in fiscal 2017. For the year ended September 30, 2017, FDIC insurance expense decreased $335,000 compared to fiscal 2016. The decrease in the federal deposit insurance premium for fiscal 2017 is due to the new regulatory calculation.

Advertising expense for fiscal 2018 decreased $64,000, or 29.6 percent, compared to fiscal 2017. The decrease for fiscal 2018 is due to decrease in advertising retainers. For fiscal 2017, these expenses increased $85,000, or 64.9 percent compared to fiscal 2016.

Data processing expense for fiscal 2018 decreased $97,000, or 8.1 percent, compared to fiscal 2017. For fiscal 2017, data processing expense increased $67,000, or 5.9 percent, over fiscal 2016.

Professional fees for fiscal 2018 increased $997,000, or 52.6 percent, compared to fiscal 2017. Professional fees reflect increased legal and accounting fees for the period related to prior period restatements, which the Company does not expect to continue into future periods. The increase is due to a $720,000 increase in legal fees, a $227,000 increase in fees associated with audit and accounting services, a $45,000 increase in fees associated with other professional services, and an increase of $5,000 in fees associated with payroll services. Professional fees increased $211,000 in fiscal 2017 from fiscal 2016 primarily due to a $130,000 increase in legal fees and a $132,000 increase in fees associated with professional services. The increase was offset by $53,000 reduction in fees associated with audit and accounting services.

Other operating expense increased in fiscal 2018 by approximately $476,000, or 19.8 percent, compared to fiscal 2017. The increase during the year ended September 30, 2018 was primarily due to a $118,000 increase in subordinated debt amortization costs, a $40,000 increase in business expenses related to personnel agency fees, a $39,000 increase in expenses associated with the OCC assessment, and a $172,000 decrease in other real estate owned credits. Other operating expense increased in fiscal 2017 by approximately $109,000, or 4.8 percent, compared to fiscal 2016. The increase during the year ended September 30, 2017 was primarily due to a $41,000 increase in business expenses related to entertainment and meals and auto expense, and a $37,000 increase in expenses associated with annual credit review such as appraisals.

Provision for Income Taxes

The Company recorded $4.3 million in income tax expense in fiscal 2018, compared to $2.9 million in income tax expense in fiscal 2017 and $6.2 million in income tax benefit in fiscal 2016, respectively. The effective tax rates for the Company for the years ended September 30, 2018, 2017 and 2016 were 36.9 percent, 33.4 percent and (103.3) percent, respectively. For a more detailed description of income taxes see Note 12 of the Notes to Consolidated Financial Statements.

In the first quarter of fiscal 2018, the Company revised its estimated annual effective rate to reflect a change in the federal statutory rate from 34% to 21%, resulting from the Tax Cuts and Jobs Act that was enacted on December 22, 2017. The rate change was administratively effective at the beginning of our fiscal year, using a blended rate for the annual period. As a result, the blended statutory tax rate for the fiscal year is 24.25%. Net deferred income taxes decreased $3.5 million to $3.2 million at September 30, 2018 compared to $6.7 million at September 30, 2017.

In addition, we recognized a tax expense in our tax provision for the quarter ended December 31, 2017 related to adjusting our deferred tax balance to reflect the new corporate tax rate. As a result, income tax expense reported for the first three months was adjusted to reflect the effects of the change in the tax law and resulted in an increase in

income tax expense of $2.0 million during the quarter ended December 31, 2017. This amount is the result of a reduction of $323,000 in income tax expense for the three-month period ended December 31, 2017 related to the lower corporate rate and a $2.3 million increase from the application of the newly enacted rates to existing deferred tax assets balances.

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Recent Accounting Pronouncements

Please refer to the note on Recent Accounting Pronouncements in Note 2 to the consolidated financial statements in Item 8 for a detailed discussion of new accounting pronouncements.

Asset and Liability Management

Asset and Liability management encompasses an analysis of market risk, the control of interest rate risk (interest sensitivity management) and the ongoing maintenance and planning of liquidity and capital. The composition of the Company s statement of condition is planned and monitored by the Asset and Liability Committee (ALCO). In general, management s objective is to optimize net interest income and minimize market risk and interest rate risk by monitoring the components of the statement of condition and the interaction of interest rates.

Short-term interest rate exposure analysis is supplemented with an interest sensitivity gap model. The Company utilizes interest sensitivity analysis to measure the responsiveness of net interest income to changes in interest rate levels. Interest rate risk arises when an earning asset matures or when its interest rate changes in a time period different than that of a supporting interest-bearing liability, or when an interest-bearing liability matures or when its interest rate changes in a time period different than that of an earning asset that it supports. While the Company matches only a small portion of specific assets and liabilities, total earning assets and interest-bearing liabilities are grouped to determine the overall interest rate risk within a number of specific time frames. The difference between interest-sensitive assets and interest-sensitive liabilities is referred to as the interest sensitivity gap. At any given point in time, the Company may be in an asset-sensitive position, whereby its interest-sensitive assets exceed its interest-sensitive liabilities, or in a liability-sensitive position, whereby its interest-sensitive liabilities exceed its interest-sensitive assets, depending in part on management s judgment as to projected interest rate trends.

The Company s interest rate sensitivity position in each time frame may be expressed as assets less liabilities, as liabilities less assets, or as the ratio between rate sensitive assets (RSA) and rate sensitive liabilities (RSL). For example, a short-funded position (liabilities repricing before assets) would be expressed as a net negative position, when period gaps are computed by subtracting repricing liabilities from repricing assets. When using the ratio method, a RSA/RSL ratio of 1 indicates a balanced position, a ratio greater than 1 indicates an asset-sensitive position and a ratio less than 1 indicates a liability-sensitive position.

A negative gap and/or a rate sensitivity ratio less than 1 tends to expand net interest margins in a falling rate environment and reduce net interest margins in a rising rate environment. Conversely, when a positive gap occurs, generally margins expand in a rising rate environment and contract in a falling rate environment. From time to time, the Company may elect to deliberately mismatch liabilities and assets in a strategic gap position.

At September 30, 2018, the Company reflected a negative interest sensitivity gap with an interest sensitivity ratio of 0.91:1.00 at the cumulative one-year position. Based on management s perception of interest rates remaining low through 2018, emphasis has been, and is expected to continue to be, placed on controlling liability costs while extending the maturities of liabilities in our efforts to insulate the net interest spread from rising interest rates in the future. However, no assurance can be given that this objective will be met.

The following table sets forth the amounts of our interest-earning assets and interest-bearing liabilities outstanding at September 30, 2018, which we expect, based upon certain assumptions, to reprice or mature in each of the future time periods shown (the GAP Table). Except as stated below, the amount of assets and liabilities shown which reprice or mature during a particular period were determined in accordance with the earlier of term to repricing or the contractual maturity of the asset or liability. The table sets forth approximation of the projected repricing of assets and liabilities

at September 30, 2018, on the basis of contractual maturities, anticipated prepayments, and scheduled rate adjustments within a three-month period and subsequent selected

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time intervals. The loan amounts in the table reflect principal balances expected to be redeployed and/or repriced as a result of contractual amortization and anticipated prepayments of adjustable-rate loans and fixed-rate loans, and as a result of contractual rate adjustments on adjustable-rate loans.

	6 Months or Less	More than 6 Months to 1 Year	More than 1 Year to 3 Years	More than 3 Year to 5 Years	More than 5 Years	Total Amount
			(Dollars in thousands)			
Interest-earning assets[(1)]:						
Loans receivable[(2)]	$ 268,573	$ 44,853	$ 221,268	$ 198,266	$ 174,565	$ 907,525
Investment securities and restricted securities	18,278	5,751	10,217	9,438	19,732	63,416
Other interest-earning assets	29,271					29,271
Total interest-earning assets	316,122	50,604	231,485	207,704	194,297	1,000,212
Interest-bearing liabilities:						
Demand and NOW accounts	8,932	8,932	35,728	35,728	116,472	205,792
Money market accounts	25,172	25,172	100,689	96,670	924	248,627
Savings accounts	1,938	1,938	7,752	7,752	25,271	44,651
Certificate accounts	71,004	39,871	93,933	11,064	17,063	232,935
FHLB advances	87,500	5,000	28,000	25,000		145,500
Total interest-bearing liabilities	194,546	80,913	266,102	176,214	159,730	877,505
Interest-earning assets less interest-bearing liabilities	$ 121,576	$ (30,309)	$ (34,617)	$ 31,490	$ 34,567	$ 122,707
Cumulative interest-rate sensitivity gap[(3)]	$ 121,576	$ 91,267	$ 56,650	$ 88,140	$ 122,707	
Cumulative interest-rate gap as a percentage of total assets at September 30, 2018	11.76%	8.83%	5.48%	8.52%	11.87%	
Cumulative interest-earning assets as a percentage of cumulative interest-bearing liabilities at September 30, 2018	162.49%	133.13%	110.46%	112.28%	113.98%	

(1) Interest-earning assets are included in the period in which the balances are expected to be redeployed and /or repriced as a result of anticipated prepayments, scheduled rate adjustments and contractual maturities.
(2) For purposes of the gap analysis, loans receivable includes non-performing loans gross of the allowance for loan losses, undisbursed loan funds, unamortized discounts and deferred loans fees.
(3) Interest-rate sensitivity gap represents the net cumulative difference between interest-earning assets and interest-bearing liabilities.

Net Portfolio Value and Net Interest Income Analysis. Our interest rate sensitivity also is monitored by management through the use of models which generate estimates of the change in its net portfolio value (NPV) and net interest income (NII) over a range of interest rate scenarios. NPV is the present value of expected cash flows from assets, liabilities, and off-balance sheet contracts. The NPV ratio, under any interest rate scenario, is defined as the NPV in that scenario divided by the market value of assets in the same scenario.

The table below sets forth as of September 30, 2018 and 2017, the estimated changes in our net portfolio value that would result from designated instantaneous changes in the United States Treasury yield curve.

Computations of prospective effects of hypothetical interest rates changes are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

	As of September 30, 2018			As of September 30, 2017		
Changes in Interest Rates (basis points)[1]	Amount	Dollar Change from Base	Percentage Change from Base	Amount	Dollar Change from Base	Percentage Change from Base
			(Dollars in thousands)			
+300	$124,186	$(25,162)	(17)%	$110,780	$(20,923)	(16)%
+200	133,197	(16,151)	(11)	119,631	(12,072)	(9)
+100	142,132	(7,216)	(5)	127,334	(4,369)	(3)
0	149,348			131,703		
-100	152,538	3,190	2	134,634	2,931	2

(1) Assumes an instantaneous uniform change in interest rates. A basis point equals 0.01%.

In addition to modeling changes in NPV, we also analyze potential changes to NII for a twelve-month period under rising and falling interest rate scenarios. The following table shows our NII model as of September 30, 2018.

Changes in Interest Rates in Basis Points (Rate Shock)	Net Interest Income	$ Change	% Change
	(Dollars in thousands)		
200	$ 28,187	$ 1,588	5.97%
100	27,437	838	3.15
Static	26,599		
(100)	25,812	(787)	(2.96)

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

Estimates of Fair Value

The estimation of fair value is significant to a number of the Company s assets, including investment securities available-for-sale. These are all recorded at either fair value or the lower of cost or fair value. Fair values are volatile and may be influenced by a number of factors. Circumstances that could cause estimates of the fair value of certain

assets and liabilities to change include a change in prepayment speeds, discount rates, or market interest rates. Fair values for most available-for-sale investment securities are based on quoted market prices. If quoted market prices are not available, fair values are based on judgments regarding future expected loss experience, current economic condition risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Impact of Inflation and Changing Prices

The financial statements and notes thereto presented elsewhere herein have been prepared in accordance with generally accepted accounting principles, which require the measurement of financial position and operating

results in terms of historical dollars without considering the change in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of operations; unlike most industrial companies, nearly all of the Company s assets and liabilities are monetary. As a result, interest rates have a greater impact on performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

Liquidity

The liquidity position of the Company is dependent primarily on successful management of the Bank s assets and liabilities so as to meet the needs of both deposit and credit customers. Liquidity needs arise principally to accommodate possible deposit outflows and to meet customers requests for loans. Scheduled principal loan repayments, maturing investments, short-term liquid assets and deposit inflows, can satisfy such needs. The objective of liquidity management is to enable the Company to maintain sufficient liquidity to meet its obligations in a timely and cost-effective manner.

Management monitors current and projected cash flows, and adjusts positions as necessary to maintain adequate levels of liquidity. Under its liquidity risk management program, the Company regularly monitors correspondent bank funding exposure and credit exposure in accordance with guidelines issued by the banking regulatory authorities. Management uses a variety of potential funding sources and staggering maturities to reduce the risk of potential funding pressure. Management also maintains a detailed contingency funding plan designed to respond adequately to situations which could lead to stresses on liquidity. Management believes that the Company has the funding capacity to meet the liquidity needs arising from potential events. The Company maintains borrowing capacity through the Federal Home Loan Bank of Pittsburgh secured with loans and marketable securities.

The Company s primary sources of short-term liquidity consist of cash and cash equivalents and investment securities available-for-sale.

At September 30, 2018, the Company had $30.8 million in cash and cash equivalents compared to $117.1 million at September 30, 2017. In addition, our investment securities available-for-sale amounted to $24.3 million at September 30, 2018 and $14.6 million at September 30, 2017.

Deposits

Total deposits decreased to $774.2 million at September 30, 2018 from $790.4 million at September 30, 2017. Total interest-bearing deposits decreased from $748.3 million at September 30, 2017 to $732.5 million at September 30, 2018, a decrease of $15.8 million or 21.1 percent. Interest-bearing demand, savings, money market and time deposits under $100,000 increased $14.9 million to a total of $572.6 million at September 30, 2018 as compared to $557.7 million at September 30, 2017. Time deposits $100,000 and over decreased $30.7 million at September 30, 2018 as compared to September 30, 2017. Time deposits $100,000 and over represented 20.7 percent of total deposits at September 30, 2018 compared to 24.1 percent at September 30, 2017. We had brokered deposits totaling $88.3 million at September 30, 2018 compared to $103.7 million at September 30, 2017.

The Company derives a significant proportion of its liquidity from its core deposit base. Total demand deposits, savings and money market accounts of $541.2 million at September 30, 2018 increased by $22.6 million, or 4.4 percent, from September 30, 2017. Total demand deposits, savings and money market accounts were 69.9 percent of total deposits at September 30, 2018 and 65.6 percent at September 30, 2017. Alternatively, the Company uses a more stringent calculation for the management of its liquidity positions internally, which calculation consists of total demand, savings accounts and money market accounts (excluding money market accounts and certificates of deposit

greater than $100,000) as a percentage of total deposits. This number increased by $19.1 million, or 5.7 percent, from $337.7 million at September 30, 2017 to $356.8 million

at September 30, 2018 and represented 46.1 percent of total deposits at September 30, 2018 as compared with 42.7 percent at September 30, 2017.

The Company continues to place the main focus of its deposit gathering efforts in the maintenance, development, and expansion of its core deposit base. Management believes that the emphasis on serving the needs of our communities will provide a long-term relationship base that will allow the Company to efficiently compete for business in its market. The success of this strategy is reflected in the growth of the demand, savings and money market balances during fiscal 2018.

The following table depicts the Company s core deposit mix at September 30, 2018 and 2017 based on the Company s alternative calculation:

	September 30,				
	2018		2017		Net Change
	Amount	Percentage	Amount	Percentage	2018 vs. 2017
	(Dollars in thousands)				
Non interest-bearing demand	$ 41,677	11.7%	$ 42,121	12.5%	$ (444)
Interest-bearing demand	184,073	51.6	155,579	46.1	28,494
Savings	44,642	12.5	44,526	13.2	116
Money market deposits under $100,000	13,374	3.7	14,299	4.2	(925)
Certificates of deposit under $100,000	73,013	20.5	81,166	24.0	(8,153)
Total core deposits	$ 356,779	100.0%	$ 337,691	100.0%	$ 19,088
Total deposits	$ 774,163		$ 790,396		$ (16,233)
Core deposits to total deposits		46.1%		42.7%	

At September 30, 2018, our certificates of deposit and other time deposits with a balance of $100,000 or more amounted to $159.9 million, of which $86.8 million are scheduled to mature within twelve months. At September 30, 2018, the weighted average remaining maturity of our certificate of deposit accounts was 19.4 months. The following table presents the maturity of our certificates of deposit and other time deposits with balances of $100,000 or more.

	Amount
	(In thousands)
Maturity Period:	
Three months or less	$ 29,563
Over three months through six months	26,653
Over six months through twelve months	30,605
Over twelve months	73,102
Total	$ 159,923

Borrowings

Borrowings from the FHLB of Pittsburgh are available to supplement the Company s liquidity position and, to the extent that maturing deposits do not remain with the Company, management may replace such funds with advances. As of September 30, 2018 and 2017, the Company s outstanding balance of FHLB advance, totaled $118.0 million. Of the $118.0 million in advances, $28.0 million represents long-term, fixed-rate advances maturing in 2020 that have terms enabling the FHLB to call the borrowing at their option prior to maturity. The remaining balance of long-term, fixed rate advances totaled $55.0 million, representing five separate advances maturing during fiscal year 2019. At September 30, 2018, there were two short-term FHLB advances totaling $35.0 million of fixed-rate borrowing with rollover of 90 days.

During fiscal 2018 the Company had purchased securities sold under agreements to repurchase as a short-term funding source. At September 30, 2018, the Company had $2.5 million in securities sold under agreements to repurchase at a rate of 2.5%. At September 30, 2017, the Company had $5.0 million in securities sold under agreements to repurchase at a rate of 1.46%. The Company had no securities sold under agreements to repurchase at September 30, 2016.

Cash Flows

The Consolidated Statements of Cash Flows present the changes in cash and cash equivalents resulting from the Company s operating, investing and financing activities. During the year ended September 30, 2018, cash and cash equivalents decreased by $86.3 million over the balance at September 30, 2017. Net cash of $9.1 million was provided by operating activities in fiscal 2018 compared to net cash of $9.8 million provided by operating activities in fiscal 2017. Net cash used in investing activities amounted to approximately $76.4 million in fiscal 2018 compared to net cash used in investing activities of approximately $207.0 million in fiscal 2017. Net cash of $19.0 million was used in financing activities in fiscal 2018 compared to net cash of $217.5 million provided by financing activities in fiscal 2017.

Payments Due Under Contractual Obligations

The following table presents information relating to the Company s payments due under contractual obligations as of September 30, 2018.

	Payments Due by Period				
	Less than One Year	One to Three Years	Three to Five Years	More than Five Years	Total
			(In thousands)		
Long-term debt obligations[1]	$ 35,070	$ 84,400	$	$	$ 119,470
Certificates of deposit[1]	112,878	95,791	11,286	17,420	237,375
Operating lease obligations	514	966	950	1,285	3,715
Total contractual obligations	$ 148,462	$ 181,157	$ 12,236	$ 18,705	$ 360,560

(1) Includes interest payments.

Off-Balance Sheet Arrangements

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with U.S. GAAP, are not recorded in its financial statements. These transactions involve, to varying degrees, elements of credit, interest rate, and liquidity risk. Such transactions are used primarily to manage customers requests for funding and take the form of loan commitments, lines of credit and letters of credit.

The contractual amounts of commitments to extend credit represent the amounts of potential accounting loss should the contract be fully drawn upon, the customer defaults and the value of any existing collateral becomes worthless. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments. Financial instruments whose contract amounts represent credit risk at September 30, 2018 and 2017 were as follows:

	September 30,	
	2018	2017
	(In thousands)	
Commitments to extend credit:[1]		
Future loan commitments	$ 52,390	$ 80,273
Undisbursed construction loans	25,128	37,064
Undisbursed home equity lines of credit	26,498	26,440
Undisbursed Commercial lines of credit	71,391	55,346
Overdraft protection lines	1,312	1,339
Standby letters of credit	7,122	4,650
Total commitments	$ 183,841	$ 205,112

(1) Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments may require payment of a fee and generally have fixed expiration dates or other termination clauses.

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

Shareholders Equity

Total shareholders equity amounted to $110.8 million, or 10.7 percent of total assets, at September 30, 2018, compared to $102.5 million, or 9.8 percent of total assets at September 30, 2017. Book value per common share was $16.84 at September 30, 2018, compared to $15.60 at September 30, 2017.

Capital

At September 30, 2018, the Bank s common equity tier 1 ratio was 15.09 percent, tier 1 leverage ratio was 12.71 percent, tier 1 risk-based capital ratio was 15.09 percent and the total risk-based capital ratio was 16.13 percent. At September 30, 2017, the Bank s common equity tier 1 ratio was 14.75 percent, tier 1 leverage ratio was 12.02 percent, tier 1 risk-based capital ratio was 14.75 percent and the total risk-based capital ratio was 15.78 percent. At September 30, 2018, the Bank was in compliance with all applicable regulatory capital requirements.

At September 30, 2018, the Company s common equity tier 1 ratio was 12.62 percent, tier 1 leverage ratio was 10.63 percent, tier 1 risk-based capital ratio was 12.62 percent and the total risk-based capital ratio was 16.45 percent. At September 30, 2017, the Company s common equity tier 1 ratio was 12.28 percent, tier 1 leverage ratio was 10.00 percent, tier 1 risk-based capital ratio was 12.28 percent and the total risk-based capital ratio was 16.27 percent. At September 30, 2018, the Bank was in compliance with all applicable regulatory capital requirements.

Looking Forward

As previously disclosed in the Company s Form 8-K filed on October 9, 2018, the Company closed an underwritten public offering of shares of our common stock for gross proceeds of $25.0 million and net proceeds of approximately $23.4 million (after deducting the underwriting discount and other estimated offering expenses).

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One of the Company s primary objectives is to achieve balanced asset and revenue growth, and at the same time expand market presence and diversify its financial products. However, it is recognized that objectives, no matter how focused, are subject to factors beyond the control of the Company, which can impede its ability to achieve these goals. The following factors should be considered when evaluating the Company s ability to achieve its objectives:

The financial market place is rapidly changing. Banks are no longer the only place to obtain loans, nor the only place to keep financial assets. The banking industry has lost market share to other financial service providers. The future is predicated on the Company s ability to adapt its products, provide superior customer service and compete in an ever-changing marketplace. Net interest income, the primary source of earnings, is impacted favorably or unfavorably by changes in interest rates. Although the impact of interest rate fluctuations is mitigated by ALCO strategies, significant changes in interest rates can have a material adverse impact on profitability.

The ability of customers to repay their obligations is often impacted by changes in the regional and local economy. Although the Company sets aside loan loss provisions toward the allowance for loan losses when management determines such action to be appropriate, significant unfavorable changes in the economy could impact the assumptions used in the determination of the adequacy of the allowance.

Technological changes will have a material impact on how financial service companies compete for and deliver services. It is recognized that these changes will have a direct impact on how the marketplace is approached and ultimately on profitability. The Company has taken steps to improve its traditional delivery channels. However, continued success will likely be measured by the Company s ability to anticipate and react to future technological changes.

This Looking Forward discussion constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from those projected in the Company s forward-looking statements due to numerous known and unknown risks and uncertainties, including the factors referred to above, on the first page of this Annual Report on Form 10-K and in other sections of this Annual Report on Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

The information contained in the section captioned Management s Discussion and Analysis of Financial Condition and Results of Operations Asset and Liability Management in Item 7 hereof is incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders

Malvern Bancorp, Inc. and Subsidiaries

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated statement of financial condition of Malvern Bancorp, Inc. and Subsidiaries (the Company) as of September 30, 2018, and the related consolidated statements of operations, comprehensive income, changes in shareholders equity, and cash flows, for the year then ended, and the related notes (collectively referred to as the consolidated financial statements). We also have audited the Company s internal control over financial reporting as of September 30, 2018, based on criteria established in *Internal Control Integrated Framework: (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of September 30, 2018, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2018, based on criteria established in *Internal Control Integrated Framework: (2013)* issued by COSO.

Basis for Opinion

The Company s management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Assessment of Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company s consolidated financial statements and an opinion on the Company s internal control over financial reporting based on our audit. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud and whether effective internal control over financial reporting was maintained in all material respects.

Our audit of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provide

a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Baker Tilly Virchow Krause, LLP

We have served as the Company s auditor since 2018.

Allentown, Pennsylvania

December 14, 2018

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders

Malvern Bancorp, Inc. and Subsidiaries

Paoli, Pennsylvania

We have audited the accompanying consolidated statements of financial condition of Malvern Bancorp, Inc. and its subsidiaries (collectively the Company) as of September 30, 2017 and the related consolidated statements of operations, comprehensive income, changes in shareholders equity, and cash flows for each of the two years in the period ended September 30, 2017. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Malvern Bancorp, Inc. and its subsidiaries at September 30, 2017, and the results of their operations and their cash flows for each of the two years in the period ended September 30, 2017, in conformity with accounting principles generally accepted in the United States of America.

/s/ BDO USA, LLP

Philadelphia, Pennsylvania

December 29, 2017

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Malvern Bancorp, Inc. and Subsidiaries

Consolidated Statements of Financial Condition

	September 30, 2018	September 30, 2017
	(Dollars in thousands, except per share and share data)	
Assets		
Cash and due from depository institutions	$ 1,563	$ 1,615
Interest bearing deposits in depository institutions	29,271	115,521
Cash and Cash Equivalents	30,834	117,136
Investment securities available for sale, at fair value (amortized cost of $24,804 and $14,869 at September 30, 2018 and 2017, respectively)	24,298	14,587
Investment securities held to maturity, at cost (fair value of $28,968 and $34,566 at September 30, 2018 and 2017, respectively)	30,092	34,915
Restricted stock, at cost	8,537	5,559
Loans receivable, net of allowance for loan losses of $9,021 and $8,405 at September 30, 2018 and 2017, respectively	902,136	834,331
Accrued interest receivable	3,800	3,139
Property and equipment, net	7,181	7,507
Deferred income taxes, net	3,195	6,671
Bank-owned life insurance	19,403	18,923
Other assets	4,475	3,244
Total Assets	$ 1,033,951	$ 1,046,012
Liabilities and Shareholders Equity		
Liabilities		
Deposits:		
Deposits-noninterest-bearing	$ 41,677	$ 42,121
Deposits-interest-bearing	732,486	748,275
Total Deposits	774,163	790,396
FHLB advances	118,000	118,000
Other short-term borrowings	2,500	5,000
Subordinated debt	24,461	24,303
Advances from borrowers for taxes and insurance	1,305	1,553
Accrued interest payable	784	694
Other liabilities	1,915	3,546
Total Liabilities	923,128	943,492

Commitments and Contingencies		
Shareholders Equity		
Preferred stock, $0.01 par value, 10,000,000 shares authorized, none issued		
Common stock, $0.01 par value, 50,000,000 shares authorized, issued and outstanding: 6,580,879 shares at September 30, 2018 and 6,572,684 shares at September 30, 2017	66	66
Additional paid-in-capital	61,099	60,736
Retained earnings	50,412	43,139
Unearned Employee Stock Ownership Plan (ESOP) shares	(1,338)	(1,483)
Accumulated other comprehensive income	584	62
Total Shareholders Equity	110,823	102,520
Total Liabilities and Shareholders Equity	$ 1,033,951	$ 1,046,012

See notes to consolidated financial statements.

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Malvern Bancorp, Inc. and Subsidiaries

Consolidated Statements of Operations

	Year Ended September 30,		
	2018	**2017**	**2016**
	(Dollars in thousands, except per share and share data)		
Interest and Dividend Income			
Loans, including fees	$ 36,862	$ 30,841	$ 21,206
Investment securities, taxable	1,094	1,561	2,824
Investment securities, tax-exempt	251	492	751
Dividends, restricted stock	467	257	250
Interest-bearing cash accounts	1,356	631	213
Total Interest and Dividend Income	40,030	33,782	25,244
Interest Expense			
Deposits	9,200	6,236	4,537
Short-term borrowings	68	34	
Long-term borrowings	2,200	2,176	2,195
Subordinated debt	1,527	1,000	
Total Interest Expense	12,995	9,446	6,732
Net Interest Income	27,035	24,336	18,512
Provision for Loan Losses	954	2,791	947
Net Interest Income after Provision for Loan Losses	26,081	21,545	17,565
Other Income			
Service charges and other fees	1,268	992	923
Rental income-other	268	227	211
Net gains on sale of investments		463	565
Net gains on sale of real estate	1,186		1
Net gains on sale of loans	102	154	116
Earnings on bank-owned life insurance	480	505	517
Total Other Income	3,304	2,341	2,333
Other Expense			
Salaries and employee benefits	8,193	7,114	6,290
Occupancy expense	2,295	2,084	1,820
Federal deposit insurance premium	298	244	579
Advertising	152	216	131

Data processing		1,098		1,195		1,128
Professional fees		2,891		1,894		1,683
Other real estate owned (income) expense, net				(172)		27
Other operating expenses		2,876		2,572		2,264
Total Other Expenses		17,803		15,147		13,922
Income before income tax expense (benefit)		11,582		8,739		5,976
Income tax expense (benefit)		4,276		2,922		(6,174)
Net Income	$	7,306	$	5,817	$	12,150
Earnings Per Common Share:						
Basic	$	1.13	$	0.90	$	1.90
Diluted	$	1.13	$	0.90	$	1.90
Weighted Average Common Shares Outstanding						
Basic		6,456,154		6,431,445		6,409,265
Diluted		6,459,510		6,432,137		6,409,325

See notes to consolidated financial statements.

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Malvern Bancorp, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

(In thousands)	Year Ended September 30, 2018	2017	2016
Net Income	$ 7,306	$ 5,817	$ 12,150
Other Comprehensive Income, Net of Tax:			
Unrealized holding gains (losses) on available-for-sale securities	(229)	(275)	2,128
Tax effect	48	94	(723)
Net of tax amount	(181)	(181)	1,405
Reclassification adjustment for net gains arising during the period[1]		(463)	(565)
Tax effect		157	192
Net of tax amount		(306)	(373)
Accretion of unrealized holding losses on securities transferred from available-for-sale to held-to-maturity[2]	6	9	9
Tax effect	(1)	(3)	(3)
Net of tax amount	5	6	6
Fair value adjustment on derivatives	868	918	(194)
Tax effect	(203)	(312)	172
Net of tax amount	665	606	(22)
Total other comprehensive income	489	125	1,016
Total comprehensive income	$ 7,795	$ 5,942	$ 13,166

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

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

See notes to consolidated financial statements.

Malvern Bancorp, Inc. and Subsidiaries

Consolidated Statements of Changes in Shareholders Equity

Years Ended September 30, 2018, 2017, and 2016

	Common Stock	Additional Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity
			(in thousands, except share data)			
Balance, October 1, 2015	$ 66	$ 60,365	$ 25,172	$ (1,775)	$ (1,079)	$ 82,749
Net Income			12,150			12,150
Other comprehensive income					1,016	1,016
Committed to be released ESOP shares (14,400 shares)		96		146		242
Balance, September 30, 2016	$ 66	$ 60,461	$ 37,322	$ (1,629)	$ (63)	$ 96,157
Net Income			5,817			5,817
Other comprehensive income					125	125
Committed to be released ESOP shares (14,400 shares)		165		146		311
Stock based compensation		110				110
Balance, September 30, 2017	$ 66	$ 60,736	$ 43,139	$ (1,483)	$ 62	$ 102,520
Net Income			7,306			7,306
Reclassification of certain tax effects from accumulated other comprehensive income			(33)		33	
Other comprehensive income					489	489
Committed to be released ESOP shares (14,400 shares)		221		145		366
Stock based compensation		142				142
Balance, September 30, 2018	$ 66	$ 61,099	$ 50,412	$ (1,338)	$ 584	$ 110,823

See notes to consolidated financial statements.

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Malvern Bancorp, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

	Year Ended September 30,		
	2018	2017	2016
	(In thousands)		
Cash Flows from Operating Activities			
Net income	$ 7,306	$ 5,817	$ 12,150
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation expense	758	724	650
Provision for loan losses	954	2,791	947
Deferred income taxes expense (benefit)	3,353	2,092	(6,316)
ESOP expense	366	311	242
Stock based compensation	142	110	
Amortization of premiums and discounts on investment securities, net	360	814	1,243
(Accretion) amortization of loan origination fees and costs	(77)	(924)	748
Amortization of mortgage service rights	45	60	73
Amortization of subordinated debt issuance costs	158	39	
Net gain on sale of investment securities available for sale		(463)	(565)
Net gain on sale of real estate	(1,186)		(1)
Net gain on sale of secondary market loans	(102)	(154)	(116)
Proceeds on sale of secondary market loans	9,189	9,270	6,390
Originations of secondary market loans	(9,087)	(9,116)	(6,274)
Gain on sale of other real estate owned			(19)
Write down of other real estate owned			20
Earnings on bank-owned life insurance	(480)	(505)	(517)
Increase in accrued interest receivable	(661)	(581)	(74)
Increase in accrued interest payable	90	267	31
(Decrease) increase in other liabilities	(1,631)	563	766
Increase in other assets	(439)	(1,058)	(44)
Increase in income tax receivable		(225)	
Net Cash Provided by Operating Activities	9,058	9,832	9,334
Cash Flows from Investing Activities			
Investment securities available-for-sale:			
Purchases	(30,140)	(250)	(2,116)
Sales		51,119	62,818
Maturities, calls and principal repayments	20,123	583	2,437
Investment securities held-to-maturity:			
Maturities, calls and principal repayments	4,545	5,350	16,391
(Loan originations) and principal collections, net	(68,682)	(262,039)	(184,548)

Proceeds from sale of other real estate owned			1,167
Proceeds from death benefit of bank-owned life insurance			1,049
Net increase in restricted stock	(2,979)	(135)	(659)
Proceeds from sale of real estate	1,315		1
Purchases of property and equipment	(561)	(1,594)	(752)
Net Cash Used in Investing Activities	(76,379)	(206,966)	(104,212)
Cash Flows from Financing Activities			
Net (decrease) increase in deposits	(16,233)	188,350	136,524
Proceeds for long-term borrowings	140,000	140,000	121,000
Repayment of long-term borrowings	(140,000)	(140,000)	(106,000)
Increase in other borrowed money		10,000	
Repayment of other borrowed money	(2,500)	(5,000)	
Decrease in advances from borrowers for taxes and insurance	(248)	(106)	(147)
Net proceeds from issuance of subordinated debt		24,264	
Net Cash (Used in) Provided by Financing Activities	(18,981)	217,508	151,377
Net (Decrease) Increase in Cash and Cash Equivalents	(86,302)	20,374	56,499
Cash and Cash Equivalent Beginning	117,136	96,762	40,263
Cash and Cash Equivalent Ending	$ 30,834	$ 117,136	$ 96,762
Supplementary Cash Flows Information			
Interest paid	$ 12,904	$ 9,179	$ 6,701
Income taxes paid	$ 2,630	$ 130	$

See notes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Organizational Structure and Nature of Operations

Malvern Bancorp, Inc. (the Company or Malvern Bancorp), a Pennsylvania corporation, is a registered bank holding company under the Bank Holding Company Act of 1956, as amended (the Holding Company Act). Malvern Bancorp is the holding company for Malvern Bank, National Association (Malvern Bank or the Bank), a national bank that was originally organized in 1887 as a federally-chartered savings bank. Malvern Bank now serves as one of the oldest banks headquartered on the Philadelphia Main Line. For more than a century, the Bank has been committed to helping people build prosperous communities as a trusted financial partner, forging lasting relationships through teamwork, respect and integrity. Effective February 12, 2018, the Bank converted from a federal savings bank charter to a national bank charter and Malvern Bancorp converted from a savings and loan holding company to a bank holding company.

The Bank conducts business from its headquarters in Paoli, Pennsylvania, a suburb of Philadelphia, and through its nine other banking locations in Chester, Delaware and Bucks counties, Pennsylvania, Palm Beach Florida, and Morristown, New Jersey, its New Jersey regional headquarters. The Bank also maintains a representative office in Montchanin, Delaware. The Bank s primary market niche is providing personalized service to its client base.

The Bank s principal business consists of attracting deposits from businesses and the general public and investing those deposits, together with borrowings and funds generated from operations, in one- to four-family residential real estate loans, construction and development loans, commercial and multi-family real estate loans, commercial business loans, home equity loans and lines of credit and other consumer loans, as well as investing in investment securities.

The Bank s revenues are derived principally from interest on loans and investment securities, loan commitment and customer service fees and our mortgage banking operation. Our primary sources of funds are deposits, borrowings (including from the Federal Home Loan Bank of Pittsburgh (the FHLB)), and principal and interest payments on loans and securities, as well as the sale of residential loans in the secondary market. The Bank s primary expenses are interest expense on deposits and borrowings, provisions for loan losses and general operating expenses.

The Bank owns 100% of Malvern Insurance Associates, LLC (Malvern Associates), a Pennsylvania limited liability company. Malvern Associates is a licensed insurance broker under Pennsylvania and New Jersey law.

The Bank owns a 10% non-controlling interest in Bell Rock Capital, LLC (Bell Rock), a Delaware limited liability company and investment advisor registered with the SEC, and headquartered in Rehoboth Beach, Delaware.

Certain mortgage-backed securities of the Bank are held through Delaware statutory trusts, 5% of which are owned by the Bank and 95% of which are owned by Coastal Asset Management Co., a Delaware corporation which is wholly owned by the Bank.

The Bank owns a 3.39% interest in Bankers Settlement Services Capital Region, LLC, a Pennsylvania limited liability company which acts as a title insurance agent or agency.

The banking industry is highly regulated. The Bank is supervised by the Office of the Comptroller of the Currency (the OCC), and the Company is supervised by the Board of Governors of the Federal Reserve Board (the FRB).

In accordance with the subsequent events topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (the Codification or the ASC), the Company evaluates events and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Organizational Structure and Nature of Operations (Continued)

transactions that occur after the statement of financial condition date and through the date these consolidated financial statements are being issued for potential recognition and disclosure in the consolidated financial statements. The effect of all subsequent events that provide additional evidence of conditions that existed at the statement of financial condition date are recognized in the audited consolidated financial statements as of September 30, 2018.

Note 2 Summary of Significant Accounting Policies

Basis of Presentation and Consolidation

The consolidated financial statements at and for the years ended September 30, 2018, 2017 and 2016 include the accounts of Malvern Bancorp, Inc. and its subsidiaries. All significant intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

Significant Group Concentrations of Credit Risk

Most of the Company s activities are with customers located within Chester County, Pennsylvania. In addition to Chester County, our lending efforts are focused in neighboring Bucks County, Montgomery County and Delaware County, which are also in southeastern Pennsylvania, New Jersey and the New York metropolitan marketplace. Note 5 discusses the types of investment securities that the Company invests in. Note 6 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations to any one industry or customer. Although the Company has a diversified portfolio, its debtor s ability to honor their contracts is influenced by, among other factors, the region s economy.

Cash and Cash Equivalents

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

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

The Company is required to maintain average reserve balances in vault cash with the Federal Reserve Bank based upon outstanding balances of deposit transaction accounts. Based upon the Company s outstanding transaction deposit balances, the Bank maintained a deposit account with the Federal Reserve Bank of Philadelphia in the amount of zero at September 30, 2018 and 2017.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

Investment Securities

Held-to-maturity (HTM) are securities that includes debt securities that the Company has the positive intent and the ability to hold to maturity. These securities are reported at amortized cost and adjusted for unamortized premiums and discounts. Securities held for trading are securities that are bought and held principally for the purpose of selling in the near term; these securities are reported at fair value, with unrealized gains and losses reported in current earnings. At September 30, 2018 and 2017, the Company had no investment securities classified as trading. Debt securities that will be held for indefinite periods of time and equity securities, including securities that may be sold in response to changes in market interest or prepayment rates, needs for liquidity and changes in the availability of and the yield of alternative investments, are classified as available for sale. Realized gains and losses are recorded on the trade date and are determined using the specific identification method. Securities held as available for sale are reported at fair value, with unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive income (AOCI). Management determines the appropriate classification of investment securities at the time of purchase.

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

Loans Receivable

The Company, through the Bank, grants mortgage, construction, commercial and consumer loans to customers. Substantially all of our loans are to individuals, businesses and real estate developers in Chester County, Pennsylvania and neighboring areas in southern Pennsylvania, New Jersey and the New York metropolitan marketplace. The ability of the Company s debtors to honor their contracts is dependent upon, among other factors, the real estate and general economic conditions in this area.

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

The loans receivable portfolio is segmented into residential loans, construction and development loans, commercial loans and consumer loans. The residential loan segment has one class, one- to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built. Commercial construction loans are

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

made for the purpose of acquiring, developing and constructing a commercial structure. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

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

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

Reserves for unfunded lending commitments represent management s estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated statement of financial condition.

Allowance for Loan Losses

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

The allowance for credit losses is maintained at a level considered adequate to provide for losses that can be reasonably estimated. Management performs a quarterly evaluation of the adequacy of the allowance. The allowance

is based on the Company s past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay, the estimated value of any underlying collateral, the composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, a specific reserve is recognized when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class that are not considered impaired.

These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these classes of loans, as adjusted for qualitative factors. These qualitative risk factors include:

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

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

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

In addition, the allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower s overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial and consumer loans. Credit quality risk ratings include categories of pass, special mention, substandard and doubtful. Assets classified as Pass are those protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. Assets which do not currently expose the insured institution to sufficient risk to warrant classification as substandard or doubtful but possess certain identified weaknesses are required to be designated special mention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

insured institution will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Residential Lending. Residential mortgage originations are secured primarily by properties located in the Company s primary market area and surrounding areas. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 10 to 30 years. We also offer adjustable rate mortgage (ARM) loans where the interest rate either adjusts on an annual basis or is fixed for the initial one, three or seven years and then adjusts annually.

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

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

Construction and Development Lending. We originate construction loans for residential and, to a lesser extent, commercial uses within our market area. We generally limit construction loans to builders and developers with whom we have an established relationship, or who are otherwise known to officers of the Bank. Our construction and development loans currently in the portfolio typically have variable rates of interest tied to the prime rate which improves the interest rate sensitivity of our loan portfolio.

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

work with builders with whom we have established relationships, require annual updating of tax returns and other financial data of developers and obtain personal guarantees from the principals.

Commercial Lending. Commercial and multi-family real estate loans generally present a higher level of risk than loans secured by one- to four-family residences. This greater risk is due to several factors, including the

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced (for example, if leases are not obtained or renewed, or a bankruptcy court modifies a lease term, or a major tenant is unable to fulfill its lease obligations), the borrower s ability to repay the loan may be impaired.

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

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

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

Once all factor adjustments are applied, general reserve allocations for each segment are calculated, summarized and reported on the ALLL summary. ALLL final schedules, calculations and the resulting evaluation process are reviewed quarterly.

In addition, Federal bank regulatory agencies, as an integral part of their examination process, periodically review the Company s allowance for loan losses and may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination. Based on management s comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

including the length of the delay, the reasons for the delay, the borrower s prior payment record and the amount of the shortfall in relation to the principal and interest owed.

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

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

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

Troubled Debt Restructurings

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring may be modified by means of extending the maturity date of the loan, reducing the interest rate on the loan to a rate which is below market, a combination of rate adjustments and maturity extensions, or by other means including covenant modifications, forbearances or other concessions. However, the Company generally only restructures loans by modifying the payment structure to interest only or by reducing the actual interest rate.

We do not accrue interest on loans that were non-accrual prior to the troubled debt restructuring until they have performed in accordance with their restructured terms for a period of at least six months. We continue to accrue interest on troubled debt restructurings which were performing in accordance with their terms prior to the restructure and continue to perform in accordance with their restructured terms. Management evaluates the ALLL with respect to TDRs under the same policy and guidelines as all other performing loans are evaluated with respect to the ALLL.

Loan Servicing

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate,

ancillary income, prepayment speeds and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into other expense in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Company later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income. The Company also sells loans in the secondary market with servicing released.

Other Real Estate Owned

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

Restricted Stock

Restricted stock represents required investments in the common stock of a correspondent bank and is carried at cost. As of September 30, 2018 and 2017, restricted stock consists of the common stock of the Federal Reserve Bank, FHLB and Atlantic Community Bankers Bank (ACBB).

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

During the years ended September 30, 2018 and 2017, there were net repurchases of restricted stock of $3.0 million and $135,000, respectively. Also, as of September 30, 2018 and 2017 the number of restricted shares was 108,151 and 54,787, respectively. There were approximately $467,000, $257,000 and $250,000 of dividends on restricted stock received or recognized in income for fiscal years 2018, 2017 and 2016, respectively.

Property and Equipment

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

Transfers of Financial Assets

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

Bank-Owned Life Insurance

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

Employee Benefit Plans

The Bank s 401(k) plan allows eligible participants to set aside a certain percentage of their salaries before taxes. The Company may elect to match employee contributions up to a specified percentage of their respective salaries in an amount determined annually by the Board of Directors. The Company s matching contribution related to the plan resulted in expenses of $121,000, $115,000, and $90,000, for fiscal 2018, 2017, and 2016, respectively.

The Company also maintains an unfunded Supplemental Executive and a Director Retirement Plan (the Plans). The accrued amount for the Plans included in other liabilities was $970,000 and $1.1 million at September 30, 2018 and 2017, respectively. Distributions made to directors for each of the fiscal years 2018 and 2017 were approximately $93,000 and $25,000, respectively. The expense associated with the Plans for the years ended September 30, 2018, 2017, and 2016 was $5,000, $30,000, and $11,000, respectively.

Derivatives and Hedging

The Company records cash flow hedges at the inception of the derivative contract based on the Company s intentions and belief as to likely effectiveness as a hedge. The Company documents the strategy for entering into the transactions and the method of assessing ongoing effectiveness. Cash flow hedges represent a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability. For a cash flow hedge that is effective, the gain or loss on the derivative is reported in other comprehensive income and is reclassified into earnings in the same periods during which the hedged transaction affects earnings. The changes in the fair value of derivatives that are not highly effective in hedging the changes in fair value or expected cash flows of the hedged item are recognized immediately in current earnings. Changes in the fair value of derivatives that do not qualify for hedge accounting are reported currently in earnings, as noninterest income.

Net cash settlements on derivatives that qualify for hedge accounting are recorded in interest income or interest expense, based on the item being hedged. Net cash settlements on derivatives that do not qualify for hedge accounting are reported in noninterest income. Cash flows on hedges are classified in the cash flow statement the same as the cash flows of the items being hedged. To determine fair value, the Company uses third party pricing models that incorporate assumptions about market conditions and risks that are current at the reporting date. The Company does not use derivative instruments for speculative purposes.

The Company also formally assesses, both at the hedge s inception and on an ongoing basis, whether the derivative instruments that are used are highly effective in offsetting changes in fair values or cash flows of the hedged items.

The Company discontinues hedge accounting when it determines that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative is settled or terminates, a hedged forecasted transaction is no longer probable, a hedged firm commitment is no longer firm, or treatment of the derivative as a hedge is no longer appropriate or intended.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

When hedge accounting is discontinued, subsequent changes in fair value of the derivative are recorded as noninterest income. When a cash flow hedge is discontinued but the hedged cash flows or forecasted transactions are still expected to occur, gains or losses that were accumulated in other comprehensive income are amortized into earnings over the same periods which the hedged transactions will affect earnings.

Advertising Costs

The Company follows the policy of charging the costs of advertising to expense as incurred. Advertising expense was $152,000, $216,000 and $131,000 in fiscal 2018, 2017 and 2016, respectively.

Income Taxes

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

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

Commitments and Contingencies

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

Segment Information

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

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale investment securities, are reported as a separate component of the shareholders equity section of the statement of financial condition, such items, along with net income, are components of comprehensive income.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

For securities transferred from available for sale to held to maturity, the Company records the amortization and/or accretion of unrealized holding losses on such investment securities, in accumulated other comprehensive income.

The Company also records changes in the fair value of interest rate derivatives used in its cash flow hedging activities, net of deferred income tax, in accumulated other comprehensive income.

Reclassifications

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

Revenue Recognition

Accounting Standards Codification (ASC) 606, *Revenue from Contracts with Customers* (ASC 606), establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity s contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.

The majority of our revenue-generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as our loans, investment securities, derivatives as well as revenue related to BOLI, sales of investment securities, rental income, and gain on sale of loans. Revenue-generating activities that are within the scope of ASC 606, which are presented in our income statements as components of other income include certain fees such as credit card fee income, DDA service and fee income, and debit card fees.

Recently Issued Accounting Pronouncements

Depository and Lending. In May 2018, the FASB issued Accounting Standards Update (ASU) 2018-06, *Codification Improvements to Topic 942, Financial Services-Depository and Lending* to supersede the guidance in Subtopic 942-740, Financial Services Depository and Lending Income Taxes, that is related to Circular 202 because that guidance has been rescinded by the OCC and no longer is relevant. The changes were effective when issued. The adoption of this new requirement did not have a material impact on the consolidated earnings, financial position or cash flows of the Company.

Income Taxes. In March 2018, the FASB issued ASU 2018-05, *Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118* to update the income tax accounting in U.S. generally accepted accounting principles (GAAP) to reflect the Securities and Exchange Commission (SEC) interpretive guidance released on Dec. 22, 2017, when the Tax Cuts and Jobs Act (the TCJA) was signed into law. The adoption of this new requirement did not have a material impact on the consolidated earnings, financial position or cash flows of the Company.

In October 2016, the FASB issued ASU No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*. The ASU requires an entity to recognize the income tax consequences of intra-entity transfers of assets other than inventory at the time that the transfer occurs. Current guidance does not require recognition of tax consequences until the asset is eventually sold to a third party. ASU 2016-16 is

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

effective for fiscal years, and interim periods within, beginning after December 15, 2017, with early adoption permitted as of the first interim period presented in a year. The Company will adopt these changes effective October 1, 2018. Adoption of this ASU will not have a material impact on our results of operations or financial position.

Income Statement. In February 2018, the FASB issued ASU 2018-02, *Income Statement Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. The amendments in this Update allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the TCJA. Consequently, the amendments eliminate the stranded tax effects resulting from the TCJA and will improve the usefulness of information reported to financial statement users. All entities may adopt the amendments in this Update for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The amendments in this Update should be applied either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the TCJA is recognized. We have elected to early adopt the ASU as of January 1, 2018. The adoption of the guidance resulted in a reclassification of an immaterial amount stranded in accumulated other comprehensive income to retained earnings in the fiscal second quarter of 2018.

Derivatives and Hedging. In August 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.* The guidance is intended to update and better align an entity s risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. To meet that objective, the amendments expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. The updated guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early application is permitted in any interim period after issuance of the Update. All transition requirements and elections should be applied to hedging relationships existing (that is, hedging relationships in which the hedging instrument has not expired, been sold, terminated, or exercised or the entity has not removed the designation of the hedging relationship) on the date of adoption. The effect of adoption should be reflected as of the beginning of the fiscal year of adoption (that is, the initial application date). The Company has elected to early adopt this standard effective October 1, 2018. Adoption of this ASU will not have a material impact on our results of operations or financial position.

Stock-Based Compensation. In May 2017, the FASB issued ASU No. 2017-09, *Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting*, to provide clarity and reduce both (1) diversity in practice and (2) cost and complexity when applying the guidance in Topic 718, Compensation Stock Compensation, to a change to the terms or conditions of a share-based payment award. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should account for the effects of a modification unless all the following are met: (1) the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification; (2) the vesting conditions of the modified award are the same as the

vesting conditions of the original award immediately before the original award is modified; (3) the classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

before the original award is modified. The current disclosure requirements in Topic 718 apply regardless of whether an entity is required to apply modification accounting under the amendments in this update. For public business entities, the amendments in this update become effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. The Company will adopt these changes effective October 1, 2018 on a prospective basis. Adoption of this ASU will not have a material impact on our results of operations or financial position.

Receivables. In March 2017, the FASB issued ASU No. 2017-08, *Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*. This ASU shortens the amortization period for the premium on certain purchased callable debt securities to the earliest call date. Today, entities generally amortize the premium over the contractual life of the security. The new guidance does not change the accounting for purchased callable debt securities held at a discount; the discount continues to be amortized to maturity. ASU No. 2017-08 is effective for interim and annual reporting periods beginning after December 15, 2018; early adoption is permitted. The guidance calls for a modified retrospective transition approach under which a cumulative-effect adjustment will be made to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is currently evaluating the provisions of ASU No. 2017-08 to determine the potential impact the new standard will have on the Company s Consolidated Financial Statements.

Statement of Cash Flows. In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force).* The ASU is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2017. The Company will adopt these changes effective October 1, 2018. Adoption of this ASU will not have a material impact on our results of operations or financial position.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230) Restricted Cash (a consensus of the FASB Emerging Issues Task Force)*. The new guidance requires restricted cash and restricted cash equivalents to be included with cash and cash equivalents when reconciling the beginning-of-period and end-of period total amounts shown on the statement of cash flows. If restricted cash is presented separately from cash and cash equivalents on the balance sheet, companies will be required to reconcile the amounts presented on the statement of cash flows to the amounts on the balance sheet. Companies will also need to disclose information about the nature of the restrictions. The amendments in this update do not provide a definition of restricted cash or restricted cash equivalents. The guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company will adopt these changes effective October 1, 2018. Adoption of this ASU will not have a material impact on our results of operations or financial position.

Financial Instruments. In January 2016, the FASB issued ASU 2016-01, *Financial Instruments Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this Update require equity securities (including other ownership interests, such as partnerships, unincorporated joint ventures, and limited liability companies) to be measured at fair value with changes in the fair value recognized through net income. The amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company will adopt these changes effective October 1, 2018

on a prospective basis. Adoption of this ASU will not have a material impact on our results of operations or financial position.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The ASU requires an organization to measure all

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2019. All entities may adopt the amendments in this Update earlier as of the fiscal year beginning after December 15, 2018, including interim periods within those fiscal years. The Company does not expect to early adopt these changes. The Bank has a software system in place to assist with the calculation of Current Expected Credit Losses (CECL). Data is being collected and refined and testing of the various models is in process. The Company is evaluating the impact of this new requirement to the consolidated financial statements.

Leases. In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The update requires lessees to recognize, as of the lease commencement date, assets and liabilities for all such leases with lease terms of more than 12 months, which is a change from the current GAAP requirement to recognize only capital leases on the balance sheet. Pursuant to the new standard, the liability initially recognized for the lease obligation is equal to the present value of the lease payments not yet made, discounted over the lease term at the implicit interest rate of the lease, if available, or otherwise at the lessee s incremental borrowing rate. The lessee is also required to recognize an asset for its right to use the underlying asset for the lease term, based on the liability subject to certain adjustments, such as for initial direct costs. Leases are required to be classified as either operating or finance, with expense on operating leases recorded as a single lease cost on a straight-line basis. For finance leases, interest expense on the lease liability is required to be recognized separately from the straight-line amortization of the right-of-use asset. Quantitative disclosures are required for certain items, including the cost of leases, the weighted-average remaining lease term, the weighted-average discount rate and a maturity analysis of lease liabilities. Additional qualitative disclosures are also required regarding the nature of the leases, such as basis, terms and conditions of: (i) variable interest payments; (ii) extension and termination options; and (iii) residual value guarantees. For lessors, the standard modifies classification criteria and accounting for sales- type and direct financing leases and requires a lessor to derecognize the carrying value of the leased asset that is considered to have been transferred to a lessee and record a lease receivable and residual asset (receivable and residual approach). This Update is effective for public companies for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Company does not expect to early adopt this standard. The new standard allows for a cumulative effect adjustment in year of adoption or adopted by applying the new guidance as of the beginning of the earliest comparative period presented, using a modified retrospective transition approach with certain optional practical expedients. The Company is in the process of evaluating the impact of this guidance but expects to report higher assets and liabilities as a result of including additional leases on the consolidated statement of financial condition.

Revenue Recognition. In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (a new revenue recognition standard). The ASU s core principle is that a company will recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, this ASU specifies the accounting for certain costs to obtain or fulfill a contract with a customer and expands disclosure requirements for revenue recognition. This ASU is effective,

as a result of ASU 2015-14, for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The Company adopted the revenue recognition guidance on October 1, 2018 using the modified retrospective approach. A significant amount of the Company s revenues is derived from net interest income on financial assets and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 Summary of Significant Accounting Policies (Continued)

liabilities, which are excluded from the scope of the amended guidance. Non-interest income streams of the Company that are out of scope of the new standard include BOLI, sales of investment securities, and certain items within other income. Non-interest items that fall within the scope of the new standard are items included within service charges and other fees. The Company analyzed the in-scope contracts and determined there were no material changes in the timing of revenue recognition when considering the amended guidance. The adoption of this ASU on October 1,2018 will not have a material impact on our results of operations, financial position or disclosure to the notes of the consolidated financial statements. The most significant impact of adoption will be expanded disclosures relating to disaggregation of in-scope revenue, which will be included in our fiscal year first quarter 2019 Form 10-Q upon adoption of the ASU.

Note 3 Earnings Per Share

Basic earnings per common share is computed based on the weighted average number of shares outstanding reduced by unearned ESOP shares. Diluted earnings per share is computed based on the weighted average number of shares outstanding and common stock equivalents (CSEs) that would arise from the exercise of dilutive securities reduced by unearned ESOP shares. For the fiscal year ended September 30, 2018, the Company issued stock options to purchase 6,996 shares of common stock, as well as 6,400 restricted shares, which are considered CSEs. For the fiscal year ended September 30, 2017, the Company issued stock options to purchase 7,000 shares of common stock, as well as 12,522 restricted shares, which are considered CSEs. For the fiscal year ended September 30, 2016, the Company issued stock options to purchase 5,000 shares of common stock, as well as 1,930 restricted shares.

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

	Year Ended September 30,		
(In thousands, except per share and share data)	2018	2017	2016
Net Income	$ 7,306	$ 5,817	$ 12,150
Weighted average shares outstanding	6,578,097	6,567,788	6,560,012
Average unearned ESOP shares	(121,943)	(136,343)	(150,747)
Basic weighted average shares outstanding	6,456,154	6,431,445	6,409,265
Plus: effect of dilutive options and restricted stock	3,356	692	60
Diluted weighted average common shares outstanding	6,459,510	6,432,137	6,409,325

Earnings per share:						
Basic	$	1.13	$	0.90	$	1.90
Diluted	$	1.13	$	0.90		1.90

Note 4 Employee Stock Ownership Plan

The Company established an employee stock ownership plan (ESOP) for substantially all of its full-time employees. As of September 30, 2018, the current ESOP trustee is Pentegra. Shares of the Company s common stock purchased by the ESOP are held until released for allocation to participants. Shares released are allocated to each eligible participant based on the ratio of each such participant s base compensation to the total base compensation of all eligible plan participants. As the unearned shares are committed to be released and allocated

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 4 Employee Stock Ownership Plan (Continued)

among participants, the Company recognizes compensation expense equal to the fair value of the ESOP shares during the periods in which they become committed to be released. To the extent that the fair value of the ESOP shares released differs from the cost of such shares, the difference is charged or credited to additional paid-in capital. During the period from May 20, 2008 to September 30, 2008, the ESOP purchased 241,178 shares of common stock for approximately $2.6 million, at an average price of $10.86 per share, which was funded by a loan from Malvern Federal Bancorp, Inc. (the Company s predecessor). The ESOP loan is being repaid principally from the Bank s contributions to the ESOP. The loan, which bears an interest rate of 5%, is being repaid in quarterly installments through 2026. Shares are released to participants proportionately as the loan is repaid. During each of the years ended September 30, 2018, 2017 and 2016, there were 14,400 shares committed to be released. At September 30, 2018, there were 114,765 unallocated shares and 144,453 allocated shares held by the ESOP. The unallocated shares had an aggregate fair value of approximately $2.7 million at September 30, 2018.

Note 5 Investment Securities

The Company s investment securities are classified as available-for-sale or held-to-maturity at September 30, 2018 and 2017. Investment securities available-for-sale are reported at fair value with unrealized gains or losses included in equity, net of tax. Accordingly, the carrying value of such securities reflects their fair value at the balance sheet date. Fair value is based upon either quoted market prices, or in certain cases where there is limited activity in the market for a particular instrument, assumptions are made to determine their fair value.

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 Investment Securities (Continued)

The following tables present information related to the Company s investment securities at September 30, 2018 and 2017.

	September 30, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Investment Securities Available-for-Sale:				
U.S. treasury notes	$ 9,996	$	$ (10)	$ 9,986
State and municipal obligations	6,953		(66)	6,887
Single issuer trust preferred security	1,000		(79)	921
Corporate debt securities	6,605		(351)	6,254
Mutual fund	250			250
Total	24,804		(506)	24,298
Investment Securities Held-to-Maturity:				
U.S. government agencies	$ 1,999	$	$ (20)	$ 1,979
State and municipal obligations	8,181		(66)	8,115
Corporate debt securities	3,715		(49)	3,666
Mortgage-backed securities:				
Collateralized mortgage obligations, fixed-rate	16,197		(989)	15,208
Total	$ 30,092	$	$ (1,124)	$ 28,968
Total investment securities	$ 54,896	$	$ (1,630)	$ 53,266

	September 30, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Investment Securities Available-for-Sale:				
State and municipal obligations	$ 6,992	$ 39	$ (2)	$ 7,029
Single issuer trust preferred security	1,000		(66)	934
Corporate debt securities	6,627		(253)	6,374
Mutual fund	250			250

Total	14,869	39	(321)	14,587
Investment Securities Held-to-Maturity:				
U.S. government agencies	$ 1,999	$	$ (8)	$ 1,991
State and municipal obligations	9,574	89		9,663
Corporate debt securities	3,818	26		3,844
Mortgage-backed securities:				
Collateralized mortgage obligations, fixed-rate	19,524	1	(457)	19,068
Total	$ 34,915	$ 116	$ (465)	$ 34,566
Total investment securities	$ 49,784	$ 155	$ (786)	$ 49,153

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 Investment Securities (Continued)

For fiscal 2018, no available-for-sale investment securities were sold. For fiscal 2017, proceeds of available-for-sale investment securities sold amounted to approximately $51.1 million. Gross realized gains on investment securities sold amounted to approximately $464,000, while gross realized losses amounted to approximately $1,000 for the period. For fiscal 2016, proceeds of available-for-sale investment securities sold amounted to approximately $62.8 million. Gross realized gains on investment securities sold amounted to approximately $595,000, while gross realized losses amounted to approximately $30,000 for the period.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 Investment Securities (Continued)

The following tables indicate gross unrealized losses not recognized in income and fair value, aggregated by investment category and the length of time individual securities have been in a continuous unrealized loss position at September 30, 2018 and 2017.

	September 30, 2018					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair value	Unrealized Losses
	(Dollars in thousands)					
Investment Securities Available-for-Sale:						
U.S. treasury notes	$ 9,986	$ (10)	$	$	$ 9,986	$ (10)
State and municipal obligations	5,433	(56)	1,000	(10)	6,433	(66)
Single issuer trust preferred security			921	(79)	921	(79)
Corporate debt securities			6,254	(351)	6,254	(351)
Total	$ 15,419	$ (66)	$ 8,175	$ (440)	$ 23,594	$ (506)
Investment Securities Held-to-Maturity:						
U.S. government agencies			1,979	(20)	1,979	(20)
State and municipal obligations	8,115	(66)			8,115	(66)
Corporate securities	3,666	(49)			3,666	(49)
Mortgage-backed securities:						
CMO, fixed-rate	127	(6)	15,081	(983)	15,208	(989)
Total	11,908	(121)	17,060	(1,003)	28,968	(1,124)
Total investment securities	$ 27,327	$ (187)	$ 25,235	$ (1,443)	$ 52,562	$ (1,630)

	September 30, 2017					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair value	Unrealized Losses
	(In thousands)					
Investment Securities Available-for-Sale:						

State and municipal obligations	$	$	$ 500	$ (2)	$ 500	$ (2)
Single issuer trust preferred security			934	(66)	934	(66)
Corporate debt securities			6,375	(253)	6,375	(253)
Total	$	$	$ 7,809	$ (321)	$ 7,809	$ (321)
Investment Securities Held-to-Maturity:						
U.S. government agencies			1,991	(8)	1,991	(8)
State and municipal obligations						
Mortgage-backed securities:						
CMO, fixed-rate			18,902	(457)	18,902	(457)
Total			20,893	(465)	20,893	(465)
Total investment securities	$	$	$ 28,702	$ (786)	$ 28,702	$ (786)

As of September 30, 2018, the estimated fair value of the securities disclosed above was primarily dependent upon the movement in market interest rates, particularly given the inherent credit risk associated with these securities. These investment securities are comprised of securities that are rated investment grade by at

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 Investment Securities (Continued)

least one bond credit rating service. Although the fair value will fluctuate as the market interest rates move, management believes that these fair values will recover as the underlying portfolios mature and are reinvested in market rate yielding investments. As of September 30, 2018, the Company held one U.S. government treasury note, two U.S. government agency securities, seventeen municipal bonds, four corporate securities, thirty-seven mortgage-backed securities, and one single issuer trust preferred security which were in an unrealized loss position. As of September 30, 2017, the Company held two municipal bonds, three corporate securities, 36 mortgage-backed securities, two U.S. government agency securities and one single issuer trust preferred security which were in an unrealized loss position. The Company does not intend to sell and expects that it is not more likely than not that it will not be required to sell these securities until such time as the value recovers or the securities mature. Management does not believe any individual unrealized loss as of September 30, 2018 represents other-than-temporary impairment.

Investment securities having a carrying value of approximately $17.9 million and $9.6 million at September 30, 2018 and September 30, 2017, respectively, were pledged to secure public deposits. In addition, investment securities having a carrying value of $3.1 million and $6.2 million were pledged to secure short-term borrowings at September 30, 2018 and September 30, 2017, respectively.

The following table presents information for investment securities at September 30, 2018, based on scheduled maturities. Actual maturities can be expected to differ from scheduled maturities due to prepayment or early call options of the issuer.

	September 30, 2018	
	Amortized Cost	Fair Value
	(In thousands)	
Investment Securities Available-for-Sale:		
Due in one year or less	$ 11,000	$ 10,984
Due after one year through five years	7,405	7,229
Due after five years through ten years	5,944	5,630
Due after ten years	455	455
Total	$ 24,804	$ 24,298
Investment Securities Held-to-Maturity:		
Due in one year or less	$ 1,000	$ 993
Due after one year through five years	999	986
Due after five years through ten years	5,578	5,490
Due after ten years	6,318	6,291
Mortgage-backed securities:		
Collateralized mortgage obligations, fixed-rate	16,197	15,208

Total	$ 30,092	$ 28,968
Total investment securities	$ 54,896	$ 53,266

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 Loans Receivable and Related Allowance for Loan Losses

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

	September 30, 2018	September 30, 2017
	(In thousands)	
Residential mortgage	$ 197,219	$ 192,500
Construction and Development:		
Residential and commercial	37,433	35,622
Land	9,221	18,377
Total Construction and Development	46,654	53,999
Commercial:		
Commercial real estate	493,929	437,760
Farmland	12,066	1,723
Multi-family	45,102	39,768
Other	80,059	74,837
Total Commercial	631,156	554,088
Consumer:		
Home equity lines of credit	14,884	16,509
Second mortgages	18,363	22,480
Other	2,315	2,570
Total Consumer	35,562	41,559
Total loans	910,591	842,146
Deferred loan fees and cost, net	566	590
Allowance for loan losses	(9,021)	(8,405)
Total loans receivable, net	$ 902,136	$ 834,331

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

The following table summarizes the primary classes of the allowance for loan losses, segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of and for the years ended September 30, 2018, 2017 and 2016.

	Year Ended September 30, 2018											
		Construction and Development		Commercial				Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Farmland	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	Tota
	(in thousands)											
wance oan es:												
nning nce	$ 1,004	$ 523	$ 132	$ 3,581	$ 9	$ 224	$ 541	$ 90	$ 402	$ 27	$ 1,872	$ 8,4
ge-offs	(60)			(276)			(45)		(88)	(2)		(4
overies	58			11			4	1	52	7		1
isions	60	(130)	(83)	1,715	57	8	(33)	(9)	(40)	19	(610)	9
ng nce	$ 1,062	$ 393	$ 49	$ 5,031	$ 66	$ 232	$ 467	$ 82	$ 326	$ 51	$ 1,262	$ 9,0
ng nce: vidually uated irment	$	$	$	$ 1,448	$	$	$	$	$ 103	$ 26	$	$ 1,5
ng nce: ctively uated irment	$ 1,062	$ 393	$ 49	$ 3,583	$ 66	$ 232	$ 467	$ 82	$ 223	$ 25	$ 1,262	$ 7,4

ns ivable:											
ng nce	$ 197,219	$ 37,433	$ 9,221	$ 493,929	$ 12,066	$ 45,102	$ 80,059	$ 14,884	$ 18,363	$ 2,315	$ 910,5
ng nce: vidually uated irment	$ 3,148	$	$ 76	$ 17,409	$	$	$	$ 34	$ 635	$ 26	$ 21,3
ng nce: ctively uated irment	$ 194,071	$ 37,433	$ 9,145	$ 476,520	$ 12,066	$ 45,102	$ 80,059	$ 14,850	$ 17,728	$ 2,289	$ 889,2

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

Year Ended September 30, 2017

		Construction and Development		Commercial				Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Farmland	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	Total
						(in thousands)						
lowance r loan sses:												
ginning lance	$ 1,201	$ 199	$ 97	$ 1,874	$	$ 109	$ 158	$ 116	$ 467	$ 34	$ 1,179	$ 5,434
arge-offs									(218)	(5)		(223
coveries	2	90		40			9	18	232	12		403
ovisions	(199)	234	35	1,667	9	115	374	(44)	(79)	(14)	693	2,797
ding lance	$ 1,004	$ 523	$ 132	$ 3,581	$ 9	$ 224	$ 541	$ 90	$ 402	$ 27	$ 1,872	$ 8,405
ding lance: dividually aluated r pairment	$	$	$	$	$	$	$ 109	$	$ 128	$	$	$ 237
ding lance: llectively aluated r pairment	$ 1,004	$ 523	$ 132	$ 3,581	$ 9	$ 224	$ 432	$ 90	$ 274	$ 27	$ 1,872	$ 8,168
ans ceivable:												
ding lance	$ 192,500	$ 35,622	$ 18,377	$ 437,760	$ 1,723	$ 39,768	$ 74,837	$ 16,509	$ 22,480	$ 2,570		$ 842,146
ding lance: dividually	$ 2,262	$	$ 94	$ 555	$	$	$ 243	$ 10	$ 356	$		$ 3,520

aluated r pairment											
ding lance: llectively aluated r pairment	$ 190,238	$ 35,622	$ 18,283	$ 437,205	$ 1,723	$ 39,768	$ 74,594	$ 16,499	$ 22,124	$ 2,570	$ 838,62

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	Year Ended September 30, 2016										
		Construction and Development		Commercial			Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	Total
	(In thousands)										
Allowance for loan losses:											
Beginning balance	$ 1,486	$ 30	$ 35	$ 1,235	$ 104	$ 108	$ 139	$ 761	$ 24	$ 745	$ 4,667
Charge-offs	(9)	(91)		(99)				(291)	(70)		(560)
Recoveries	17	243		3		3	1	100	13		380
Provision	(293)	17	62	735	5	47	(24)	(103)	67	434	947
Ending Balance	$ 1,201	$ 199	$ 97	$ 1,874	$ 109	$ 158	$ 116	$ 467	$ 34	$ 1,179	$ 5,434
Ending balance: individually evaluated for impairment	$	$	$	$	$	$	$	$ 23	$	$	$ 23
Ending balance: collectively evaluated for impairment	$ 1,201	$ 199	$ 97	$ 1,874	$ 109	$ 158	$ 116	$ 444	$ 34	$ 1,179	$ 5,411
Loans receivable:											
Ending balance	$ 209,186	$ 18,579	$ 10,013	$ 231,439	$ 19,515	$ 38,779	$ 19,757	$ 29,204	$ 1,914		$ 578,386
Ending balance:	$ 1,159	$ 109	$	$ 2,039	$	$	$ 74	$ 277	$		$ 3,658

individually evaluated for impairment											
Ending balance: collectively evaluated for impairment	$ 208,027	$ 18,470	$ 10,013	$ 229,400	$ 19,515	$ 38,779	$ 19,683	$ 28,927	$ 1,914		$ 574,728

In assessing the adequacy of the ALLL, it is recognized that the process, methodology and underlying assumptions require a significant degree of judgment. The estimation of credit losses is not precise; the range of factors considered is wide and is significantly dependent upon management s judgment, including the outlook and potential changes in the economic environment. At present, components of the commercial loan segments of the portfolio are new originations and the associated volumes continue to see increased growth. At the same time, historical loss levels have decreased as factors in assessing the portfolio. Any unallocated portion of the allowance reflects management s estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about a borrower s financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

The following table presents impaired loans in portfolio by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary as of September 30, 2018 and 2017.

	Impaired Loans With Specific Allowance		Impaired Loans With No Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
			(In thousands)		
September 30, 2018:					
Residential mortgage	$	$	$ 3,148	$ 3,148	$ 3,337
Construction and Development:					
Land			76	76	76
Commercial:					
Commercial real estate	16,343	1,448	1,066	17,409	17,685
Consumer:					
Home equity lines of credit			34	34	34
Second mortgages	120	103	515	635	730
Other	26	26		26	26
Total impaired loans	$ 16,489	$ 1,577	$ 4,839	$ 21,328	$ 21,888
September 30, 2017:					
Residential mortgage	$	$	$ 2,262	$ 2,262	$ 2,379
Construction and Development:					
Land			94	94	94
Commercial:					
Commercial real estate			555	555	555
Other	243	109		243	243
Consumer:					
Home equity lines of credit			10	10	11
Second mortgages	131	128	225	356	385
Total impaired loans	$ 374	$ 237	$ 3,146	$ 3,520	$ 3,667

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

The following table presents the average recorded investment in impaired loans in portfolio and related interest income recognized year ended September 30, 2018, 2017 and 2016.

	Average Impaired Loans	Interest Income Recognized on Impaired Loans
	(In thousands)	
Year Ended September 30, 2018:		
Residential mortgages	$ 1,833	$ 56
Construction and Development:		
Land	65	5
Commercial:		
Commercial real estate	6,510	245
Other	138	
Consumer:		
Home equity lines of credit	14	
Second mortgages	458	8
Other	1	
Total	$ 9,019	$ 314
Year Ended September 30, 2017:		
Residential mortgages	$ 2,076	$ 52
Construction and Development:		
Residential and commercial	80	4
Land	24	1
Commercial:		
Commercial real estate	932	18
Other	144	2
Consumer:		
Home equity lines of credit	38	
Second mortgages	209	3
Total	$ 3,503	$ 80
Year Ended September 30, 2016:		
Residential mortgages	$ 707	$
Construction and Development:		

Residential and commercial	150		4
Commercial:			
Commercial real estate	1,646		69
Consumer:			
Home equity lines of credit	24		
Second mortgages	214		
Total	$ 2,741	$	73

No additional funds are committed to be advanced in connection with impaired loans.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

The following table presents the classes of the loan portfolio summarized by loans considered to be rated as pass and the categories of special mention, substandard and doubtful within the Company s internal risk rating system as of September 30, 2018 and 2017.

	September 30, 2018				
	Pass	Special Mention	Substandard	Doubtful	Total
	(In thousands)				
Residential mortgage	$ 193,584	$	$ 3,635	$	$ 197,219
Construction and Development:					
Residential and commercial	37,433				37,433
Land	9,146		75		9,221
Commercial:					
Commercial real estate	474,232	949	18,748		493,929
Farmland	12,066				12,066
Multi-family	45,102				45,102
Other	79,902		157		80,059
Consumer:					
Home equity lines of credit	14,707		177		14,884
Second mortgages	17,402	103	858		18,363
Other	2,289		26		2,315
Total	$ 885,863	$ 1,052	$ 23,676	$	$ 910,591

	September 30, 2017				
	Pass	Special Mention	Substandard	Doubtful	Total
	(In thousands)				
Residential mortgage	$ 189,925	$ 114	$ 2,461	$	$ 192,500
Construction and Development:					
Residential and commercial	35,622				35,622
Land	13,207		5,170		18,377
Commercial:					
Commercial real estate	431,336	4,456	1,968		437,760
Farmland	1,723				1,723
Multi-family	39,410	358			39,768
Other	73,935		902		74,837
Consumer:					

Home equity lines of credit	16,399		110		16,509
Second mortgages	21,611	112	757		22,480
Other	2,563	6	1		2,570
Total	$ 825,731	$ 5,046	$ 11,369	$	$ 842,146

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

The following table presents loans on which we are no longer accruing interest by portfolio class at the dates indicated.

	September 30, 2018	September 30, 2017
	(In thousands)	
Residential mortgage	$ 1,817	$ 826
Commercial:		
Commercial real estate	520	
Consumer:		
Home equity lines of credit	34	10
Second mortgages	290	202
Other	26	
Total non-accrual loans	$ 2,687	$ 1,038

Under the Bank s loan policy, once a loan has been placed on non-accrual status, we do not resume interest accruals until the loan has been brought current and has maintained a current payment status for not less than six consecutive months. Interest income that would have been recognized on nonaccrual loans had they been current in accordance with their original terms was approximately $28,000, $32,000 and $48,000 for fiscal 2018, 2017 and 2016, respectively. At September 30, 2018 and 2017 there were approximately $374,000 and $173,000, respectively, loans past due 90 days or more and still accruing interest.

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by whether a loan payment is current, that is, it is received from a borrower by the scheduled due date, or the length of time a scheduled payment is past due. The following table presents the classes of the loan portfolio summarized by the aging categories as of September 30, 2018 and 2017.

	Current	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Total Loans Receivable	Accruing 90 Days or More Past Due
				(in thousands)			
September 30, 2018:							
Residential mortgage	$ 193,727	$ 450	$ 1,016	$ 2,026	$ 3,492	$ 197,219	$ 339
Construction and Development:							

Residential and commercial	37,433					37,433	
Land	9,221					9,221	
Commercial:							
Commercial real estate	485,886	449	7,019	575	8,043	493,929	
Farmland	12,066					12,066	
Multi-family	45,102					45,102	
Other	80,059					80,059	
Consumer:							
Home equity lines of credit	14,815			69	69	14,884	35
Second mortgages	17,928	121	103	211	435	18,363	
Other	2,282	7	1	25	33	2,315	
Total	$ 898,519	$ 1,027	$ 8,139	$ 2,906	$ 12,072	$ 910,591	$ 374

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	Current	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Total Loans Receivable	Accruing 90 Days or More Past Due
				(in thousands)			
September 30, 2017:							
Residential mortgage	$ 189,272	$ 1,442	$ 1,145	$ 641	$ 3,228	$ 192,500	$ 31
Construction and Development:							
Residential and commercial	35,622					35,622	
Land	18,377					18,377	
Commercial:							
Commercial real estate	436,804	160	796		956	437,760	
Farmland	1,723					1,723	
Multi-family	39,768					39,768	
Other	74,837					74,837	
Consumer:							
Home equity lines of credit	16,122	350	37		387	16,509	
Second mortgages	21,183	844	182	271	1,297	22,480	141
Other	2,561	7	1	1	9	2,570	1
Total	$ 836,269	$ 2,803	$ 2,161	$ 913	$ 5,877	$ 842,146	$ 173

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

The Company had eighteen and twelve loans classified as TDRs with an aggregate outstanding balance of $18.9 million and $2.3 million at September 30, 2018 and 2017, respectively. At September 30, 2018, these loans were also classified as impaired. Fifteen of the TDR loans continue to perform under the restructured terms through September 30, 2018 and we continued to accrue interest on such loan through such date. In November 2018, one TDR with an aggregate outstanding balance of approximately $7.0 million ceased to perform under modified terms and as a result the Company is in the process of accepting a deed in lieu.

The increase in TDRs at September 30, 2018 compared to September 30, 2017 was primarily due to two commercial real estate loans with an aggregate outstanding balance of approximately $16.4 million moving to performing TDR status in the second fiscal quarter of 2018. All of such loans have been classified as TDRs since we modified the payment terms and in some cases interest rate from the original agreements and allowed the borrowers, who were

experiencing financial difficulty, to make interest only payments for a period of time in order to relieve some of their overall cash flow burden. Some loan modifications classified as TDRs may not ultimately result in the full collection of principal and interest, as modified, and result in potential incremental losses. These potential incremental losses have been factored into our overall estimate of the allowance for loan losses. The level of any defaults will likely be affected by future economic conditions. A default on a troubled debt restructured loan for purposes of this disclosure occurs when the borrower is 90 days past due or a foreclosure or repossession of the applicable collateral has occurred.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

TDRs may arise in which, due to financial difficulties experienced by the borrower, the Company obtains through physical possession one or more collateral assets in satisfaction of all or part of an existing credit. Once possession is obtained, the Company reclassifies the appropriate portion of the remaining balance of the credit from loans to OREO, which is included within other assets in the Consolidated Statements of Financial Condition. For any residential real estate property collateralizing a consumer mortgage loan, the Company is considered to possess the related collateral only if legal title is obtained upon completion of foreclosure, or the borrower conveys all interest in the residential real estate property to the Company through completion of a deed in lieu of foreclosure or similar legal agreement. Excluding OREO, the Company had $1.4 million and $252,000 of residential real estate properties in the process of foreclosure at September 30, 2018 and 2017, respectively.

	Total Troubled Debt Restructurings	Troubled Debt Restructured Loans That Have Defaulted on Modified Terms Within The Past 12 Months
	Number of Loans	