

CAPITOL FEDERAL FINANCIAL  
Form 10-Q  
May 05, 2009

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

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2009

or

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

Commission file number: 000-25391

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

United States 48-1212142 (I.R.S.  
(State or other jurisdiction of incorporation

Employer

or  
(Identification No.)

organization)

700 Kansas Avenue, Topeka, Kansas 66603  
(Address of principal executive offices) (Zip

Code)

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.) Yes  No

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

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

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

As of April 27, 2009, there were 74,091,055 shares of Capitol Federal Financial Common Stock outstanding.

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

|   | March 31,<br>2009   | September<br>30,<br>2008 |
|---|---------------------|--------------------------|
| <b>ASSETS:</b>  | (Unaudited)         |                          |
| Cash and cash equivalents   | \$ 52,025           | \$ 87,138                |
| Investment securities:  |                     |                          |
| Available-for-sale ("AFS") at market (amortized cost of \$158,556 and \$51,700)   | 156,550             | 49,586                   |
| Held-to-maturity ("HTM") at cost (market value of \$58,889 and \$92,211)  | 57,860              | 92,773                   |
| Mortgage-backed securities ("MBS")  |                     |                          |
| AFS, at market (amortized cost of \$1,490,325 and \$1,491,536)  | 1,531,916           | 1,484,055                |
| HTM, at cost (market value of \$689,454 and \$743,764)  | 672,453             | 750,284                  |
| Loans receivable held-for-sale, net ("LHFS")  | 146,412             | 997                      |
| Loans receivable, net   | 5,377,699           | 5,320,780                |
| Capital stock of Federal Home Loan Bank ("FHLB"), at cost   | 131,278             | 124,406                  |
| Accrued interest receivable   | 32,564              | 33,704                   |
| Premises and equipment, net   | 33,240              | 29,874                   |
| Real estate owned ("REO"), net  | 5,824               | 5,146                    |
| Other assets  | 72,060              | 76,506                   |
| <b>TOTAL ASSETS</b>   | <b>\$ 8,269,881</b> | <b>\$ 8,055,249</b>      |
| <b>LIABILITIES:</b>   |                     |                          |
| Deposits  | \$ 4,116,514        | \$ 3,923,883             |
| Advances from FHLB  | 2,411,560           | 2,447,129                |
| Other borrowings, net   | 713,609             | 713,581                  |
| Advance payments by borrowers for taxes and insurance   | 46,433              | 53,213                   |
| Income taxes payable  | 8,011               | 6,554                    |
| Deferred income tax liabilities, net  | 24,031              | 3,223                    |
| Accounts payable and accrued expenses   | 33,332              | 36,450                   |
| <b>Total liabilities</b>  | <b>7,353,490</b>    | <b>7,184,033</b>         |
| <b>STOCKHOLDERS' EQUITY:</b>  |                     |                          |
| Preferred stock (\$0.01 par value) 50,000,000 shares authorized; none issued  | --                  | --                       |
| Common stock (\$0.01 par value) 450,000,000 shares authorized, 91,512,287 shares issued; 74,091,055 and 74,079,868 shares outstanding as of March 31, 2009 and September 30, 2008, respectively | 915                 | 915                      |
| Additional paid-in capital  | 449,782             | 445,391                  |
| Unearned compensation, Employee Stock Ownership Plan ("ESOP")   | (9,074)             | (10,082)                 |
| Unearned compensation, Recognition and Retention Plan ("RRP")   | (394)               | (553)                    |
| Retained earnings   | 770,186             | 759,375                  |
| Accumulated other comprehensive gain (loss)   | 24,622              | (5,968)                  |
| Less shares held in treasury (17,421,232 and 17,432,419 shares as of March 31, 2009 and September 30, 2008, respectively, at cost)  | (319,646)           | (317,862)                |
| <b>Total stockholders' equity</b>   | <b>916,391</b>      | <b>871,216</b>           |

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY

\$ 8,269,881 \$ 8,055,249

See accompanying notes to consolidated interim financial statements.

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

|   | For the Three Months       |           | For the Six Months Ended |            |
|---|----------------------------|-----------|--------------------------|------------|
|   | Ended<br>March 31,<br>2009 | 2008      | March 31,<br>2009        | 2008       |
| <b>INTEREST AND DIVIDEND INCOME:</b>                                |                            |           |                          |            |
| Loans receivable  | \$ 77,446                  | \$ 75,276 | \$ 154,162               | \$ 151,539 |
| MBS   | 25,088                     | 20,246    | 51,490                   | 37,373     |
| Investment securities   | 955                        | 3,061     | 2,281                    | 7,191      |
| Capital stock of FHLB   | 778                        | 1,864     | 1,558                    | 3,944      |
| Cash and cash equivalents   | 68                         | 1,369     | 117                      | 2,797      |
| Total interest and dividend income                                  | 104,335                    | 101,816   | 209,608                  | 202,844    |
| <b>INTEREST EXPENSE:</b>  |                            |           |                          |            |
| FHLB advances   | 26,653                     | 31,796    | 56,198                   | 65,957     |
| Deposits  | 24,711                     | 35,145    | 51,496                   | 73,178     |
| Other borrowings  | 7,109                      | 3,873     | 14,834                   | 6,080      |
| Total interest expense  | 58,473                     | 70,814    | 122,528                  | 145,215    |
| NET INTEREST AND DIVIDEND INCOME                                    | 45,862                     | 31,002    | 87,080                   | 57,629     |
| PROVISION FOR LOAN LOSSES   | 2,107                      | 119       | 2,656                    | 119        |
| NET INTEREST AND DIVIDEND INCOME<br>AFTER PROVISION FOR LOAN LOSSES | 43,755                     | 30,883    | 84,424                   | 57,510     |
| <b>OTHER INCOME:</b>  |                            |           |                          |            |
| Retail fees and charges   | 4,031                      | 4,095     | 8,561                    | 8,584      |
| Insurance commissions   | 873                        | 697       | 1,364                    | 1,175      |
| Loan fees   | 597                        | 581       | 1,166                    | 1,179      |
| Income from bank-owned life insurance ("BOLI")                      | 241                        | 612       | 625                      | 1,233      |
| Gains on sale of LHFS, net  | 516                        | 180       | 540                      | 257        |
| Other, net  | 678                        | 1,817     | 1,322                    | 2,665      |
| Total other income  | 6,936                      | 7,982     | 13,578                   | 15,093     |
| <b>OTHER EXPENSES:</b>  |                            |           |                          |            |
| Salaries and employee benefits                                      | 10,569                     | 10,273    | 21,732                   | 20,708     |
| Occupancy of premises   | 3,770                      | 3,477     | 7,492                    | 6,634      |
| Advertising   | 1,947                      | 1,386     | 3,689                    | 2,217      |
| Deposit and loan transaction fees                                   | 1,418                      | 1,216     | 2,722                    | 2,571      |
| Regulatory and other services                                       | 980                        | 1,459     | 2,129                    | 3,078      |
| Other, net  | 3,311                      | 3,096     | 6,418                    | 5,150      |
| Total other expenses  | 21,995                     | 20,907    | 44,182                   | 40,358     |
| INCOME BEFORE INCOME TAX EXPENSE                                    | 28,696                     | 17,958    | 53,820                   | 32,245     |
| INCOME TAX EXPENSE  | 10,564                     | 6,231     | 19,836                   | 11,405     |
| NET INCOME  | \$ 18,132                  | \$ 11,727 | \$ 33,984                | \$ 20,840  |
| Basic earnings per common share                                     | \$ 0.25                    | \$ 0.16   | \$ 0.46                  | \$ 0.29    |

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|  |    |        |    |        |    |        |    |        |
|--|----|--------|----|--------|----|--------|----|--------|
| Diluted earnings per common share      | \$ | 0.25   | \$ | 0.16   | \$ | 0.46   | \$ | 0.29   |
| Dividends declared per public share    | \$ | 0.50   | \$ | 0.50   | \$ | 1.11   | \$ | 1.00   |
| Basic weighted average common shares   |    | 73,113 |    | 72,875 |    | 73,088 |    | 72,916 |
| Diluted weighted average common shares |    | 73,175 |    | 72,929 |    | 73,168 |    | 72,973 |

See accompanying notes to consolidated interim financial statements.

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

(Dollars in thousands except per share data and amounts)

|   | Common<br>Stock | Additional<br>Paid-In<br>Capital | Unearned<br>Compensation<br>(ESOP) | Unearned<br>Compensation<br>(RRP) | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Gain<br>(Loss) | Treasury<br>Stock | Total      |
|---|-----------------|----------------------------------|------------------------------------|-----------------------------------|----------------------|---|-------------------|------------|
| Balance at October 1, 2008  | \$ 915          | \$ 445,391                       | \$ (10,082)                        | \$ (553)                          | \$ 759,375           | \$ (5,968)  | \$ (317,862)      | \$ 871,216 |
| Comprehensive income:   |                 |                                  |                                    |                                   |                      |   |                   |            |
| Net income  |                 |                                  |                                    |                                   | 33,984               |   |                   | 33,984     |
| Changes in unrealized gains (losses) on securities available-for-sale, net of deferred income taxes of \$18,588 |                 |                                  |                                    |                                   |                      | 30,590  |                   | 30,590     |
| Total comprehensive income  |                 |                                  |                                    |                                   |                      |   |                   | 64,574     |
| ESOP activity, net  |                 | 3,145                            | 1,008                              |                                   |                      |   |                   | 4,153      |
| RRP activity, net   |                 | 35                               |                                    |                                   |                      |   |                   | 35         |
| Stock based compensation - stock options and RRP  |                 | 150                              |                                    | 159                               |                      |   |                   | 309        |
| Acquisition of treasury stock   |                 |                                  |                                    |                                   |                      |   | (2,426)           | (2,426)    |
| Stock options exercised   |                 | 1,061                            |                                    |                                   |                      |   | 642               | 1,703      |
| Dividends on common stock to public stockholders (\$1.11 per public share)                                      |                 |                                  |                                    |                                   | (23,173)             |   |                   | (23,173)   |
| Balance at March 31, 2009   | \$ 915          | \$ 449,782                       | \$ (9,074)                         | \$ (394)                          | \$ 770,186           | \$ 24,622   | \$ (319,646)      | \$ 916,391 |



See accompanying notes to consolidated interim financial statements.

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CAPITOL FEDERAL FINANCIAL AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)  
(Dollars in thousands)

|   | For the Six Months Ended<br>March 31, |           |
|---|---------------------------------------|-----------|
|   | 2009                                  | 2008      |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                                       |           |
| Net income  | \$ 33,984                             | \$ 20,840 |
| Adjustments to reconcile net income to net cash provided by operating activities:     |                                       |           |
| FHLB stock dividends  | (1,558)                               | (3,944)   |
| Provision for loan losses   | 2,656                                 | 119       |
| Originations of LHFS  | (863)                                 | (15,034)  |
| Proceeds from sales of LHFS   | 31,631                                | 16,409    |
| Amortization and accretion of premiums and discounts on MBS and investment securities | 503                                   | 283       |
| Depreciation and amortization of premises and equipment                               | 2,415                                 | 2,537     |
| Amortization of deferred amounts related to FHLB advances, net                        | 584                                   | --        |
| Common stock committed to be released for allocation - ESOP                           | 4,153                                 | 3,353     |
| Stock based compensation - stock options and RRP                                      | 309                                   | 427       |
| Other, net  | 41                                    | 1,239     |
| Changes in:   |                                       |           |
| Accrued interest receivable   | 1,140                                 | 4,331     |
| Other assets  | 4,665                                 | (792)     |
| Income taxes payable/receivable   | 4,212                                 | 12,392    |
| Accounts payable and accrued expenses   | (4,120)                               | (2,063)   |
| Net cash provided by operating activities   | 79,752                                | 40,097    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                                       |           |
| Proceeds from maturities or calls of investment securities AFS                        | 19,996                                | 99,782    |
| Purchases of investment securities AFS  | (127,151)                             | --        |
| Proceeds from maturities or calls of investment securities HTM                        | 39,600                                | 510,108   |
| Purchases of investment securities HTM  | (3,962)                               | (173,843) |
| Principal collected on MBS AFS  | 119,712                               | 102,075   |
| Purchases of MBS AFS  | (118,469)                             | (810,881) |
| Principal collected on MBS HTM  | 77,870                                | 112,850   |
| Purchases of MBS HTM  | --                                    | (3,389)   |
| Proceeds from the redemption of capital stock of FHLB                                 | 3,688                                 | 27,361    |
| Purchases of capital stock of FHLB  | (9,002)                               | (12,926)  |
| Loan originations, net of principal collected   | (84,890)                              | (29,903)  |
| Loan purchases, net of principal collected  | (155,984)                             | 25,459    |
| Net deferred fee activity   | 490                                   | 235       |
| Purchases of premises and equipment   | (5,838)                               | (1,445)   |
| Proceeds from sales of REO  | 3,273                                 | 2,168     |
| Net cash used in investing activities   | (240,667)                             | (152,349) |

(Continued)



|  | For the Six Months Ended<br>March 31, |                |
|--|---------------------------------------|----------------|
|  | 2009                                  | 2008           |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                       |                                       |                |
| Dividends paid   | (23,173)                              | (20,760)       |
| Deposits, net of withdrawals   | 192,631                               | 98,184         |
| Proceeds from advances/line of credit from FHLB                                    | 1,261,102                             | 300,000        |
| Repayments on advances/line of credit from FHLB                                    | (1,261,102)                           | (500,000)      |
| Deferred prepayment penalty on FHLB advances                                       | (36,153)                              | --             |
| Proceeds from repurchase agreements  | --                                    | 350,000        |
| Change in advance payments by borrowers for taxes and insurance                    | (6,780)                               | (6,488)        |
| Acquisitions of treasury stock   | (2,426)                               | (7,245)        |
| Stock options exercised and excess tax benefits from stock options                 | 1,703                                 | 271            |
| Net cash provided by financing activities  | 125,802                               | 213,962        |
| <b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>                        | <b>(35,113)</b>                       | <b>101,710</b> |
| <b>CASH AND CASH EQUIVALENTS:</b>  |                                       |                |
| Beginning of period  | 87,138                                | 162,791        |
| End of period  | \$ 52,025                             | \$ 264,501     |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>                          |                                       |                |
| Income tax payments, net of refunds  | \$ 15,596                             | \$ 410         |
| Interest payments, net of interest credited to deposits                            | \$ 71,907                             | \$ 70,979      |
| <b>SUPPLEMENTAL DISCLOSURE OF NON-CASH<br/>INVESTING AND FINANCING ACTIVITIES:</b> |                                       |                |
| Loans transferred to REO   | \$ 5,137                              | \$ 2,804       |
| Purchase of security that will settle in a subsequent period                       | \$ 1,002                              | \$ 56,003      |
| Repurchase agreements that will settle in a subsequent period                      | \$ --                                 | \$ (50,000)    |
| Market value change related to fair value hedge:                                   |                                       |                |
| Interest rate swaps hedging FHLB advances  | \$ --                                 | \$ (13,948)    |
| Transfer of loans receivable to LHFS, net  | \$ 175,862                            | \$ --          |

(Concluded)

See accompanying notes to consolidated interim financial statements.

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## Notes to Consolidated Interim Financial Statements (Unaudited)

## 1. Basis of Financial Statement Presentation

The accompanying consolidated financial statements of Capitol Federal Financial (“CFFN”) and subsidiary (the “Company”) have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s 2008 Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”). Interim results are not necessarily indicative of results for a full year.

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

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

## 2. Earnings Per Share (“EPS”)

The Company accounts for the 3,024,574 shares acquired by its ESOP in accordance with Statement of Position (“SOP”) 93-6 and the shares awarded pursuant to its RRP in a manner similar to the ESOP shares. Shares acquired by the ESOP and shares awarded pursuant to the RRP are not considered in the basic average shares outstanding until the shares are committed for allocation or vested to an employee’s individual account. The following is a reconciliation of the numerators and denominators of the basic and diluted EPS calculations.

|   | For the Three Months                             |             | For the Six Months Ended |             |
|---|--|-------------|--------------------------|-------------|
|   | Ended<br>March 31,<br>2009(1)                    | 2008(2) (3) | March 31,<br>2009(1)     | 2008(2) (3) |
|   | (Dollars in thousands, except per share amounts) |             |                          |             |
| Net income                                      | \$ 18,132  | \$ 11,727   | \$ 33,984                | \$ 20,840   |
| Average common shares outstanding               | 73,062,516                                       | 72,824,366  | 73,062,425               | 72,890,074  |
| Average committed ESOP shares outstanding       | 50,970   | 50,964      | 25,482                   | 25,618      |
| Total basic average common shares outstanding   | 73,113,486                                       | 72,875,330  | 73,087,907               | 72,915,692  |
| Effect of dilutive RRP shares                   | 4,269  | 2,663       | 6,535                    | 4,457       |
| Effect of dilutive stock options                | 57,074   | 50,953      | 73,628                   | 53,100      |
| Total diluted average common shares outstanding | 73,174,829                                       | 72,928,946  | 73,168,070               | 72,973,249  |

|          |    |      |    |      |    |      |    |      |
|----------|----|------|----|------|----|------|----|------|
| Net EPS: |    |      |    |      |    |      |    |      |
| Basic    | \$ | 0.25 | \$ | 0.16 | \$ | 0.46 | \$ | 0.29 |
| Diluted  | \$ | 0.25 | \$ | 0.16 | \$ | 0.46 | \$ | 0.29 |

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(1) Options to purchase 55,800 shares of common stock at prices between \$38.77 per share and \$43.46 per share were outstanding as of March 31, 2009, but were not included in the computation of diluted EPS because they were anti-dilutive for the three and six months ended March 31, 2009.

(2) Options to purchase 217,800 shares of common stock at prices between \$32.13 per share and \$38.77 were outstanding as of March 31, 2008, but were not included in the computation of diluted EPS because they were anti-dilutive for the three and six months ended March 31, 2008.

(3) At March 31, 2008, there were 6,000 unvested RRP shares at \$32.30 per share that were excluded from the computation of diluted EPS because they were anti-dilutive for the three months and the six months ended March 31, 2008.

### 3. Fair Value Measurements

Effective October 1, 2008, the Company adopted Statement of Financial Accounting Standards (“SFAS”) No. 157 “Fair Value Measurements” which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The statement applies whenever other standards require or permit assets or liabilities to be measured at fair value. The statement does not require new fair value measurements, but rather provides a definition and framework for measuring fair value which will result in greater consistency and comparability among financial statements prepared under GAAP. The Company’s adoption of SFAS No. 157 did not have a material impact on its financial condition or results of operations. The following disclosures, which include certain disclosures which are generally not required in interim period financial statements, are included herein as a result of the Company’s adoption of SFAS No. 157.

The Company uses fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. The Company did not have any liabilities that were measured at fair value at March 31, 2009. The Company’s AFS securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets or liabilities on a non-recurring basis, such as REO, loans held-for-sale, and impaired loans. These non-recurring fair value adjustments involve the application of lower-of-cost-or-fair value accounting or write-downs of individual assets.

In accordance with SFAS No. 157, the Company groups its assets at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value. These levels are:

- Level 1 — Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 — Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 — Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company’s own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques. The results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability.





The Company bases its fair values on the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. SFAS No. 157 requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

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

#### AFS Securities

The Company's AFS securities portfolio is carried at estimated fair value on a recurring basis, with any unrealized gains and losses, net of taxes, reported as accumulated other comprehensive income/loss in stockholders' equity. Substantially all of the securities within the AFS portfolio consist of MBS and investment securities issued by U.S. Government sponsored enterprises or agencies. The fair values for all the AFS securities are obtained from independent nationally recognized pricing services. Various modeling techniques are used to determine pricing for the Company's MBS and investment securities, including option pricing and discounted cash flow models. The inputs to these models may include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, benchmark securities, bids, offers and reference data. There are some AFS securities in the AFS portfolio that have significant unobservable input requiring the independent pricing services to use some judgment in pricing the related securities. These AFS securities are classified as Level 3. All other AFS securities are classified as Level 2.

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

|                        | Carrying Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) (1) |
|------------------------|----------------|--|---|---|
| (Dollars in thousands) |                |  |   |   |
| AFS securities:        |                |  |   |   |
| Investment securities  | \$ 156,550     | \$ --  | \$ 154,728                                    | \$ 1,822                                      |
| MBS                    | 1,531,916      | --   | 1,531,916                                     | --  |
|                        | \$ 1,688,466   | \$ --  | \$ 1,686,644                                  | \$ 1,822                                      |

(1) The Company's Level 3 AFS securities were immaterial as of March 31, 2009 and had no material activity during the period ended March 31, 2009.

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

#### Loans Receivable

Loans which meet certain criteria are evaluated individually for impairment. A loan is considered impaired when, based upon current information and events, it is probable the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. Substantially all of the Bank's impaired loans at March 31, 2009 are secured by real estate. These impaired loans are individually assessed to determine that the carrying value of the loan is not in excess of the fair value of the collateral, less estimated selling costs. Fair value is estimated through current appraisals, real estate brokers or listing prices. Fair values may be adjusted by management to reflect current economic and market conditions and, as such, are classified as Level 3. Impaired loans at March 31, 2009 were \$22.7 million. Based on this evaluation, the Company maintains an

allowance for loan losses of \$2.7 million at March 31, 2009 for such impaired loans.

REO, net

REO represents real estate acquired as a result of foreclosure or by deed in lieu of foreclosure and is carried at the lower of cost or fair value less estimated selling costs. Fair value is estimated through current appraisals, real estate brokers or listing prices. As these properties are actively marketed, estimated fair values may be adjusted by management to reflect current economic and market conditions and, as such, are classified as Level 3. REO at March 31, 2009 was \$5.8 million. During the quarter and six months ended March 31, 2009, charge-offs to the allowance for loan losses related to loans that were transferred to REO were \$607 thousand and \$697 thousand, respectively. Write downs related to REO that were charged to other expense were \$396 thousand and \$640 thousand for the quarter and six months ended March 31, 2009.

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

|                | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
|----------------|--|---|--|
|                | (Dollars in thousands)   |   |  |
| Impaired loans | \$ --  | \$ --   | \$ 22,665  |
| REO, net       | --   | --  | 5,824  |
|                | \$ --  | \$ --   | \$ 28,489  |

#### 4. FHLB Advances

During the quarter ended March 31, 2009, the Bank prepaid \$575.0 million of fixed-rate FHLB advances with a weighted average interest rate of 6.35% and a weighted average remaining term to maturity of 15 months. The prepaid FHLB advances were replaced with \$575.0 million of fixed-rate FHLB advances, with a weighted average contractual interest rate of 3.70% and an average term of 65 months. This 265 basis point decrease in the contractual interest rate resulted in a \$4.9 million decrease in FHLB interest expense for the quarter ended March 31, 2009 compared to the quarter ended March 31, 2008. The Bank paid a \$36.2 million prepayment penalty to the FHLB as a result of prepaying the FHLB advances. In accordance with Emerging Issues Task Force ("EITF") 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments", the prepayment penalty was deferred as an adjustment to the carrying value of the new advances since the new FHLB advances were not "substantially different," as defined within EITF 96-19, from the prepaid FHLB advances. The present value of the cash flows under the terms of the new FHLB advances was not more than 10% different from the present value of the cash flows under the terms of the prepaid FHLB advances (including the prepayment penalty) and there were no embedded conversion options in the prepaid FHLB advances or in the new FHLB advances. The deferred prepayment penalty will be recognized in interest expense over the life of the new FHLB advances. The following table presents the face value of FHLB advances and the maturities and rates for all FHLB advances outstanding at March 31, 2009.

| Maturity by fiscal year | FHLB<br>Advances<br>Amount | Weighted<br>Average<br>Contractual<br>Rate | Weighted<br>Average<br>Effective<br>Rate |
|-------------------------|----------------------------|--|--|
|                         | (Dollars in thousands)     |  |  |
| 2009                    | \$ 320,000                 | 4.37%                                      | 4.37%                                    |
| 2010                    | 350,000                    | 4.49                                       | 4.49                                     |
| 2011                    | 276,000                    | 4.87                                       | 4.87                                     |
| 2012                    | 350,000                    | 3.35                                       | 3.35                                     |
| 2013                    | 525,000                    | 3.72                                       | 4.06                                     |
| Thereafter              | 625,000                    | 3.68                                       | 4.63                                     |
| Total                   | \$ 2,446,000               | 3.98%                                      | 4.30%                                    |

## 5. Recent Accounting Pronouncements

In January 2009, the Financial Accounting Standards Board (“FASB”) issued Staff Position (“FSP”) EITF 99-20-1, “Amendments to the Impairment Guidance of EITF Issue No. 99-20.” FSP EITF 99-20-1 eliminates the requirement that a security holder’s best estimate of cash flows be based upon those that “a market participant” would use. Instead, an other-than-temporary impairment (“OTTI”) should be recognized as a realized loss through earnings when it is probable there has been an adverse change in the security holder’s estimated cash flows from previous projections. This treatment is consistent with the impairment model in SFAS No. 115 “Accounting for Certain Investments in Debt and Equity Securities.” FSP EITF 99-20-1 was effective for the Company for the period ending December 31, 2008, and did not have a material impact on the Company’s financial condition or results of operations.

In April 2009, the FASB issued FSP FAS 157-4, “Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly.” FSP FAS 157-4 provides additional guidance on valuation techniques for estimating the fair value of assets or liabilities in accordance with SFAS No. 157 “Fair Value Measurements” when there has been a significant decrease in volume and level of market activity. The FSP also provides guidance on identifying circumstances that indicate a transaction is not orderly. As part of the judgment involved with estimating fair value, the entity will need to determine which valuation technique or techniques are the most appropriate, and, within those techniques, which results are “most representative” of fair value under market conditions. The FSP emphasizes that the notion of exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions remains unchanged. FSP FAS 157-4 is effective for interim reporting periods after June 15, 2009, which is June 30, 2009 for the Company. The FSP is not expected to have a material impact on the Company’s financial condition or results of operations.

In April 2009, the FASB issued FSP FAS 115-2, “Recognition and Presentation of Other-Than-Temporary Impairments.” FSP FAS 115-2 amends existing OTTI guidance for debt securities by requiring the recognition of an OTTI if an entity has the intent to sell an impaired debt security, it is more likely than not the entity will be required to sell the debt security before recovery, or if the entity does not expect to recover the entire amortized cost basis of the debt security. The FSP also expands and increases the frequency of existing disclosures requirements of SFAS 115, “Accounting for Certain Investments in Debt and Equity Securities.” FSP FAS 115-2 is effective for interim reporting periods after June 15, 2009, which is June 30, 2009 for the Company. FSP FAS 115-2 will affect certain interim reporting disclosures, but is not expected to have a material impact on the Company’s financial condition or results of operations.

In April 2009, the FASB issued FSP FAS 107-1 and Accounting Principles Board (“APB”) Opinion No. 28-1, “Interim Disclosures About Fair Value of Financial Instruments” which amends SFAS No. 107, “Disclosures about Fair Value of Financial Instruments” and APB No. 28, “Interim Financial Reporting” to require publicly traded companies to include fair value disclosures of its financial instruments whenever it issues summarized financial information for interim reporting periods. The FSP also requires entities to disclose the methods and significant assumptions used to estimate the fair value of financial instruments, and to disclose significant changes in methods or assumptions used to estimate fair values. FSP FAS 107-1 and APB 28-1 is effective for interim reporting periods after June 15, 2009, which is June 30, 2009 for the Company. The FSP will affect certain interim reporting disclosures, but is not expected to have a material impact on the Company’s financial condition or results of operations.

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

The Company and its wholly-owned subsidiary, the Bank, may from time to time make written or oral “forward-looking statements,” including statements contained in the Company’s filings with the SEC. These

forward-looking statements may be included in this Quarterly Report on Form 10-Q and the exhibits attached to it, in the Company's reports to stockholders and in other communications by the Company, which are made in good faith by us pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995.

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

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

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

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

The following discussion and analysis is intended to assist in understanding the financial condition and results of operations of the Company. It should be read in conjunction with the consolidated financial statements and notes presented in this report. The discussion includes comments relating to the Bank, since the Bank is wholly owned by the Company and comprises the majority of its assets and is the principal source of income for the Company. This discussion and analysis should be read in conjunction with the management discussion and analysis included in the Company’s 2008 Annual Report on Form 10-K filed with the SEC.



## Executive Summary

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

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

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

The Company's results of operations are primarily dependent on net interest income, which is the difference between the interest earned on loans, MBS, investment securities, and cash, and the interest paid on deposits and borrowings. Net interest income is affected by the shape of the market yield curve, the re-pricing of interest-earning assets and interest-bearing liabilities on our balance sheet, and the prepayment rate on our loans and MBS as it relates to reinvestment opportunities. On a weekly basis, management reviews deposit flows, loan demand, cash levels, and changes in several market rates to assess all pricing strategies. We generally price our loan and deposit products based upon an analysis of our competition and changes in market rates. The Bank generally prices its first mortgage loan products based upon prices available in the secondary market while considering the demand for our products and our ability to service customers in a timely manner. Generally, deposit pricing is based upon a survey of peers in the Bank's market areas, and the need to attract funding and retain maturing deposits. The majority of our loans are fixed-rate products with maturities up to 30 years, while the majority of our deposits have maturity or reprice dates of less than two years.

During fiscal year 2009, the financial services industry and the economy as a whole continued to experience turmoil in the wake of steep declines in credit quality and asset quality due largely to real estate devaluations and an increase in unemployment caused by the ongoing economic recession. The Bank has not experienced the same magnitude of adverse operational impacts felt by many financial institutions. However, we are not immune to negative consequences arising from the overall economic weakness and sharp downturn in the housing and real estate markets nationally. We have experienced an increase in the balance of non-performing loans, but the balance of our non-performing loans continues to remain at low levels relative to the size of our loan portfolio. During the current quarter, we modified our allowance for loan loss methodology in response to the continued deterioration of the housing and real estate markets, the increasing weakness in the overall economy, and the trends and composition of our delinquent and non-performing loans and losses on foreclosed property transactions, primarily related to purchased loans. As a result of the change in our allowance for loan loss methodology and charge-offs, primarily related to purchased loans, a \$2.1 million provision for loan loss was recorded during the current quarter.

During late December 2008 and continuing into the second quarter of fiscal year 2009, mortgage rates declined to record lows in response to the Federal Reserve's purchases of U.S. agency debt and MBS. The decline in mortgage



rates has spurred an increased demand for our loan modification program and mortgage refinances. Our loan modification program allows existing loan customers, whose loans have not been sold to third parties and who have been current on their contractual loan payments for the previous 12 months, the opportunity to modify their original loan terms to current loan terms being offered. The volume and magnitude of these loan modifications and refinances will likely have a negative impact on our net interest margin in future periods as a result of loans repricing to lower market interest rates. During the quarter ended March 31, 2009 we modified \$568.5 million and refinanced \$92.0 million of our originated loans. The weighted average interest rate reduction for the modified loans is approximately 88 basis points. To help mitigate the impact to net interest income and interest rate risk as a result of loan modifications, the Bank sold \$30.1 million of modified loans during the current quarter. The Bank is retaining the servicing on the sold modified loans. These modified loans are being sold on a bulk basis, and based upon past experience, we do not expect all modified loans held-for-sale as of the balance sheet date to be purchased

by the investor. Loans not purchased by the investor will be transferred back to the loans receivable portfolio at the lower of cost or market. Additionally, the Bank refinanced \$575.0 million of FHLB advances during the quarter also in an effort to mitigate the net interest income impact of loan modifications and refinances and to extend maturities. As a result of refinancing the FHLB advances, the Bank was able lower its FHLB advance effective interest rate 118 basis points at the time of the refinance. See additional discussion regarding the FHLB advance refinance in “Notes to Financial Statements-- Note 4 – FHLB Advances.”

The Bank continues to maintain access to liquidity in excess of forecasted needs by diversifying its funding sources and maintaining a strong retail oriented deposit portfolio. We believe the turmoil in the credit and equity markets has made deposit products in strong financial institutions desirable for many customers. We also believe that our strong capital position (the Bank’s tangible equity ratio at March 31, 2009 was 10%), lending policies, and underwriting standards have helped position us to withstand these adverse economic conditions. In addition, the investments of the Bank are government-agency backed securities which are highly liquid and have not been credit impaired, and are therefore available as collateral for additional borrowings or for sale if the need or unforeseen conditions warrant. See additional discussion regarding liquidity in the section entitled “Liquidity and Capital Resources.”

In fiscal year 2009, the Bank has opened two branches and has plans to open two additional branches in our Kansas City market area. The Bank has preliminary plans to open three additional branches in our market areas in Kansas City and Wichita during fiscal year 2010.

#### Available Information

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

#### Critical Accounting Policies

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

**Allowance for Loan Losses.** Management maintains an allowance for loan losses to absorb known and inherent losses in the loan portfolio based upon ongoing quarterly assessments of the loan portfolio. Our methodology for assessing the appropriateness of the allowance for loan losses consists of a formula analysis for general valuation allowances and specific valuation allowances for identified problem loans and portfolio segments. The allowance for loan losses is maintained through provisions for loan losses which are charged to income. The provision for loan losses is established after considering the results of management’s quarterly assessment of the allowance for loan losses.

All loans that are not impaired, as defined in SFAS No. 114, “Accounting by Creditors for Impairment of a Loan, an Amendment of FASB Statements No. 5 and 15” and No. 118 “Accounting by Creditors for Impairment of a Loan – Income Recognition and Disclosures, an Amendment of FASB Statement No. 114,” are included in a formula analysis,

as permitted by SFAS No. 5, "Accounting for Contingencies." Each quarter, the loan portfolio is segregated into categories in the formula analysis based upon certain risk characteristics such as loan type (one- to four-family, multi-family, etc.), interest payments (fixed-rate, adjustable-rate), loan source (originated or purchased), and payment status (i.e. current or number of days delinquent). Loss factors are assigned to each category in the formula analysis based on management's assessment of the potential risk inherent in each category. The greater the risks associated with a particular category, the higher the loss factor. Loss factors increase as individual loans become classified, delinquent, the foreclosure process begins or as economic and market conditions and trends warrant.

The loss factors applied in the formula analysis are periodically reviewed by management to assess whether the factors adequately cover probable and estimable losses inherent in the loan portfolio. The review considers such

factors as the trends and composition of delinquent and non-performing loans, the results of foreclosed property transactions, and the status and trends of the local and national economies and housing markets. Our allowance for loan loss methodology permits modifications to any loss factor used in the computation of the formula analysis in the event that, in management's judgment, significant factors which affect the collectibility of the portfolio or any category of the loan portfolio, as of the evaluation date, are not reflected in the current loss factors. Management's evaluation of the inherent loss with respect to these conditions is subject to a higher degree of uncertainty because they are not identified with a specific problem loan or portfolio segments. As such, the amounts actually observed with respect to these losses can vary significantly from the estimated amounts. By assessing the estimated losses inherent in our loan portfolio on a quarterly basis, management can adjust specific and inherent loss estimates based upon more current information.

The Bank has been experiencing an increase in delinquencies, non-performing loans, net loan charge-offs and losses on foreclosed property transactions, primarily on purchased loans, as a result of the decline in housing and real estate markets, as well as the ongoing economic recession. Management's current quarter analysis of delinquency and non-performing loan trends, results of foreclosed property transactions and current status and trends of the local and national economies and housing markets indicated differences in the performance and loss experience, with respect to the ultimate disposition of the underlying collateral, of our originated and purchased loan portfolios. As a result of the analysis, loss factors on 30-89 day delinquent loans were modified based upon whether the loan is an originated or purchased loan. Based upon our experience with delinquent purchased loans, the loss factor for purchased loans is higher than that of originated loans. Management believes this modification to the formula analysis will result in a more accurate estimate of the inherent losses in the 30-89 day delinquent loan portfolio. Additionally, the real estate market factors used to calculate current loan-to-value ("LTV") ratios in the formula analysis were adjusted as a result of management's analysis. The real estate market factors used in the formula analysis are now based upon a nationally recognized source of indices that management believes will more accurately reflect the current market value of the underlying collateral and therefore allocate loans to a more appropriate LTV category in the formula analysis.

Specific valuation allowances are established in connection with individual loan reviews of specifically identified problem loans and the asset classification process, including the procedures for impairment recognition under SFAS No. 114 and SFAS No. 118. Evaluations of loans for which full collectability is not reasonably assured include evaluation of the estimated fair value of the underlying collateral based upon current appraisals, real estate broker values or listing prices. Additionally, trends and composition of non-performing loans, results of foreclosed property transactions and current status and trends in economic and market conditions are also evaluated. During management's current quarter analysis of the results of foreclosed property transactions and the current status and trends of national housing markets, it was noted that the updated estimated fair values obtained from loan servicers when a loan became 90 days delinquent were not always an accurate representation of the fair value of the collateral once it was sold. The decline in fair value between the date the loan became 90 days delinquent and the time the property was sold was due to the continued decline in real estate values between those points in time, as it often takes several months for a loan to work through the foreclosure process. As a result of the analysis, management applied market value adjustments to non-performing purchased loans at March 31, 2009 to more accurately estimate the fair values of the underlying collateral based upon recent trends. The adjustments were determined based upon the location of the underlying collateral, losses recognized on foreclosed property transactions and trends of non-performing purchased loans entering REO. Specific valuations on non-performing loans were established if the adjusted estimated fair value was less than the current loan balance. Management intends to evaluate the appropriateness of the market value adjustments each quarter. The market value adjustments will continue to be applied to non-performing loans until the real estate markets and economy improve to such a level that the adjustments are no longer necessary.

Loans with an outstanding balance of \$1.5 million or more are reviewed annually if secured by property in one of the following categories: multi-family (five or more units) property, unimproved land, other improved commercial property, acquisition and development of land projects, developed building lots, office building, single-use building,

or retail building. Specific valuation allowances are established if the individual loan review determines a quantifiable impairment.

Management considers quantitative and qualitative factors when determining the appropriateness of the allowance for loan losses. Such factors include changes in underwriting standards, the trend and composition of delinquent and non-performing loans, results of foreclosed property transactions, historical charge-offs, the current status and trends of local and national economies and housing markets, changes in interest rates, and loan portfolio growth and concentrations. Our allowance for loan loss methodology is applied in a consistent manner; however, the methodology can be modified in response to changing conditions. The allowance for loan losses increased \$1.4 million from \$6.1 million at December 31, 2008 to \$7.5 million at March 31, 2009, primarily due to the modification to the formula analysis and application of market value adjustments on non-performing purchased loans as discussed above. During the current quarter, a provision for loan loss of \$2.1 million was recorded as a

result of the modifications to our allowance for loan loss methodology and current quarter charge-offs, primarily on purchased loans.

Assessing the adequacy of the allowance for loan losses is inherently subjective. Actual results could differ from our estimates as a result of changes in economic or market conditions. Changes in estimates could result in a material change in the allowance for loan losses. In the opinion of management, the allowance for loan losses, when taken as a whole, is adequate to absorb reasonable estimated losses inherent in our loan portfolio. However, future adjustments may be necessary if portfolio performance or economic or market conditions differ substantially from the conditions that existed at the time of the initial determinations.

**Securities Impairment.** Management continually monitors the MBS and investment security portfolios for impairment on a security by security basis. Many factors are considered in determining whether the impairment is deemed to be other-than-temporary, including, but not limited to, the nature of the investment, the length of time the security has had a market value less than the cost basis, the cause(s), severity of the loss, the intent and ability of the Bank to hold the security for a period of time sufficient for a substantial recovery of its investment, expectation of an anticipated recovery period, recent events specific to the issuer or industry including the issuer's financial condition and current ability to make future payments in a timely manner, external credit ratings and recent downgrades in such ratings. If management deems the decline to be other-than-temporary, the carrying value of the security is adjusted and an impairment amount is recorded in the consolidated statements of income. At March 31, 2009, no securities had been identified as other-than-temporarily impaired.

#### Financial Condition

Total assets increased from \$8.06 billion at September 30, 2008 to \$8.27 billion at March 31, 2009. The \$214.6 million increase in assets was primarily attributed to a \$202.3 million increase in loans receivable and loans receivable held-for-sale. Total liabilities increased from \$7.18 billion at September 30, 2008 to \$7.35 billion at March 31, 2009. The \$169.5 million increase in liabilities was primarily a result of an increase in deposits of \$192.6 million, primarily in the certificate of deposit and money market portfolios. Stockholders' equity increased \$45.2 million to \$916.4 million at March 31, 2009, from \$871.2 million at September 30, 2008. A large component of this increase was related to an increase in accumulated other comprehensive gain (loss) due to an increase in the market value of AFS securities at March 31, 2009.

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

|  | March 31,<br>2009 | December<br>31,<br>2008 | Balance at<br>September<br>30,<br>2008 | June 30,<br>2008 | March 31,<br>2008 |
|--|-------------------|-------------------------|--|------------------|-------------------|
| (Dollars in thousands, except per share amounts) |                   |                         |  |                  |                   |
| <b>Selected Balance Sheet Data:</b>              |                   |                         |  |                  |                   |
| Total assets                                     | \$ 8,269,881      | \$ 8,157,324            | \$ 8,055,249                           | \$ 7,892,137     | \$ 8,034,662      |
| Cash and cash equivalents                        | 52,025            | 143,134                 | 87,138                                 | 86,437           | 264,501           |
| Investment securities                            | 214,410           | 105,965                 | 142,359                                | 144,346          | 88,597            |
| MBS  | 2,204,369         | 2,176,302               | 2,234,339                              | 2,066,685        | 2,076,766         |
| Loans receivable, net                            | 5,377,699         | 5,456,569               | 5,320,780                              | 5,326,061        | 5,292,866         |
| Capital stock of FHLB                            | 131,278           | 131,230                 | 124,406                                | 129,172          | 129,170           |
| Deposits   | 4,116,514         | 3,867,304               | 3,923,883                              | 3,961,543        | 4,020,966         |

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|  |           |           |           |           |           |
|--|-----------|-----------|-----------|-----------|-----------|
| Advances from FHLB                             | 2,411,560 | 2,596,964 | 2,447,129 | 2,547,294 | 2,547,588 |
| Other borrowings                               | 713,609   | 713,595   | 713,581   | 453,566   | 453,552   |
| Stockholders' equity                           | 916,391   | 897,435   | 871,216   | 863,906   | 869,106   |
| Accumulated other comprehensive gain<br>(loss) | 24,622    | 14,263    | (5,968)   | (5,202)   | 6,215     |
| Equity to total assets at end of period        | 11.1%     | 11.0%     | 10.8%     | 11.0%     | 10.8%     |
| Bank tangible equity ratio                     | 9.9%      | 10.0%     | 10.0%     | 10.0%     | 9.8%      |
| Book value per share                           | \$ 12.52  | \$ 12.27  | \$ 11.93  | \$ 11.84  | \$ 11.92  |

Loans Receivable. The loans receivable portfolio increased \$56.9 million from \$5.32 billion at September 30, 2008 to \$5.38 billion at March 31, 2009. The increase was primarily a result of \$191.6 million of loan purchases from nationwide lenders, partially offset by the transfer of \$175.9 million of modified loans to the LHFS portfolio. The loans purchased from nationwide lenders during fiscal year 2009 had an average credit score of 745 at the time of origination and a current weighted average LTV ratio of 50%. The majority of the loans are seasoned loans and were originated in years outside of the years with peak real estate values and non-traditional underwriting standards. Approximately 80% were originated in 2004 or earlier and approximately 20% were originated in 2008. Additionally, states that have experienced high foreclosure rates were avoided. See additional discussion regarding the underwriting standards for purchased loans in "Lending Practices and Underwriting Standards." Loans purchased from nationwide lenders represented 15% of the loan portfolio at March 31, 2009 compared to 14% at September 30, 2008. As of March 31, 2009, the average balance of a purchased nationwide mortgage loan was approximately \$370 thousand while the average balance of an originated mortgage loan was approximately \$140 thousand.

Included in the loan portfolio at March 31, 2009 were \$303.8 million of interest-only loans, which were primarily purchased from nationwide lenders during fiscal year 2005. These loans do not typically require principal payments during their initial term, and have initial interest-only terms of either five or ten years. At March 31, 2009, \$295.5 million, or 97%, of these loans were still in their interest-only payment term. As of March 31, 2009, \$134.8 million will begin to amortize principal within two years, \$21.0 million will begin amortizing principal within two-to-five years, and the remaining \$139.7 million will begin to amortize principal within five-to-ten years. Loans of this type generally are considered to be of greater risk to the lender because of the possibility that the borrower may default once principal payments are required. The loans had an average credit score of 737 and an average LTV ratio of 80% or less at the time of purchase. The Bank has not purchased any interest-only loans since 2006.



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

|   | For the Three Months Ended<br>March 31, 2009 |       |            | For the Three Months Ended<br>March 31, 2008 |       |            |
|---|--|-------|------------|--|-------|------------|
|   | Amount                                       | Rate  | % of Total | Amount                                       | Rate  | % of Total |
| <b>Fixed-Rate:</b>                              |  |       |            |  |       |            |
| (Dollars in thousands)                          |  |       |            |  |       |            |
| One- to four-family                             |  |       |            |  |       |            |
| <= 15 years                                     | \$ 75,884                                    | 4.82% | 18.70%     | \$ 30,583                                    | 5.30% | 13.16%     |
| > 15 years                                      | 226,148                                      | 5.10  | 55.74      | 141,922                                      | 5.69  | 61.08      |
| Other real estate                               | 5,971  | 6.00  | 1.47       | 300  | 6.75  | 0.13       |
| Consumer  | 2,111  | 7.75  | 0.52       | 4,389  | 7.77  | 1.90       |
| Total fixed-rate                                | 310,114                                      | 5.07  | 76.43      | 177,194                                      | 5.68  | 76.27      |
| <b>Adjustable-Rate:</b>                         |  |       |            |  |       |            |
| One- to four-family                             |  |       |            |  |       |            |
| <= 36 months                                    | 50,448                                       | 4.79  | 12.43      | 8,306  | 5.16  | 3.57       |
| > 36 months                                     | 23,117                                       | 5.16  | 5.70       | 25,070                                       | 5.51  | 10.79      |
| Consumer  | 22,053                                       | 4.81  | 5.44       | 21,775                                       | 6.82  | 9.37       |
| Total adjustable-rate                           | 95,618                                       | 4.88  | 23.57      | 55,151                                       | 5.97  | 23.73      |
| Total originations, refinances<br>and purchases | \$ 405,732                                   | 5.02% | 100.00%    | \$ 232,345                                   | 5.75% | 100.00%    |
| Purchased loans included<br>above:              |  |       |            |  |       |            |
| <b>Fixed-Rate:</b>                              |  |       |            |  |       |            |
| Correspondent                                   | \$ 33,226                                    | 5.18% |            | \$ 10,191                                    | 5.71  |            |
| <b>Adjustable-Rate:</b>                         |  |       |            |  |       |            |
| Correspondent                                   | 4,851  | 5.12  |            | 20,322                                       | 5.51  |            |
| Nationwide                                      | 65,498                                       | 4.89  |            | --   | --    |            |
| Total purchased loans                           | \$ 103,575                                   | 4.99% |            | \$ 30,513                                    | 5.58% |            |

|   | For the Six Months Ended<br>March 31, 2009 |       |            | For the Six Months Ended<br>March 31, 2008 |       |            |
|---|--|-------|------------|--|-------|------------|
|   | Amount                                     | Rate  | % of Total | Amount                                     | Rate  | % of Total |
| (Dollars in thousands)                          |  |       |            |  |       |            |
| <b>Fixed-Rate:</b>                              |  |       |            |  |       |            |
| One- to four-family                             |  |       |            |  |       |            |
| <= 15 years                                     | \$ 103,901                                 | 4.99% | 14.48%     | \$ 57,197                                  | 5.52% | 13.03%     |
| > 15 years                                      | 333,293                                    | 5.32  | 46.45      | 252,043                                    | 5.87  | 57.44      |
| Other real estate                               | 11,936                                     | 5.94  | 1.66       | 300  | 6.75  | 0.07       |
| Consumer  | 5,395                                      | 7.66  | 0.75       | 11,085                                     | 8.17  | 2.53       |
| Total fixed-rate                                | 454,525                                    | 5.29  | 63.34      | 320,625                                    | 5.88  | 73.07      |
| <b>Adjustable-Rate:</b>                         |  |       |            |  |       |            |
| One- to four-family                             |  |       |            |  |       |            |
| <= 36 months                                    | 138,524                                    | 4.92  | 19.30      | 18,046                                     | 5.36  | 4.11       |
| > 36 months                                     | 79,039                                     | 5.27  | 11.01      | 57,709                                     | 5.70  | 13.15      |
| Consumer  | 45,556                                     | 4.95  | 6.35       | 42,430                                     | 7.55  | 9.67       |
| Total adjustable-rate                           | 263,119                                    | 5.03  | 36.66      | 118,185                                    | 6.31  | 26.93      |
| Total originations, refinances<br>and purchases | \$ 717,644                                 | 5.20% | 100.00%    | \$ 438,810                                 | 6.00% | 100.00%    |
| Purchased loans included<br>above:              |  |       |            |  |       |            |
| <b>Fixed-Rate:</b>                              |  |       |            |  |       |            |
| Correspondent                                   | \$ 46,975                                  | 5.36% |            | \$ 22,277                                  | 5.97% |            |
| Nationwide                                      | 256  | 4.38  |            | --   | --    |            |
| <b>Adjustable-Rate:</b>                         |  |       |            |  |       |            |
| Correspondent                                   | 11,100                                     | 5.48  |            | 39,947                                     | 5.68  |            |
| Nationwide                                      | 191,313                                    | 5.00  |            | 155  | 5.38  |            |
| Total purchased loans                           | \$ 249,644                                 | 5.09% |            | \$ 62,379                                  | 5.79% |            |

Loan modification activity is not included in the tables above because a new loan is not generated at the time of modification. During the three and six months ended March 31, 2009, the Bank modified \$568.5 million and \$593.2 million loans, respectively, with a weighted average rate change of 88 basis points and 84 basis points, respectively.

The Bank generally prices its one- to four-family loan products based upon prices available in the secondary market. During the six months ended March 31, 2009, the rate on the Bank's 30-year fixed-rate one- to four-family loans, with no points paid by the borrower, were approximately 250 basis points above the average 10-year Treasury rate, while the rate on the Bank's 15-year fixed-rate one- to four-family loans were approximately 220 basis points above the average 10-year Treasury rate. Even though longer-term market interest rates decreased as a result of the Federal Reserve's purchase of U.S. agency debt and MBS, mortgage interest rates maintained a wider spread relative to U.S. Treasury securities resulting in higher yields on our one- to four-family loans.



The following table summarizes the activity in the loan portfolio for the periods indicated, excluding changes in loans in process, deferred fees and allowance for loan losses. Included in the three and six months ended March 31, 2009 balances are \$92.0 million and \$111.1 million of refinances, respectively. Loans that were paid-off as a result of the refinances are included in 'repayments'. Loan modification activity is not included in the activity in the following table because a new loan is not generated at the time of modification. See modification activity for the three and six months ended March 31, 2009 on the previous page. The modified balance and rate are included in the ending loan portfolio balance and rate.

|                               | March 31, 2009         |       | For the Three Months Ended |                    |               |        |              |       |
|-------------------------------|------------------------|-------|----------------------------|--------------------|---------------|--------|--------------|-------|
|                               | Amount                 | Rate  | December 31, 2008          | September 30, 2008 | June 30, 2008 | Amount | Rate         |       |
|                               | (Dollars in thousands) |       |                            |                    |               |        |              |       |
| Beginning balance             | \$ 5,506,352           | 5.63% | \$ 5,379,845               | 5.66%              | \$ 5,389,901  | 5.63%  | \$ 5,352,278 | 5.66% |
| Originations and refinances   |                        |       |                            |                    |               |        |              |       |
| Fixed                         | 276,888                | 5.06  | 130,406                    | 5.77               | 140,565       | 6.08   | 213,098      | 5.72  |
| Adjustable                    | 25,269                 | 4.83  | 35,437                     | 5.23               | 45,333        | 5.69   | 47,641       | 5.82  |
| Purchases                     |                        |       |                            |                    |               |        |              |       |
| Fixed                         | 33,226                 | 5.18  | 14,005                     | 5.76               | 7,309         | 6.12   | 18,209       | 5.51  |
| Adjustable                    | 70,349                 | 4.90  | 132,064                    | 5.09               | 17,225        | 5.76   | 14,509       | 5.51  |
| Repayments                    | (311,733)              |       | (183,532)                  |                    | (216,090)     |        | (254,784)    |       |
| Transfer of modified loans to |                        |       |                            |                    |               |        |              |       |
| LHFS, net                     | (175,862)              |       | --                         |                    | --            |        | --           |       |
| Other (1)                     | (1,691)                |       | (1,873)                    |                    | (4,398)       |        | (1,050)      |       |
| Ending balance                | \$ 5,422,798           | 5.50% | \$ 5,506,352               | 5.63%              | \$ 5,379,845  | 5.66%  | \$ 5,389,901 | 5.63% |

|                               | For the Six Months Ended |       |                |       |
|-------------------------------|--------------------------|-------|----------------|-------|
|                               | March 31, 2009           |       | March 31, 2008 |       |
|                               | Amount                   | Rate  | Amount         | Rate  |
|                               | (Dollars in thousands)   |       |                |       |
| Beginning balance             | \$ 5,379,845             | 5.66% | \$ 5,346,626   | 5.68% |
| Originations and refinances   |                          |       |                |       |
| Fixed                         | 407,294                  | 5.28  | 298,348        | 5.88  |
| Adjustable                    | 60,706                   | 5.07  | 75,850         | 6.65  |
| Purchases                     |                          |       |                |       |
| Fixed                         | 47,231                   | 5.35  | 22,277         | 5.98  |
| Adjustable                    | 202,413                  | 5.02  | 40,102         | 5.68  |
| Repayments                    | (495,265)                |       | (428,304)      |       |
| Transfer of modified loans to |                          |       |                |       |
| LHFS, net                     | (175,862)                |       | --             |       |
| Other(1)                      | (3,564)                  |       | (2,621)        |       |
| Ending balance                | \$ 5,422,798             | 5.50% | \$ 5,352,278   | 5.66% |

(1) "Other" consists of transfers to REO and net fees advanced.



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

|                              | March 31, 2009 |              |            | December 31, 2008 |              |            | September 30, 2008 |              |            |
|------------------------------|----------------|--------------|------------|-------------------|--------------|------------|--------------------|--------------|------------|
|                              | Amount         | Average Rate | % of Total | Amount            | Average Rate | % of Total | Amount             | Average Rate | % of Total |
| (Dollars in thousands)       |                |              |            |                   |              |            |                    |              |            |
| <b>Real Estate Loans</b>     |                |              |            |                   |              |            |                    |              |            |
| One- to four-family          | \$ 5,085,227   | 5.49%        | 93.77%     | \$ 5,154,113      | 5.60%        | 93.60%     | \$ 5,026,358       | 5.61%        | 93.43%     |
| Multi-family and commercial  | 67,278         | 6.30         | 1.24       | 61,353            | 6.38         | 1.12       | 56,081             | 6.44         | 1.04       |
| Construction and development | 63,823         | 5.28         | 1.18       | 76,601            | 5.59         | 1.39       | 85,178             | 5.66         | 1.58       |
| Total real estate loans      | 5,216,328      | 5.50         | 96.19      | 5,292,067         | 5.61         | 96.11      | 5,167,617          | 5.62         | 96.05      |
| <b>Consumer Loans</b>        |                |              |            |                   |              |            |                    |              |            |
| Savings loans                | 4,524          | 5.65         | 0.08       | 4,497             | 5.79         | 0.08       | 4,634              | 5.95         | 0.09       |
| Automobile                   | 3,083          | 6.96         | 0.06       | 3,307             | 6.97         | 0.06       | 3,484              | 7.00         | 0.07       |
| Home equity                  | 197,939        | 5.67         | 3.65       | 205,409           | 5.97         | 3.73       | 202,956            | 6.53         | 3.77       |
| Other                        | 924            | 8.27         | 0.02       | 1,072             | 7.74         | 0.02       | 1,154              | 7.13         | 0.02       |
| Total consumer loans         | 206,470        | 5.70         | 3.81       | 214,285           | 5.99         | 3.89       | 212,228            | 6.52         | 3.95       |
| Total loans receivable       | 5,422,798      | 5.50%        | 100.00%    | 5,506,352         | 5.63%        | 100.00%    | 5,379,845          | 5.66%        | 100.00%    |
| <b>Less:</b>                 |                |              |            |                   |              |            |                    |              |            |
| Loans in process             | 27,058         |              |            | 33,593            |              |            | 43,186             |              |            |
| Deferred fees and discounts  | 10,577         |              |            | 10,053            |              |            | 10,088             |              |            |
| Allowance for loan losses    | 7,464          |              |            | 6,137             |              |            | 5,791              |              |            |
| Total loans receivable, net  | \$ 5,377,699   |              |            | \$ 5,456,569      |              |            | \$ 5,320,780       |              |            |

## Lending Practices and Underwriting Standards

The Bank's primary lending activity is the origination of loans and the purchase of loans from a select group of correspondent lenders. These loans are generally secured by first mortgages on owner-occupied, one- to four-family residences in the Bank's primary market areas and select market areas in Missouri. The Bank also makes consumer loans, construction loans secured by residential or commercial properties, and multi-family real estate loans secured by multi-family dwellings. Additional lending volume has been generated by purchasing whole one- to four-family mortgage loans from nationwide lenders. By purchasing loans from nationwide lenders, the Bank is able to attain some geographic diversification in its loan portfolio, and help mitigate the Bank's interest rate risk exposure as the purchased loans are predominately adjustable-rate or 15-year fixed-rate loans. As a result of the decline in real estate values and the economic recession, we have experienced an increase in non-performing purchased loans. At the time these loans were purchased, they met our underwriting standards; however, some are located in areas that have recently experienced high unemployment rates and sharp declines in real estate values. See additional discussion regarding non-performing purchased loans in "Critical Accounting Policies – Allowance for Loan Losses" and "Asset Quality." The loans purchased during fiscal year 2009 had an average credit score of 745 and a current weighted average LTV ratio of 50%. See additional discussion regarding loans purchased during fiscal year 2009 in "Financial Condition – Loans Receivable."

The Bank's one- to four-family loans are primarily fully amortizing fixed- or adjustable-rate loans with contractual maturities of up to 30 years, except for interest-only loans which require the payment of interest during the interest-only period, all with payments due monthly. Our one- to four- family loans are generally not assumable and do not contain prepayment penalties. A "due on sale" clause, allowing the Bank to declare the unpaid principal balance due and payable upon the sale of the secured property, is generally included in the security instrument.

Current adjustable-rate one- to four-family loans originated by the Bank generally provide for a specified rate limit or cap on the periodic adjustment to the interest rate, as well as a specified maximum lifetime cap and minimum rate, or floor. As a consequence of using caps, the interest rates on these loans may not be as rate sensitive as our cost of funds. Negative amortization of principal is not allowed. Borrowers are qualified based on the principal, interest, taxes and insurance payments at the initial rate for three, five and seven year adjustable-rate mortgage ("ARM") loans. After the initial three, five or seven year period, the interest rate is repriced annually and the new principal and interest payment is based on the new interest rate, remaining unpaid principal balance and term of the ARM loan. Our ARM loans are not automatically convertible into fixed-rate loans; however, we do allow borrowers to pay a modification fee to convert an ARM loan to a fixed-rate loan. ARM loans can pose different credit risks than fixed-rate loans, primarily because as interest rates rise, the borrower's payment also rises, increasing the potential for default. This specific risk type is known as repricing risk.

During 2008, the Bank discontinued offering an interest-only ARM product, but holds in its portfolio originated and purchased interest-only ARM loans. The product was discontinued to reduce future credit risk exposure. At the time of origination, these loans did not require principal payments for a period of up to ten years. Borrowers were qualified based on a fully amortizing payment at the initial loan rate. The Bank was more restrictive on debt-to-income ratios and credit scores on interest-only ARM loans than on other ARM loans to offset the potential risk of payment shock at the time the loan rate adjusts and/or the principal and interest payments begin. At March 31, 2009, 6% of our loan portfolio consisted of non-amortizing interest-only ARM loans. The majority of these loans were purchased from nationwide lenders during fiscal year 2005. These loans had an initial interest-only term of either five or ten years, with approximately equal distribution between the two terms. At March 31, 2009, \$8.4 million or approximately 40% of non-performing loans were interest-only. Non-performing interest-only loans represent approximately 3% of the total interest-only portfolio at March 31, 2009. See discussion regarding the allowance for loan losses in "Critical Accounting Policies – Allowance for Loan Losses."

One- to four-family loans are generally underwritten using an automated underwriting system developed by a third party. The system's components closely resemble the Bank's manual underwriting standards which are generally in accordance with Federal Home Loan Mortgage Corporation ("FHLMC") and Federal National Mortgage Association ("FNMA") underwriting guidelines. The automated underwriting system analyzes the applicant's data, with emphasis on credit history, employment and income history, qualifying ratios reflecting the applicant's ability to repay, asset reserves, and loan-to-value ratio. Loans that do not meet the automated underwriting standards are referred to a staff underwriter for manual underwriting. Full documentation to support the applicant's credit, income, and sufficient funds to cover all applicable fees and reserves at closing are required on all loans. Properties securing one- to four-family loans are appraised by either staff appraisers or fee appraisers, both of which are independent of the loan origination function and have been approved by the board of directors.

For loans with an LTV ratio in excess of 80% at the time of origination, private mortgage insurance is required in order to reduce the Bank's loss exposure to less than 80% of the appraised value or the purchase price of the property. The Bank will lend up to 97% of the lesser of the appraised value or purchase price for one- to four-family loans provided the Bank is able to



obtain private mortgage insurance. At this time, we believe that our private mortgage insurance counterparties have the ability to meet potential claim obligations we may file in the foreseeable future.

The underwriting standards of the lenders from whom the Bank purchases loans are generally similar to the Bank's internal underwriting standards. "No Doc" or "Stated Income, Stated Assets" loans are not permitted. Lenders are required to fully document all data sources for each application. Management believes these requirements reduce the credit risk associated with these loans. Before committing to purchase a pool of loans from a nationwide lender, the Bank's Chief Lending Officer or Secondary Marketing Manager reviews specific criteria such as loan amount, credit scores, LTV ratios, geographic location, and debt ratios of each loan in the pool. If the specific criteria do not meet the Bank's underwriting standards and compensating factors are not sufficient, then a loan will be removed from the pool. Once the review of the specific criteria is complete and loans not meeting the Bank's standards are removed from the pool, changes are sent back to the lender for acceptance and pricing. Before the pool is funded, an approved Bank underwriter reviews at least 25% of the loan files and the supporting documentation in the pool. Our standard contractual agreement with the lender includes recourse options for any breach of representation or warranty with respect to the loans purchased.

The underwriting of loans purchased through correspondent lenders is generally performed by a third party underwriter who is under contract to use a product description supplied by the Bank that is specific to each correspondent. The products offered by the correspondents are at least as restrictive as the Bank's own internal underwriting standards. Correspondent lenders are located within the metropolitan Kansas City market area and select market areas in Missouri. The Bank purchases approved loans and the related servicing rights, on a loan-by-loan basis.

In an effort to offset the impact of repayments and to retain our customers, the Bank offers existing loan customers whose loans have not been sold to third parties the opportunity to modify their original loan terms to new loan terms generally consistent with those currently being offered. This is a convenient tool for customers who may have considered refinancing from an ARM loan to a fixed-rate loan, would like to reduce their term, or take advantage of lower rates associated with current market rates. The program helps ensure the Bank maintains the relationship with the customer and significantly reduces the amount of effort required for customers to obtain current market pricing and terms without having to refinance their loans. The Bank charges a fee for this service generally comparable to fees charged on new loans. The Bank does not solicit customers for this program, but considers it a valuable opportunity to retain customers who, due to our strict initial underwriting, could likely obtain similar financing elsewhere.

The Bank also originates construction-to-permanent loans primarily secured by one- to four-family residential real estate. Presently, all of the one- to four-family construction loans are secured by property located within the Bank's market areas. Construction loans are obtained primarily by homeowners who will occupy the property when construction is complete. The Bank is also a participant with five other banking institutions on a construction loan secured by a retail shopping center in Kansas with two major retailers. Construction loans to builders for speculative purposes are not permitted. The application process includes submission of complete plans, specifications, and costs of the project to be constructed. These items are used as a basis to determine the appraised value of the subject property. All construction loans are manually underwritten using the Bank's internal underwriting standards. The construction and permanent loans are closed at the same time allowing the borrower to secure the interest rate at the beginning of the construction period and throughout the permanent loan. Construction draw requests and the supporting documentation are reviewed and approved by management. The Bank also performs regular documented inspections of the construction project to ensure the funds are being used for the intended purpose and the project is being completed according to the plans and specifications provided.

The Bank offers a variety of secured consumer loans, including home equity loans and lines of credit, home improvement loans, auto loans, and loans secured by savings deposits. The Bank also originates a very limited amount of unsecured loans. The Bank does not originate any consumer loans on an indirect basis, such as contracts purchased from retailers of goods or services which have extended credit to their customers. All consumer loans are originated in the Bank's market areas. Home equity loans may be originated in amounts, together with the amount of the existing first mortgage, of up to 95% of the value of the property securing the loan. In order to minimize risk of loss, home equity loans that are greater than 80% of the value of the property, when combined with the first mortgage, require private mortgage insurance. The term-to-maturity of home equity and home improvement loans may be up to 20 years. Other home equity lines of credit have no stated term-to-maturity and require a payment of 1.5% of the outstanding loan balance per month. Interest-only home equity lines of credit have a maximum term of 12 months, monthly payments of accrued interest, and a balloon payment at maturity. Repaid principal may be re-advanced at any time, not to exceed the original credit limit of the loan. Other consumer loan terms vary according to the type of collateral and the length of the contract. The majority of the consumer loan portfolio is comprised of home equity lines of credit, which have interest rates that can adjust monthly based upon changes in the prime rate, to a maximum of 18%.

The underwriting standards for consumer loans include a determination of the applicant's payment history on other debts and an assessment of their ability to meet existing obligations and payments on the proposed loan. Although creditworthiness of the

applicant is a primary consideration, the underwriting process also includes a comparison of the value of the security in relation to the proposed loan amount.

Consumer loans generally have shorter terms to maturity or reprice more frequently, which reduces our exposure to changes in interest rates, and usually carry higher rates of interest than do one- to four-family mortgage loans. However, consumer loans may entail greater risk than do one- to four-family mortgage loans, particularly in the case of consumer loans that are secured by rapidly depreciable assets, such as automobiles. Management believes that offering consumer loan products helps to expand and create stronger ties to our existing customer base by increasing the number of customer relationships and providing cross-marketing opportunities.

The Bank's multi-family and commercial real estate loans are secured primarily by multi-family dwellings and small commercial buildings generally located in the Bank's market areas. These loans are granted based on the income producing potential of the property and the financial strength of the borrower. LTV ratios on multi-family and commercial real estate loans usually do not exceed 80% of the appraised value of the property securing the loans. The net operating income, which is the income derived from the operation of the property less all operating expenses, must be sufficient to cover the payments related to the outstanding debt at the time of origination. The Bank generally requires personal guarantees of the borrowers covering a portion of the debt in addition to the security property as collateral for these loans. Appraisals on properties securing these loans are performed by independent state certified fee appraisers approved by the board of directors. Our multi-family and commercial real estate loans are originated with either a fixed or adjustable interest rate. The interest rate on adjustable-rate loans is based on a variety of indices, generally determined through negotiation with the borrower. While maximum maturities may extend to 30 years, these loans frequently have shorter maturities and may not be fully amortizing, requiring balloon payments of unamortized principal at maturity.

Our multi-family and commercial real estate loans are generally large dollar loans and involve a greater degree of credit risk than one- to four-family mortgage loans. Such loans typically involve large balances to single borrowers or groups of related borrowers. Because payments on multi-family and commercial real estate loans are often dependent on the successful operation or management of the properties, repayment of such loans may be subject to adverse conditions in the real estate market or the economy. If the cash flow from the project is reduced, or if leases are not obtained or renewed, the borrower's ability to repay the loan may be impaired. See "Asset Quality – Non-performing Loans."

Loans over \$500 thousand must be underwritten by two Class V underwriters, which is the highest class of underwriter. Any loan greater than \$750 thousand must be approved by the Asset and Liability Management Committee ("ALCO") and loans over \$1.5 million must be approved by the board of directors. For loans requiring ALCO and/or board of directors' approval, lending management is responsible for presenting to the ALCO and/or board of directors information about the creditworthiness of the borrower and the estimated value of the subject property. Information pertaining to the creditworthiness of the borrower generally consists of a summary of the borrower's credit history, employment stability, sources of income, assets, net worth, and debt ratios. The estimated value of the property must be supported by an independent appraisal report prepared in accordance with our appraisal policy.

## Asset Quality

The Bank's traditional underwriting guidelines have provided the Bank with loans of high quality and generally low delinquencies and low levels of non-performing assets compared to national levels. Of particular importance is the complete documentation required for each loan the Bank originates and purchases. This allows the Bank to make an informed credit decision based upon a thorough assessment of the borrower's ability to repay the loan compared to underwriting methodologies that do not require full documentation.

The following matrix shows the balance of one-to-four family mortgage loans cross-referenced by LTV ratio and credit score. The LTV ratios used in the matrix were based on the current loan balance and the most recent bank appraisal available, or the lesser of the purchase price or original appraisal. In most cases, the most recent appraisal was obtained at the time of origination. The LTV ratios based upon appraisals obtained at the time of origination may not necessarily indicate the extent to which we may incur a loss on any given loan that may go into foreclosure as the value of the underlying collateral may have declined since the time of origination. Credit scores were updated in March 2009 for loans originated by the Bank and purchased loans. Management will continue to update credit scores as deemed necessary based upon economic conditions. Per the matrix, the greatest concentration of loans fall into the "751 and above" credit score category and have a LTV ratio of less than 70%. The loans falling into the "less than 660" credit score category and having LTV ratios of more than 80% comprise the lowest concentration. The average LTV ratio of our one-to-four family mortgage loans at March 31, 2009 was approximately 66%.

| LTV ratio     | Less than 660          |            | 661 to 700 |            | 701 to 750   |            | 751 and above |            | Total        |            |
|---------------|------------------------|------------|------------|------------|--------------|------------|---------------|------------|--------------|------------|
|               | Amount                 | % of total | Amount     | % of total | Amount       | % of total | Amount        | % of total | Amount       | % of total |
|               | (Dollars in thousands) |            |            |            |              |            |               |            |              |            |
| Less than 70% | \$ 127,321             | 2.5%       | \$ 148,287 | 2.9%       | \$ 436,622   | 8.6%       | \$ 1,876,381  | 36.9%      | \$ 2,588,611 | 50.9%      |
| 70% to 80%    | 113,590                | 2.2        | 123,483    | 2.4        | 369,389      | 7.3        | 1,133,483     | 22.3       | 1,739,945    | 34.2       |
| More than 80% | 79,085                 | 1.6        | 77,352     | 1.5        | 203,550      | 4.0        | 396,684       | 7.8        | 756,671      | 14.9       |
| Total         | \$ 319,996             | 6.3%       | \$ 349,122 | 6.8%       | \$ 1,009,561 | 19.9%      | \$ 3,406,548  | 67.0%      | \$ 5,085,227 | 100.0%     |

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

|                                    | March 31,<br>2009 |           | December 31,<br>2008 |           | September 30,<br>2008 |           | June 30,<br>2008 |           | March 31,<br>2008 |           |
|------------------------------------|-------------------|-----------|----------------------|-----------|-----------------------|-----------|------------------|-----------|-------------------|-----------|
|                                    | Number            | Amount    | Number               | Amount    | Number                | Amount    | Number           | Amount    | Number            | Amount    |
| (Dollars in thousands)             |                   |           |                      |           |                       |           |                  |           |                   |           |
| <b>Loans 30-89 days delinquent</b> |                   |           |                      |           |                       |           |                  |           |                   |           |
| Originated                         | 157               | \$ 14,120 | 199                  | \$ 15,691 | 179                   | \$ 14,026 | 160              | \$ 12,591 | 146               | \$ 10,552 |
| Purchased                          | 43                | 9,698     | 42                   | 9,359     | 37                    | 7,083     | 33               | 6,621     | 36                | 8,356     |
| <b>Non-performing loans</b>        |                   |           |                      |           |                       |           |                  |           |                   |           |
| Originated                         | 128               | 10,213    | 124                  | 9,607     | 100                   | 6,958     | 90               | 6,555     | 81                | 5,440     |
| Purchased                          | 45                | 12,158    | 32                   | 9,625     | 25                    | 6,708     | 26               | 6,699     | 19                | 4,444     |
| <b>REO</b>                         |                   |           |                      |           |                       |           |                  |           |                   |           |
| Originated                         | 48                | 4,119     | 38                   | 2,833     | 36                    | 2,228     | 31               | 1,274     | 38                | 2,329     |
| Purchased                          | 10                | 1,705     | 6                    | 1,644     | 12                    | 2,918     | 5                | 933       | 2                 | 435       |
| <b>Non-performing assets</b>       |                   |           |                      |           |                       |           |                  |           |                   |           |
| as a percentage of total assets    |                   | 0.34%     |                      | 0.29%     |                       | 0.23%     |                  | 0.20%     |                   | 0.16%     |
| <b>Non-performing loans</b>        |                   |           |                      |           |                       |           |                  |           |                   |           |
| as a percentage of total loans     |                   | 0.42%     |                      | 0.35%     |                       | 0.26%     |                  | 0.25%     |                   | 0.19%     |

Loans 30 to 89 days delinquent increased approximately \$2.7 million from \$21.1 million at September 30, 2008 to \$23.8 million at March 31, 2009. At March 31, 2009, 59% of loans 30 to 89 days delinquent were secured by property located in our market areas and 41% were purchased from nationwide lenders. There is not believed to be a geographic trend associated with our purchased loans 30 to 89 days delinquent. During the past two quarters, on average, approximately 35% of loans that entered the 30 to 89 days delinquent category made their required loan payments and did not go back into the 30-89 day delinquent category or paid off during this time period. During the same time period, on average, approximately 45% of loans that entered the 30 to 89 days delinquent category made a portion of their required loan payments but the loans either stayed in the 30 to 89 day delinquent category because not all required loan payments were made or went back into the 30-89 day delinquent category at some point during the noted time period as the borrower once again became delinquent on their loan payments. Approximately 20% of the loans that entered the 30-89 days delinquent category during the past two quarters progressed to the non-performing loan or REO categories.

Non-performing loans increased \$8.7 million from \$13.7 million at September 30, 2008 to \$22.4 million at March 31, 2009. At March 31, 2009, 46% of non-performing loans were secured by property in our market areas and 54% were purchased from nationwide lenders. There is not believed to be a geographic trend associated with our purchased non-performing loans. The weighted average LTV ratio of non-performing one-to-four family loans at March 31, 2009 was approximately 74% based on the current loan balance and the most recent bank appraisal available, or the

lesser of the purchase price or original appraisal. The increase in non-performing loans reflects the economic recession coupled with the continued deterioration of the housing market. The conditions in the housing market are evidenced by declining house prices, fewer home sales, increasing inventories of houses on the market and an increase in the length of time houses remain on the market. The increase in non-performing loans increased our ratio of non-performing loans to total loans from 0.26% as of September 30, 2008 to 0.42% at March 31, 2009.

At March 31, 2009, non-performing loans with LTV ratios greater than 80% comprised 13% of total non-performing loans. Of these loans, 84% have private mortgage insurance which substantially reduces or eliminates the Bank's exposure to loss. The balance of non-performing loans with LTV ratios greater than 80% with no private mortgage insurance was \$502 thousand at March 31, 2009. At origination, these loans had LTV ratios less than 80%, but as a result of updating the appraisals, the LTV ratios are now in excess of 80%.

Management maintains an allowance for loan losses to absorb known and inherent losses in the loan portfolio based upon ongoing quarterly assessments of the loan portfolio. Our allowance for loan loss methodology considers a number of quantitative and qualitative factors, including the trend and composition of our delinquent and non-performing loans, results of foreclosed property transactions, and the status and trends of the local and national economies and housing markets. See "Critical Accounting Policies – Allowance for Loan Losses." The \$2.1 million provision for loan loss reflects our current quarter change in the allowance for loan loss methodology and accounts for charge-offs during the quarter. Although we believe we have established and maintained the allowance for loan losses at adequate levels, additions may be necessary if future economic or other conditions differ substantially from the current operating environment.

The following table presents the Company's activity for the allowance for loan losses and related ratios at the dates and for the periods indicated.

|  | For the Three Months Ended |                         |                   | For the Six Months Ended |                   |
|--|----------------------------|-------------------------|-------------------|--------------------------|-------------------|
|  | March 31,<br>2009          | December<br>31,<br>2008 | March 31,<br>2008 | March 31,<br>2009        | March 31,<br>2008 |
|  | (Dollars in thousands)     |                         |                   | (Dollars in thousands)   |                   |
| Beginning balance  | \$ 6,137                   | \$ 5,791                | \$ 4,171          | \$ 5,791                 | \$ 4,181          |
| Charge-offs:   |                            |                         |                   |                          |                   |
| One- to four-family loans—originated                             | 12                         | 10                      | 33                | 22                       | 30                |
| One- to four-family loans—purchased                              | 766                        | 182                     | --                | 948                      | --                |
| Multi-family loans   | --                         | --                      | --                | --                       | --                |
| Commercial and other loans                                       | --                         | --                      | --                | --                       | --                |
| Consumer loans   | 2                          | 11                      | 7                 | 13                       | 20                |
| Total charge-offs  | 780                        | 203                     | 40                | 983                      | 50                |
| Recoveries   | --                         | --                      | --                | --                       | --                |
| Provision charged to expense                                     | 2,107                      | 549                     | 119               | 2,656                    | 119               |
| Ending balance   | \$ 7,464                   | \$ 6,137                | \$ 4,250          | \$ 7,464                 | \$ 4,250          |
| Allowance for loan losses to non-performing loans at period end  | 33.36%                     | 31.91%                  | 43.00%            |                          |                   |
| Allowance for loan losses to loans receivable, net at period end | 0.14%                      | 0.11%                   | 0.08%             |                          |                   |

Historically, our charge-offs have been low due to our low level of non-performing loans and the amount of underlying equity in the properties collateralizing one-to-four-family loans. The increase in non-performing purchased loans and the decline in real estate and housing markets have begun to result in higher charge-offs,

specifically related to purchased loans. However, the overall amount of charge-offs has not been significant because of our underwriting standards and the geographic areas in which the Bank lends.



The following table presents the Company's allocation of the allowance for loan losses to each respective loan category at March 31, 2009 and September 30, 2008.

|                                 | At<br>March 31, 2009 |                                  |                | At<br>September 30, 2008           |                      |                                  |                |                                    |
|---------------------------------|----------------------|----------------------------------|----------------|------------------------------------|----------------------|----------------------------------|----------------|------------------------------------|
|                                 | Amount<br>of<br>ALLL | % of<br>ALLL<br>to Total<br>ALLL | Total<br>Loans | % of<br>Loans<br>to Total<br>Loans | Amount<br>of<br>ALLL | % of<br>ALLL<br>to Total<br>ALLL | Total<br>Loans | % of<br>Loans<br>to Total<br>Loans |
| (Dollars in thousands)          |                      |                                  |                |                                    |                      |                                  |                |                                    |
| <b>One- to four-family:</b>     |                      |                                  |                |                                    |                      |                                  |                |                                    |
| Originated                      | \$ 3,351             | 44.9%                            | \$ 4,262,813   | 78.6%                              | \$ 3,076             | 53.2%                            | \$ 4,302,870   | 80.0%                              |
| Purchased                       | 3,695                | 49.5%                            | 822,413        | 15.2%                              | 2,307                | 39.8%                            | 723,488        | 13.5%                              |
| Multi-family and<br>commercial  | 64                   | 0.8%                             | 67,278         | 1.2%                               | 53                   | 0.9%                             | 56,081         | 1.0%                               |
| Construction and<br>development | 36                   | 0.5%                             | 63,823         | 1.2%                               | 41                   | 0.7%                             | 85,178         | 1.6%                               |
| Consumer                        | 318                  | 4.3%                             | 206,471        | 3.8%                               | 314                  | 5.4%                             | 212,228        | 3.9%                               |
|                                 | \$ 7,464             | 100.0%                           | \$ 5,422,798   | 100.0%                             | \$ 5,791             | 100.0%                           | \$ 5,379,845   | 100.0%                             |

Mortgage-Backed Securities. The balance of MBS decreased \$30.0 million from \$2.23 billion at September 30, 2008 to \$2.20 billion at March 31, 2009. The following tables provide a summary of the activity in our portfolio of MBS for the periods presented. The yields and weighted average life (“WAL”) for purchases are presented as recorded at the time of purchase. The yields for the beginning and ending balances are as of the period presented and are generally derived from recent prepayment activity on the securities in the portfolio as of the dates presented. The decrease in the yield at March 31, 2009 compared to September 30, 2008 was due to repricing and to the purchase of securities with yields lower than the overall portfolio. The beginning and ending WAL is the estimated remaining maturity after historical prepayment speeds have been applied. The increase in the WAL at March 31, 2009 compared to September 30, 2008 was due to a projected slowdown in future prepayments during the current quarter.

|  | For the Three Months Ended |       |      |                   |       |      |                    |       |      |               |       |      |
|--|----------------------------|-------|------|-------------------|-------|------|--------------------|-------|------|---------------|-------|------|
|  | March 31, 2009             |       |      | December 31, 2008 |       |      | September 30, 2008 |       |      | June 30, 2008 |       |      |
|  | Amount                     | Yield | WAL  | Amount            | Yield | WAL  | Amount             | Yield | WAL  | Amount        | Yield | WAL  |
|  | (Dollars in thousands)     |       |      |                   |       |      |                    |       |      |               |       |      |
| Beginning balance                      | \$ 2,176,302               | 4.82% | 5.81 | \$ 2,234,339      | 4.82% | 5.05 | \$ 2,066,685       | 4.76% | 4.32 | \$ 2,076,766  | 4.70% | 4.88 |
| Maturities and payments                | (107,388)                  |       |      | (90,194)          |       |      | (112,777)          |       |      | (172,376)     |       |      |
| Net amortization of premiums/discounts | 46                         |       |      | 27                |       |      | 23                 |       |      | (9)           |       |      |
| Purchases:                             |                            |       |      |                   |       |      |                    |       |      |               |       |      |
| Fixed                                  | --                         | --    | --   | --                | --    | --   | 60,137             | 5.03  | 4.48 | 129,614       | 4.64  | 4.55 |
| Adjustable                             | 118,469                    | 2.68  | 1.90 | --                | --    | --   | 219,888            | 4.99  | 5.07 | 50,443        | 4.25  | 4.00 |
| Change in valuation                    |                            |       |      |                   |       |      |                    |       |      |               |       |      |
| AFS securities:                        | 16,940                     |       |      | 32,130            |       |      | 383                |       |      | (17,753)      |       |      |
| Ending balance                         | \$ 2,204,369               | 4.72% | 5.55 | \$ 2,176,302      | 4.82% | 5.81 | \$ 2,234,339       | 4.82% | 5.05 | \$ 2,066,685  | 4.76% | 4.32 |

|  | For the Six Months Ended |       |      |                |       |      |  |
|--|--------------------------|-------|------|----------------|-------|------|--|
|  | March 31, 2009           |       |      | March 31, 2008 |       |      |  |
|  | Amount                   | Yield | WAL  | Amount         | Yield | WAL  |  |
|  | (Dollars in thousands)   |       |      |                |       |      |  |
| Beginning balance                      | \$ 2,234,339             | 4.82% | 5.05 | \$ 1,414,271   | 4.46% | 4.04 |  |
| Maturities and payments                | (197,582)                |       |      | (214,925)      |       |      |  |
| Net amortization of premiums/discounts | 73                       |       |      | (761)          |       |      |  |
| Purchases:                             |                          |       |      |                |       |      |  |
| Fixed                                  | --                       | --    | --   | 595,430        | 4.99  | 4.64 |  |
| Adjustable                             | 118,469                  | 2.68  | 1.90 | 274,843        | 4.77  | 4.94 |  |
| Change in valuation                    |                          |       |      |                |       |      |  |
| AFS securities:                        | 49,070                   |       |      | 7,908          |       |      |  |
| Ending balance                         | \$ 2,204,369             | 4.72% | 5.55 | \$ 2,076,766   | 4.70% | 4.88 |  |

Investment Securities. Investment securities, which consist primarily of agency bonds (primarily issued by FNMA, FHLMC, or FHLB) and municipal investments, increased \$72.0 million from \$142.4 million at September 30, 2008 to \$214.4 million at March 31, 2009. The following tables provide a summary of the activity of investment securities for the periods presented. The yields for the beginning and ending balances are as of the periods presented. The decrease in the yield at March 31, 2009 compared to September 30, 2008 was a result of calls and/or maturities of securities with yields higher than the overall portfolio yield. The beginning and ending WAL represent the estimated remaining maturity of the securities after projected call dates have been considered, based upon market rates at each date presented. The decrease in the WAL at March 31, 2009 compared to September 30, 2008 was due to issuers of certain securities in the portfolio exercising their option to call the security, to maturing securities, and to purchases of investment securities with WALs shorter than that of the portfolio.

|  | For the Three Months Ended |       |      |                   |       |      |                    |       |      |               |       |       |
|--|----------------------------|-------|------|-------------------|-------|------|--------------------|-------|------|---------------|-------|-------|
|  | March 31, 2009             |       |      | December 31, 2008 |       |      | September 30, 2008 |       |      | June 30, 2008 |       |       |
|  | Amount                     | Yield | WAL  | Amount            | Yield | WAL  | Amount             | Yield | WAL  | Amount        | Yield | WAL   |
|  | (Dollars in thousands)     |       |      |                   |       |      |                    |       |      |               |       |       |
| Beginning balance                      | \$ 105,965                 | 3.34% | 3.64 | \$ 142,359        | 3.94% | 6.06 | \$ 144,346         | 3.94% | 4.45 | \$ 88,597     | 4.48% | 2.78  |
| Maturities and calls                   | (22,168)                   |       |      | (37,428)          |       |      | (119)              |       |      | (4,009)       |       |       |
| Net amortization of premiums/discounts | (329)                      |       |      | (247)             |       |      | (244)              |       |      | (204)         |       |       |
| Purchases:                             |                            |       |      |                   |       |      |                    |       |      |               |       |       |
| Fixed                                  | 131,229                    | 1.62  | 1.04 | 886               | 4.52  | 2.75 | --                 | --    | --   | 56,669        | 3.12  | 1.46  |
| Adjustable                             | --                         | --    | --   | --                | --    | --   | --                 | --    | --   | 3,874         | 6.58  | 28.98 |
| Change in valuation of AFS securities  | (287)                      |       |      | 395               |       |      | (1,624)            |       |      | (581)         |       |       |
| Ending balance                         | \$ 214,410                 | 2.16% | 2.32 | \$ 105,965        | 3.34% | 3.64 | \$ 142,359         | 3.94% | 6.06 | \$ 144,346    | 3.94% | 4.45  |

|  | For the Six Months Ended |       |      |                |       |      |
|--|--------------------------|-------|------|----------------|-------|------|
|  | March 31, 2009           |       |      | March 31, 2008 |       |      |
|  | Amount                   | Yield | WAL  | Amount         | Yield | WAL  |
|  | (Dollars in thousands)   |       |      |                |       |      |
| Beginning balance                      | \$ 142,359               | 3.94% | 6.06 | \$ 524,168     | 4.52% | 1.66 |
| Maturities and calls                   | (59,596)                 |       |      | (609,890)      |       |      |
| Net amortization of premiums/discounts | (576)                    |       |      | 478            |       |      |
| Purchases:                             |                          |       |      |                |       |      |
| Fixed                                  | 132,115                  | 1.64  | 1.05 | 173,843        | 4.23  | 0.94 |
| Adjustable                             | --                       | --    | --   | --             | --    | --   |
| Change in valuation of AFS securities  | 108                      |       |      | (2)            |       |      |
| Ending balance                         | \$ 214,410               | 2.16% | 2.32 | \$ 88,597      | 4.48% | 2.78 |

Liabilities. Total liabilities increased from \$7.18 billion at September 30, 2008 to \$7.35 billion at March 31, 2009. The \$169.5 million increase in liabilities was primarily a result of an increase in deposits of \$192.6 million. The increase in deposits was a result of an increase in certificates, money market, and checking accounts. We believe the turmoil in the credit and equity markets has made deposit products in strong financial institutions, like the Bank, desirable for many customers.

During the current quarter, the Bank prepaid \$575.0 million of fixed-rate FHLB advances with a weighted average contractual rate of 6.35%. The prepaid FHLB advances were replaced with \$575.0 million of fixed-rate FHLB advances with a weighted average contractual interest rate of 3.70%. The Bank paid a \$36.2 million prepayment penalty to the FHLB. The prepayment penalty was deferred as an adjustment to the carrying value of the new advances and will be recognized as expense over the life of the new advances, resulting in an effective rate of 5.05% on the new advances. See additional discussion of the transaction in “Notes to Financial Statements-- Note 4 – FHLB Advances.”

The following table presents the amount, average rate and percentage of total deposits for checking, savings, money market and certificates for the periods presented.

|                        | At<br>March 31, 2009 |                 |               | At<br>December 31, 2008 |                 |               | At<br>September 30, 2008 |                 |               | At<br>June 30, 2008 |                 |               |
|------------------------|----------------------|-----------------|---------------|-------------------------|-----------------|---------------|--------------------------|-----------------|---------------|---------------------|-----------------|---------------|
|                        | Amount               | Average<br>Rate | % of<br>Total | Amount                  | Average<br>Rate | % of<br>Total | Amount                   | Average<br>Rate | % of<br>Total | Amount              | Average<br>Rate | % of<br>Total |
| (Dollars in thousands) |                      |                 |               |                         |                 |               |                          |                 |               |                     |                 |               |
| Checking               | \$ 448,086           | 0.21%           | 10.89%        | \$ 429,170              | 0.21%           | 11.10%        | \$ 400,461               | 0.21%           | 10.21%        | \$ 419,678          | 0.21%           | 10.3%         |
| Savings                | 229,905              | 0.72            | 5.58          | 227,773                 | 0.87            | 5.89          | 232,103                  | 1.51            | 5.91          | 232,807             | 1.64            | 5.8%          |
| Money<br>Market        | 826,488              | 1.04            | 20.08         | 781,832                 | 1.12            | 20.21         | 772,323                  | 1.48            | 19.68         | 811,415             | 1.46            | 20.4%         |
| Certificates           | 2,612,035            | 3.45            | 63.45         | 2,428,529               | 3.64            | 62.80         | 2,518,996                | 3.91            | 64.20         | 2,497,643           | 4.16            | 63.5%         |
| Total<br>Deposits      | \$ 4,116,514         | 2.46%           | 100.00%       | \$ 3,867,304            | 2.59%           | 100.00%       | \$ 3,923,883             | 2.91%           | 100.00%       | \$ 3,961,543        | 3.04%           | 100.0%        |

At March 31, 2009, \$95.9 million of the \$2.61 billion in certificates were brokered deposits, compared to \$180.6 million in brokered deposits at September 30, 2008. The remaining brokered deposits will mature within one year. Management regularly considers brokered deposits as a source of funding, but does not currently consider the cost of this funding source to be balanced with investment opportunities. As of March 31, 2009, \$95.0 million in certificates were public unit deposits, compared to no public unit deposits at September 30, 2008. Management will continue to monitor the wholesale deposit market for attractive opportunities.

Stockholders' Equity. Stockholders' equity increased \$45.2 million from \$871.2 million at September 30, 2008 to \$916.4 million at March 31, 2009. The increase was primarily a result of an increase in unrealized gains on AFS securities of \$30.6 million and net income of \$34.0 million, partially offset by dividends paid of \$23.2 million.

On April 21, 2009, the board of directors approved a dividend of \$0.50 per public share. The dividend will be paid on May 15, 2009 to stockholders of record on May 1, 2009. It is the board of directors' intention to continue to pay regular quarterly dividends of \$0.50 per share for the foreseeable future.

Dividends from the Company are the only source of funds for MHC. It is expected that MHC will waive future dividends except to the extent they are needed to fund its continuing operations. The following table shows the number of shares eligible to receive dividends ("public shares") because of the waiver of dividends by MHC at March 31, 2009. The unvested shares in the ESOP receive cash equal to the dividends paid on the public shares. The cash received is used to repay the annual debt obligation on the loan taken out by the ESOP from the Company at the time of the mutual-to-stock conversion of the Bank to purchase shares for the ESOP. These shares are held in trust for a future employee benefit, and are therefore excluded from the calculation of public shares.

|  |              |
|--|--------------|
| Total voting shares outstanding at September 30, 2008                        | 74,079,868   |
| Treasury stock acquisitions  | (56,063)     |
| RRP grants   | --           |
| Options exercised  | 67,250       |
| Total voting shares outstanding at March 31, 2009                            | 74,091,055   |
| Unvested shares in ESOP  | (1,008,194)  |
| Shares held by MHC   | (52,192,817) |
| Total shares eligible to receive dividends at March 31, 2009 (public shares) | 20,890,044   |

The following table presents quarterly dividends paid in calendar years 2009, 2008, and 2007. The dollar amounts represent dividends paid during the quarter. The actual amount of dividends to be paid during the quarter ending June 30, 2009, as declared on April 21, 2009, will be based upon the number of shares outstanding on the record date of May 1, 2009. All shares outstanding presented in the table below, except for the quarter ending June 30, 2009, are as of the date of record per the dividend declaration. For the purposes of the table below, the number of dividend shares for the quarter ending June 30, 2009 is based upon shares outstanding on April 27, 2009. This does not represent the actual dividend payout, but rather management's estimate of the number of shares eligible to receive the dividend and the total dividend payout as of April 27, 2009.

|   | Calendar Year                                    |            |            |
|---|--|------------|------------|
|   | 2009   | 2008       | 2007       |
|   | (Dollars in thousands, except per share amounts) |            |            |
| <b>Quarter ended March 31</b>             |  |            |            |
| Number of dividend shares                 | 20,874,269                                       | 20,660,510 | 20,520,793 |
| Dividend per share                        | \$ 0.50  | \$ 0.50    | \$ 0.50    |
| Total dividends paid                      | \$ 10,436  | \$ 10,330  | \$ 10,261  |
| <b>Quarter ended June 30</b>              |  |            |            |
| Number of dividend shares                 | 20,890,044                                       | 20,661,660 | 20,673,933 |
| Dividend per share                        | \$ 0.50  | \$ 0.50    | \$ 0.50    |
| Total dividends paid                      | \$ 10,445  | \$ 10,331  | \$ 10,337  |
| <b>Quarter ended September 30</b>         |  |            |            |
| Number of dividend shares                 |  | 20,668,519 | 20,694,333 |
| Dividend per share                        |  | \$ 0.50    | \$ 0.50    |
| Total dividends paid                      |  | \$ 10,334  | \$ 10,347  |
| <b>Quarter ended December 31</b>          |  |            |            |
| Number of dividend shares                 |  | 20,881,157 | 20,860,278 |
| Dividend per share                        |  | \$ 0.50    | \$ 0.50    |
| Total dividends paid                      |  | \$ 10,440  | \$ 10,430  |
| <b>Special year end dividend</b>          |  |            |            |
| Number of dividend shares                 |  | 20,881,157 | --         |
| Dividend per share                        |  | \$ 0.11    | \$ --      |
| Total dividends paid                      |  | \$ 2,297   | \$ --      |
| Calendar year-to-date dividends per share | \$ 1.00  | \$ 2.11    | \$ 2.00    |

#### Analysis of Net Interest Income

Net interest income represents the difference between interest income earned on interest-earning assets, such as mortgage loans, investment securities, and MBS, and interest paid on interest-bearing liabilities, such as deposits, FHLB advances, and other borrowings. Net interest income depends on the balance of interest-earning assets and interest-bearing liabilities, and the interest rates earned or paid on them.

Average Balance Sheet: The following table presents the average balances of our assets, liabilities and stockholders' equity and the related annualized yields and rates on our interest-earning assets and interest-bearing liabilities for the periods indicated and the yield/rate on our interest-earning assets and interest-bearing liabilities at March 31, 2009. Average yields are derived by dividing annualized income by the average balance of the related assets and average rates are derived by dividing annualized expense by the average balance of the related liabilities, for the periods shown. Average outstanding balances are derived from average daily balances, except as noted. The yields and rates include amortization of fees, costs, premiums and discounts which are considered adjustments to yields/rates. Yields on tax-exempt securities were not calculated on a tax-equivalent basis.

|                                       | At<br>March<br>31,<br>2009                          |                | For the Three Months Ended                                |                |  |                |   |                |                |
|---------------------------------------|---|----------------|---|----------------|--|----------------|---|----------------|----------------|
|                                       | March 31, 2009<br>Average<br>Outstanding<br>Balance |                | December 31,<br>2008<br>Average<br>Outstanding<br>Balance |                | September 30,<br>2008<br>Average<br>Outstanding<br>Balance |                | March 31, 2008<br>Average<br>Outstanding<br>Balance |                |                |
|                                       | Yield/<br>Rate                                      | Yield/<br>Rate | Yield/<br>Rate  | Yield/<br>Rate | Yield/<br>Rate   | Yield/<br>Rate | Yield/<br>Rate                                      | Yield/<br>Rate | Yield/<br>Rate |
| Assets:                               |   |                |   |                |  |                |   |                |                |
| Interest-earning assets:              |   |                |   |                |  |                |   |                |                |
| Loans receivable                      |   |                |   |                |  |                |   |                |                |
| (1)                                   | 5.54%   | \$ 5,485,551   | 5.65%   | \$ 5,419,179   | 5.66%  | \$ 5,328,776   | 5.69%   | \$ 5,306,797   | 5.67%          |
| MBS(2)                                | 4.72  | 2,120,481      | 4.73  | 2,201,531      | 4.80   | 2,192,268      | 4.77  | 1,756,593      | 4.61           |
| Investment securities(2)              | 2.16  | 125,932        | 3.03  | 136,295        | 3.89   | 144,718        | 3.95  | 304,470        | 4.02           |
| Capital stock of FHLB                 | 2.39  | 130,574        | 2.42  | 124,958        | 2.48   | 124,365        | 4.72  | 130,752        | 5.73           |
| Cash and cash equivalents             | 0.24  | 103,768        | 0.26  | 33,025         | 0.58   | 59,351         | 1.92  | 171,356        | 3.16           |
| Total interest-earning assets (1) (2) | 5.10  | 7,966,306      | 5.24  | 7,914,988      | 5.32   | 7,849,478      | 5.36  | 7,669,968      | 5.31           |
| Other noninterest-earning assets      |   | 201,462        |   | 161,092        |  | 151,695        |   | 202,741        |                |
| Total assets                          |   | \$ 8,167,768   |   | \$ 8,076,080   |  | \$ 8,001,173   |   | \$ 7,872,709   |                |
| Liabilities and stockholders' equity: |   |                |   |                |  |                |   |                |                |
| Interest-bearing liabilities:         |   |                |   |                |  |                |   |                |                |
| Savings                               | 0.73  | 227,431        | 0.74  | 229,540        | 1.07   | 231,986        | 1.66  | 228,710        | 1.66           |
| Checking                              | 0.21  | 423,107        | 0.20  | 405,787        | 0.21   | 403,327        | 0.20  | 395,295        | 0.21           |
| Money market                          | 1.04  | 800,155        | 1.08  | 775,386        | 1.31   | 799,408        | 1.45  | 810,464        | 2.22           |
| Certificates                          | 3.45  | 2,529,090      | 3.52  | 2,473,763      | 3.75   | 2,485,619      | 3.99  | 2,531,232      | 4.68           |
| Total deposits                        | 2.46  | 3,979,783      | 2.52  | 3,884,476      | 2.73   | 3,920,340      | 2.94  | 3,965,701      | 3.56           |
| FHLB advances                         | 4.30  | 2,451,927      | 4.40  | 2,477,961      | 4.72   | 2,469,082      | 4.73  | 2,602,210      | 4.88           |
| Other borrowings                      | 3.96  | 713,600        | 3.99  | 713,585        | 4.24   | 638,463        | 4.10  | 323,323        | 4.74           |
| Total borrowings                      | 4.22  | 3,165,527      | 4.31  | 3,191,546      | 4.61   | 3,107,545      | 4.60  | 2,925,533      | 4.86           |
|                                       | 3.22  | 7,145,310      | 3.31  | 7,076,022      | 3.58   | 7,027,885      | 3.67  | 6,891,234      | 4.11           |

|  |              |              |              |              |
|--|--------------|--------------|--------------|--------------|
| Total interest-bearing liabilities         |              |              |              |              |
| Other noninterest-bearing liabilities      | 114,699      | 121,970      | 103,332      | 111,881      |
| Stockholders' equity                       | 907,759      | 878,088      | 869,956      | 869,594      |
| Total liabilities and stockholders' equity | \$ 8,167,768 | \$ 8,076,080 | \$ 8,001,173 | \$ 7,872,709 |

(Continued)



|  |            |            |            |            |        |
|--|------------|------------|------------|------------|--------|
| Net interest rate spread   | 1.88%      | 1.93%      | 1.74%      | 1.68%      | 1.20%  |
| Net interest-earning assets                                      | \$ 820,996 | \$ 838,966 | \$ 821,593 | \$ 778,734 |        |
| Net interest margin  |            | 2.30%      | 2.08%      | 2.03%      | 1.62%  |
| Ratio of interest-earning assets to interest-bearing liabilities |            | 1.11       | 1.12       | 1.12       | 1.11   |
| Selected performance ratios:                                     |            |            |            |            |        |
| Return on average assets (annualized)                            |            | 0.89%      | 0.79%      | 0.79%      | 0.60%  |
| Return on average equity (annualized)                            |            | 7.99%      | 7.22%      | 7.25%      | 5.39%  |
| Average equity to average assets                                 |            | 11.11%     | 10.87%     | 10.87%     | 11.05% |

(Concluded)

(1) Calculated net of deferred loan fees, loan discounts, and loans in process. Non-accruing loans are included in the loans receivable average balance with a yield of zero percent.

(2) MBS and investment securities classified as AFS are stated at amortized cost, adjusted for unamortized purchase premiums or discounts.

The following table presents selected income statement information for the quarters indicated.

|   | For the Three Months Ended                       |                         |                          |                  |                   |
|---|--|-------------------------|--------------------------|------------------|-------------------|
|   | March 31,<br>2009                                | December<br>31,<br>2008 | September<br>30,<br>2008 | June 30,<br>2008 | March 31,<br>2008 |
| Selected income statement data:                                       | (Dollars in thousands, except per share amounts) |                         |                          |                  |                   |
| Interest and dividend income:   |  |                         |                          |                  |                   |
| Loans receivable  | \$ 77,446  | \$ 76,716               | \$ 75,830                | \$ 74,651        | \$ 75,276         |
| MBS   | 25,088   | 26,402                  | 26,153                   | 24,869           | 20,246            |
| Investment securities   | 955  | 1,326                   | 1,428                    | 1,298            | 3,061             |
| Other interest and dividend income                                    | 846  | 829                     | 1,766                    | 1,967            | 3,233             |
| Total interest and dividend income                                    | 104,335  | 105,273                 | 105,177                  | 102,785          | 101,816           |
| Interest expense:   |  |                         |                          |                  |                   |
| FHLB advances   | 26,653   | 29,545                  | 29,543                   | 30,248           | 31,796            |
| Deposits  | 24,711   | 26,785                  | 29,083                   | 31,174           | 35,145            |
| Other borrowings  | 7,109  | 7,725                   | 6,693                    | 4,682            | 3,873             |
| Total interest expense  | 58,473   | 64,055                  | 65,319                   | 66,104           | 70,814            |
| Provision for loan losses   | 2,107  | 549                     | 330                      | 1,602            | 119               |
| Net interest and dividend income<br>(after provision for loan losses) | 43,755   | 40,669                  | 39,528                   | 35,079           | 30,883            |
| Other income  | 6,936  | 6,642                   | 7,589                    | 7,345            | 7,982             |
| Other expenses  | 21,995   | 22,187                  | 21,795                   | 19,836           | 20,907            |
| Income tax expense  | 10,564   | 9,272                   | 9,563                    | 8,233            | 6,231             |
| Net income  | \$ 18,132  | \$ 15,852               | \$ 15,759                | \$ 14,355        | \$ 11,727         |
| Efficiency ratio  | 41.66  | 46.36                   | 45.94                    | 45.05            | 53.63             |
| Basic earnings per share  | \$ 0.25  | \$ 0.22                 | \$ 0.22                  | \$ 0.20          | \$ 0.16           |
| Diluted earnings per share  | \$ 0.25  | \$ 0.22                 | \$ 0.22                  | \$ 0.20          | \$ 0.16           |
| Dividends declared per public share                                   | \$ 0.50  | \$ 0.61                 | \$ 0.50                  | \$ 0.50          | \$ 0.50           |

Comparison of Operating Results for the Three Months Ended March 31, 2009 and 2008

Net income for the quarter ended March 31, 2009 was \$18.1 million compared to \$11.7 million for the same period in the prior fiscal year. The \$6.4 million increase in net income was primarily a result of a \$12.3 million decrease in interest expense, partially offset by a \$4.3 million increase in income tax expense.

Interest and Dividend Income

Total interest and dividend income for the quarter was \$104.3 million compared to \$101.8 million for the prior year quarter. The \$2.5 million increase was a result of an increase in interest income on MBS of \$4.9 million and interest income on loans receivable of \$2.2 million, partially offset by a decrease in interest income on investment securities of \$2.1 million, a decrease in interest income on cash and cash equivalents of \$1.3 million, and a decrease in dividends received on FHLB stock of \$1.1 million.

Interest income on loans receivable for the quarter was \$77.4 million compared to \$75.3 million for the prior year quarter. The \$2.1 million increase was a result of a \$178.8 million increase in the average balance of the loan portfolio between the two periods, partially offset by a two basis point decrease in the weighted average yield of the portfolio from 5.67% in the prior year quarter to 5.65% for the current quarter. The increase in the average balance was primarily due to loan purchases between the two periods. The decrease in the weighted average yield was primarily a result of the home equity loan portfolio repricing to lower market interest rates.

Interest income on MBS for the quarter was \$25.1 million compared to \$20.2 million for the prior year quarter. The \$4.9 million increase in interest income was due to an increase of \$363.9 million in the average balance of the MBS portfolio and to a lesser extent, an increase of 12 basis points in the weighted average yield to 4.73% for the current quarter. The increase in the average portfolio balance was a result of purchases. The funds for the purchases came from maturities and calls of investment securities and from new borrowings. The weighted average yield of the MBS portfolio increased between the two periods due to purchases of MBS at an average yield higher than the existing portfolio between the two periods.

Interest income on investment securities for the quarter was \$955 thousand compared to \$3.1 million for the prior year quarter. The \$2.1 million decrease in interest income was primarily a result of a decrease of \$178.5 million in the average balance of the portfolio and, to a lesser extent, a 99 basis point decrease in the weighted average portfolio yield to 3.03% for the current quarter. The decrease in the average balance was a result of calls and maturities that were not reinvested in their entirety into the investment securities portfolio but rather were invested in the higher yielding MBS portfolio. The decrease in the weighted average yield of the portfolio was attributed to maturities and calls of securities with weighted average yields greater than the portfolio, and also due to reinvestments made at lower yields than the overall portfolio yield.

Dividends on FHLB stock for the quarter were \$778 thousand compared to \$1.9 million for the prior year quarter. The \$1.1 million decrease was primarily due to a 331 basis point decrease in the weighted average yield. The dividend rate on FHLB stock correlates to the federal funds rate, which decreased between periods.

Interest income on cash and cash equivalents for the quarter was \$68 thousand, compared to \$1.4 million in the prior year quarter. The decrease was due to a 290 basis point decrease in the weighted average yield, and a decrease in the average balance of \$67.6 million. The decrease in the weighted average yield was a result of a decrease in short-term interest rates between periods. The decrease in the average balance was a result of the timing of cash being utilized to purchase MBS and to repay maturing FHLB advances.

Interest Expense

Interest expense on deposits for the current quarter was \$24.7 million compared to \$35.1 million for the prior year quarter. The \$10.4 million decrease in interest expense was a result of a decrease in the average rate paid on the certificate, money market, and savings deposit portfolios due to the portfolios repricing to lower market rates.

Interest expense on FHLB advances for the current quarter was \$26.7 million compared to \$31.8 million for the prior year quarter. The \$5.1 million decrease in interest expense was primarily a result of a decrease in the average rate as a result of the refinance of advances during the second quarter of fiscal year 2009 and the termination and maturity of the interest rate swap agreements during fiscal year 2008, and due to a decrease in the average balance.

See additional discussion of the refinance of the FHLB advances in “Notes to Financial Statements-- Note 4 – FHLB Advances.”

Interest expense on other borrowings was \$7.1 million compared to \$3.9 million in the prior year quarter. The \$3.2 million increase was due to an increase in the average balance of other borrowings due to the Bank entering into \$260.0 million of repurchase agreements between the two periods. The proceeds from the repurchase agreements were used to purchase MBS and to repay maturing FHLB advances.

#### Provision for Loan Losses

The Bank recorded a provision for loan losses of \$2.1 million during the current quarter, compared to \$119 thousand in the prior year quarter. The provision for loan losses recorded in the current quarter reflects the change in our allowance for loan loss methodology and charge-offs during the quarter. See additional discussion regarding the provision for loan losses in the sections entitled “Critical Accounting Policies – Allowance for Loan Losses” and “Asset Quality.”

#### Other Income and Expense

Total other income for the current quarter was \$6.9 million compared to \$8.0 million in the prior year quarter. The \$1.1 million decrease in other income was primarily a result of a \$1.1 million decrease in other income, net primarily due to the redemption of shares received in the Visa, Inc. initial public offering of \$992 thousand in the prior year quarter.

Total other expenses for the current quarter increased \$1.1 million to \$22.0 million, compared to \$20.9 million in the prior year quarter. The increase was due primarily to increases in advertising expense of \$561 thousand. The increase in advertising expense was due to expense associated with the Bank’s new debit card rewards program and advertising campaigns undertaken to reassure customers of the Bank’s safety and soundness in response to current economic conditions.

#### Income Tax Expense

Income tax expense for the current quarter was \$10.6 million compared to \$6.2 million in the prior year quarter. The increase in income tax expense was primarily due to an increase in earnings compared to the prior year quarter. The effective tax rate was 36.8% for the current year quarter, compared to 34.7% for the prior year quarter. The 210 basis point difference in effective tax rates between the two periods was primarily a result of a decrease in nontaxable income from BOLI, an increase in nondeductible expenses associated with the ESOP and an increase in pre-tax income which reduced the effective tax rate benefit of nontaxable income. In addition, the prior year quarter included a decrease in FASB Interpretation Number (“FIN”) 48 items due to lapses in applicable statutes of limitations.

The table below presents the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities, comparing the quarter ended March 31, 2009 to the quarter ended March 31, 2008. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in volume, which are changes in the average balance multiplied by the previous year's average rate and (2) changes in rate, which are changes in the average rate multiplied by the average balance from the previous year. The net changes attributable to the combined impact of both rate and volume have been allocated proportionately to the changes due to volume and the changes due to rate.

|  | Quarter Ended March 31,<br>2009 vs. 2008 |             |             |
|--|--|-------------|-------------|
|  | Increase (Decrease) Due to               |             |             |
|  | Volume                                   | Rate        | Total       |
|  | (Dollars in thousands)                   |             |             |
| <b>Interest-earning assets:</b>                |  |             |             |
| Loans receivable                               | \$ 2,489                                 | \$ (319)    | \$ 2,170    |
| MBS  | 4,293                                    | 549         | 4,842       |
| Investment securities                          | (1,484)                                  | (622)       | (2,106)     |
| Capital stock of FHLB                          | (3)                                      | (1,083)     | (1,086)     |
| Cash equivalents                               | (391)                                    | (910)       | (1,301)     |
| Total interest-earning assets                  | \$ 4,904                                 | \$ (2,385)  | \$ 2,519    |
| <b>Interest-bearing liabilities:</b>           |  |             |             |
| Savings  | \$ (5)                                   | \$ (533)    | \$ (538)    |
| Checking                                       | 4  | --          | 4           |
| Money market                                   | (58)                                     | (2,328)     | (2,386)     |
| Certificates                                   | (26)                                     | (7,488)     | (7,514)     |
| FHLB advances                                  | (1,825)                                  | (3,318)     | (5,143)     |
| Other borrowings                               | 3,867                                    | (631)       | 3,236       |
| Total interest-bearing liabilities             | \$ 1,957                                 | \$ (14,298) | \$ (12,341) |
| Net change in net interest and dividend income | \$ 2,947                                 | \$ 11,913   | \$ 14,860   |

#### Comparison of Operating Results for the Six Months Ended March 31, 2009 and 2008

Net income for the six months ended March 31, 2009 was \$34.0 million compared to \$20.8 million for the same period in the prior fiscal year. The \$13.2 million increase in net income was primarily a result of a \$22.7 million decrease in interest expense and a \$6.8 million increase in interest and dividend income, partially offset by a \$8.4 million increase in income tax expense, a \$3.8 million increase in other expenses, and a \$2.5 million increase in provision for loan loss.

#### Interest and Dividend Income

Total interest and dividend income for the six months ended March 31, 2009 was \$209.6 million compared to \$202.8 million for the prior year period. The \$6.8 million increase was a result of an increase in interest income on MBS of \$14.1 million and an increase in interest income on loans receivable of \$2.7 million, partially offset by a decrease in interest income on investment securities of \$4.9 million, a decrease in interest income on cash and cash equivalents of \$2.7 million, and a decrease in dividends received on FHLB stock of \$2.3 million.

Interest income on loans receivable for the six months ended March 31, 2009 was \$154.2 million compared to \$151.5 million for the prior year period. The \$2.7 million increase was a result of a \$143.7 million increase in the

average balance of the loan portfolio between the two periods, partially offset by a decrease of 5 basis points in weighted average yield of the portfolio to 5.66% for the current six month period. The decrease in the weighted average yield was primarily a result of the home equity loan portfolio repricing to lower market interest rates.

Interest income on MBS for the six months ended March 31, 2009 was \$51.5 million compared to \$37.4 million for the prior year period. The \$14.1 million increase in interest income was due to an increase of \$535.3 million in the average balance and, to a lesser extent, an increase of 16 basis points in the weighted average yield to 4.76% for the for the current six month period. The increase in the average portfolio balance was a result of purchases. The funds for the purchases came from maturities and calls of investment securities and from new borrowings. The weighted average yield of the MBS portfolio increased between the two periods due to purchases of MBS at an average yield higher than the existing portfolio between the two periods.

Interest income on investment securities for the six months ended March 31, 2009 was \$2.3 million compared to \$7.2 million for the prior year period. The \$4.9 million decrease in interest income was primarily a result of a decrease of \$216.9 million in the average balance of the portfolio and a 65 basis point decrease in the weighted average portfolio yield to 3.48% for the for the current six month period. The decrease in the average balance was a result of calls and maturities that were not reinvested in their entirety into the investment securities portfolio but rather into the higher yielding MBS portfolio and also to repay maturing FHLB advances. The decrease in the weighted average yield of the portfolio was attributed to maturities and calls of securities with weighted average yields greater than that of the portfolio, and also due to reinvestments made at lower yields than the overall portfolio yield.

Dividends on FHLB stock for the six months ended March 31, 2009 were \$1.6 million compared to \$3.9 million for the prior year period. The \$2.3 million decrease was primarily due to a 352 basis point decrease in the weighted average yield. The dividend rate on FHLB stock correlates to the federal funds rate, which decreased during the period.

Interest income on cash and cash equivalents for the six months ended March 31, 2009 was \$117 thousand, compared to \$2.8 million in the prior year period. The decrease was due to a 334 basis point decrease in the weighted average yield, and a decrease in the average balance of \$77.8 million. The decrease in the weighted average yield was a result of a decrease in short-term interest rates during the period. The decrease in the average balance was a result of cash being utilized to purchase MBS and to repay maturing FHLB advances.

#### Interest Expense

Total interest expense for the six months ended March 31, 2009 was \$122.5 million, compared to \$145.2 million for the prior year period. The \$22.7 million decrease was primarily due to a decrease in interest expense on deposits of \$21.7 million.

Interest expense on deposits for the six months ended March 31, 2009 was \$51.5 million compared to \$73.2 million for the prior year period. The \$21.7 million decrease in interest expense was primarily a result of a decrease in the average rate paid on certificate of deposit, savings, and money market portfolios due to the portfolios repricing to lower market rates.

Interest expense on FHLB advances for the current six month period was \$56.2 million compared to \$66.0 million for the prior year period. The \$9.8 million decrease in interest expense was primarily a result of a decrease in rate as a result of the termination and maturity of the interest rate swap agreements during fiscal year 2008 and to the refinance of \$575.0 million of advances during the second quarter of fiscal year 2009. The decrease was also due to a decrease in the average balance as a result of maturing advances that were not renewed. See additional discussion of the refinance of the FHLB advances in "Notes to Financial Statements-- Note 4 – FHLB Advances."



Interest expense on other borrowings was \$14.8 million compared to \$6.1 million in the prior year period. The \$8.7 million increase was due to an increase in the average balance of other borrowings due to the Bank entering into \$260.0 million of repurchase agreements between the two periods. The proceeds from the repurchase agreement funds were used to purchase MBS and to repay maturing FHLB advances.

#### Provision for Loan Losses

The Bank recorded a provision for loan losses of \$2.7 million during the current six month period, compared to a provision of \$119 thousand in the prior year period. Of the \$2.7 million, \$2.1 million was recorded in the second quarter of 2009, and reflects the changes in our allowance for loss methodology and charge-offs during the quarter. See additional discussion regarding the provision for loan losses in the sections entitled “Critical Accounting Policies – Allowance for Loan Losses” and “Asset Quality.”

#### Other Income and Expense

Total other income for the current six month period was \$13.6 million compared to \$15.1 million in the prior year period. The \$1.5 million decrease in other income was primarily a result of a \$1.3 million decrease in other income, net primarily due to the redemption of shares received in the Visa, Inc. initial public offering of \$992 thousand in the prior year period and to a decrease in income from BOLI of \$608 thousand as a result of a decrease in market interest rates.

Total other expenses for the current six month period increased \$3.8 million to \$44.2 million, compared to \$40.4 million in the prior year period. The increase was due to increases in advertising expense of \$1.5 million, other expense, net of \$1.3 million, and salaries and employee benefits of \$1.0 million. The increase in advertising expense was due to advertising campaigns undertaken to reassure customers of the Bank’s safety and soundness in response to current economic conditions, and to expense associated with the Bank’s new debit card rewards program. The increase in other expense, net was due primarily to REO operations and to an impairment and valuation allowance taken on the MSR asset due to an increase in prepayment speeds. These increases were partially offset by the reversal of a portion of the Visa, Inc. litigation liability accrued in the prior year period. The increase in salaries and employee benefits was due to an increase in costs associated with the ESOP as a result of a higher average CFFN stock price in the current period compared to the prior year period.

#### Income Tax Expense

Income tax expense for the current six month period was \$19.8 million compared to \$11.4 million in the prior year period. The increase in income tax expense was primarily due to an increase in earnings compared to the prior year period. The effective tax rate was 36.9% for the current year period, compared to 35.4% for the prior year period. The 150 basis point difference in effective tax rates between the two periods was primarily a result of a decrease in nontaxable income from BOLI, an increase in nondeductible expenses associated with the ESOP and an increase in pre-tax income which reduced the effective tax rate benefit of nontaxable income.

The following table presents the average balances of our assets, liabilities and stockholders' equity and the related annualized yields and costs on our interest-earning assets and interest-bearing liabilities for the periods indicated. Average yields are derived by dividing annualized income by the average balance of the related assets and average costs are derived by dividing annualized expense by the average balance of the related liabilities, for the periods shown. Average outstanding balances are derived from average daily balances. The yields and costs include amortization of fees, costs, premiums and discounts which are considered adjustments to yields/rates. Yields on tax-exempt securities were not calculated on a tax-equivalent basis.

|   | For the Six Months Ended          |                |                                   |                |
|---|-----------------------------------|----------------|-----------------------------------|----------------|
|   | March 31, 2009                    |                | March 31, 2008                    |                |
|   | Average<br>Outstanding<br>Balance | Yield/<br>Rate | Average<br>Outstanding<br>Balance | Yield/<br>Rate |
|   | (Dollars in thousands)            |                |                                   |                |
| <b>Assets:</b>  |                                   |                |                                   |                |
| <b>Interest-earning assets:</b>                                     |                                   |                |                                   |                |
| Loans receivable (1)  | \$ 5,452,000                      | 5.66%          | \$ 5,308,286                      | 5.71%          |
| MBS(2)  | 2,161,451                         | 4.76           | 1,626,128                         | 4.60           |
| Investment securities(2)  | 131,171                           | 3.48           | 348,058                           | 4.13           |
| Capital stock of FHLB   | 127,735                           | 2.45           | 132,072                           | 5.97           |
| Cash and cash equivalents   | 72,342                            | 0.32           | 150,176                           | 3.66           |
| <b>Total interest-earning assets (1) (2)</b>                        | <b>7,944,699</b>                  | <b>5.28</b>    | <b>7,564,720</b>                  | <b>5.36</b>    |
| Other noninterest-earning assets                                    | 176,721                           |                | 203,036                           |                |
| <b>Total assets</b>   | <b>\$ 8,121,420</b>               |                | <b>\$ 7,767,756</b>               |                |
| <b>Liabilities and stockholders' equity:</b>                        |                                   |                |                                   |                |
| <b>Interest-bearing liabilities:</b>                                |                                   |                |                                   |                |
| Savings   | \$ 228,497                        | 0.91           | \$ 230,832                        | 2.00           |
| Checking  | 414,352                           | 0.21           | 388,987                           | 0.21           |
| Money market  | 787,634                           | 1.19           | 802,383                           | 2.67           |
| Certificates  | 2,501,123                         | 3.64           | 2,517,775                         | 4.73           |
| <b>Total deposits</b>   | <b>3,931,606</b>                  | <b>2.63</b>    | <b>3,939,977</b>                  | <b>3.70</b>    |
| FHLB advances   | 2,465,087                         | 4.56           | 2,597,716                         | 5.04           |
| Other borrowings  | 713,593                           | 4.11           | 236,049                           | 5.07           |
| <b>Total borrowings</b>   | <b>3,178,680</b>                  | <b>4.46</b>    | <b>2,833,765</b>                  | <b>5.04</b>    |
| <b>Total interest-bearing liabilities</b>                           | <b>7,110,286</b>                  | <b>3.45</b>    | <b>6,773,742</b>                  | <b>4.26</b>    |
| Other noninterest-bearing liabilities                               | 118,373                           |                | 124,776                           |                |
| Stockholders' equity  | 892,761                           |                | 869,238                           |                |
| <b>Total liabilities and stockholders' equity</b>                   | <b>\$ 8,121,420</b>               |                | <b>\$ 7,767,756</b>               |                |
| Net interest rate spread  |                                   | 1.83%          |                                   | 1.10%          |
| Net interest-earning assets   | \$ 834,413                        |                | \$ 790,978                        |                |
| Net interest margin   |                                   | 2.19%          |                                   | 1.52%          |
| Ratio of interest-earning assets<br>to interest-bearing liabilities |                                   | 1.12           |                                   | 1.12           |
| <b>Selected Performance Ratios:</b>                                 |                                   |                |                                   |                |
| Return on average assets (annualized)                               |                                   | 0.84%          |                                   | 0.54%          |
| Return on average equity (annualized)                               |                                   | 7.61%          |                                   | 4.80%          |

|                                  |        |        |
|----------------------------------|--------|--------|
| Average equity to average assets | 10.99% | 11.19% |
|----------------------------------|--------|--------|

(1) Calculated net of deferred loan fees, loan discounts, and loans in process. Non-accruing loans are included in the loans receivable average balance with a yield of zero percent.

(2) MBS and investment securities classified as AFS are stated at amortized cost, adjusted for unamortized purchase premiums or discounts.

The table below presents the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities, comparing the six months ended March 31, 2009 to the six months ended March 31, 2008. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in volume, which are changes in the average balance multiplied by the previous year's average rate and (2) changes in rate, which are changes in the average rate multiplied by the average balance from the previous year. The net changes attributable to the combined impact of both rate and volume have been allocated proportionately to the changes due to volume and the changes due to rate.

|  | For the Six Months Ended<br>March 31, 2009 vs. March 31, 2008<br>Increase (Decrease) Due to |             |             |
|--|---|-------------|-------------|
|  | Volume  | Rate        | Total       |
|  | (Dollars in thousands)  |             |             |
| <b>Interest-earning assets:</b>                |   |             |             |
| Loans receivable                               | \$ 3,987  | \$ (1,364)  | \$ 2,623    |
| MBS  | 12,768  | 1,349       | 14,117      |
| Investment securities                          | (3,916)   | (994)       | (4,910)     |
| Capital stock of FHLB                          | (126)   | (2,260)     | (2,386)     |
| Cash and cash equivalents                      | (971)   | (1,709)     | (2,680)     |
| Total interest-earning assets                  | \$ 11,742   | \$ (4,978)  | \$ 6,764    |
| <b>Interest-bearing liabilities:</b>           |   |             |             |
| Savings(1)                                     | \$ (24)   | \$ (1,269)  | \$ (1,293)  |
| Checking                                       | 27  | --          | 27          |
| Money market                                   | (197)   | (5,939)     | (6,136)     |
| Certificates(1)                                | (398)   | (13,882)    | (14,280)    |
| FHLB advances                                  | (3,403)   | (6,356)     | (9,759)     |
| Other borrowings                               | 9,589   | (835)       | 8,754       |
| Total interest-bearing liabilities             | \$ 5,594  | \$ (28,281) | \$ (22,687) |
| Net change in net interest and dividend income | \$ 6,148  | \$ 23,303   | \$ 29,451   |

#### Comparison of Operating Results for the Three Months Ended March 31, 2009 and December 31, 2008

For the quarter ended March 31, 2009, the Company recognized net income of \$18.1 million, compared to net income of \$15.9 million for the quarter ended December 31, 2008.

#### Interest and Dividend Income

Total interest and dividend income for the current quarter was \$104.3 million compared to \$105.3 million for the quarter ended December 31, 2008. The decrease of \$1.0 million was primarily a result of decreases in interest income on MBS of \$1.3 million, partially offset by an increase in loans receivable of \$730 thousand.

Interest income on loans receivable for the current quarter was \$77.4 million compared to \$76.7 million for the quarter ended December 31, 2008. The \$730 thousand increase in interest income was primarily a result of a \$66.4 million increase in the average balance of the portfolio, partially offset by a decrease of one basis point in the weighted average yield.

Interest income on MBS for the current quarter was \$25.1 million compared to \$26.4 million for the quarter ended December 31, 2008. The \$1.3 million decrease was primarily a result of an \$81.1 million decrease in the average

balance of the portfolio and a decrease in the average yield of seven basis points. The decrease in the average balance was a result of principal repayments.

Interest income on investment securities for the current quarter was \$955 thousand compared to \$1.3 million for the quarter ended December 31, 2008. The slight decrease was primarily a result of an 86 basis point decrease in the weighted average yield and a \$10.4 million decrease in the average balance.

#### Interest Expense

Interest expense decreased \$5.6 million to \$58.5 million for the current quarter from \$64.1 million for the quarter ended December 31, 2008. The decrease was due to a decrease in interest expense on FHLB advances of \$2.9 million, a decrease in interest expense on deposits of \$2.1 million, and a decrease in interest expense on other borrowings of \$616 thousand. The decrease in interest expense on FHLB advances was due to a decrease in the average rate as a result of the refinance of \$575.0 million of FHLB advances during the current quarter. The decrease in deposit interest expense was primarily a result of a decrease in the rate paid on the certificate of deposit portfolio, partially offset by an increase in the average balance of deposits of \$95.3 million. The decrease in interest expense on other borrowings was due to a decrease of 25 basis points in the average rate due to a decrease in the three-month LIBOR during the period.

#### Provision for Loan Losses

The Bank recorded a provision for loan losses of \$2.1 million during the current quarter, compared to a provision of \$549 thousand in the quarter ended December 31, 2008. The provision for loan losses recorded in the current quarter reflects the change in our allowance for loan loss methodology and charge-offs during the quarter. See additional discussion regarding the provision for loan losses in the sections entitled "Critical Accounting Policies – Allowance for Loan Losses" and "Asset Quality."

#### Other Income and Expense

Total other income increased \$294 thousand to \$6.9 million for the current quarter compared to \$6.6 million for the quarter ended December 31, 2008. The increase was due primarily to an increase of \$492 thousand in gains on loans held for sale due to the sale of certain modified loans and an increase of \$382 thousand in insurance commissions, partially offset by a decrease in retail fees of \$499 thousand due to a decrease in ATM, debit card, and insufficient funds fees.

Total other expenses for the current quarter were \$22.0 million for the current quarter, compared to \$22.2 million in the prior quarter. The decrease was due primarily to a decrease in salaries and employee benefits of \$595 thousand, partially offset by increases in advertising of \$205 thousand and other expenses, net of \$204 thousand. The decrease in salaries and employee benefits was due to an increase in deferred payroll costs related to SFAS 91 "Accounting for Nonrefundable Fees and Costs Associated with Originating and Acquiring Loans and Initial Direct Costs of Leases" as a result of an increase in loan originations. The decrease in salaries and employee benefits was also a result of a decrease in costs associated with the ESOP as a result of a lower average CFFN stock price in the current period compared to the prior period.

#### Income Tax Expense

Income tax expense for the current quarter was \$10.6 million compared to \$9.3 million for the quarter ended December 31, 2008. The effective tax rate for each period was relatively unchanged at 36.8% for the current quarter, compared to 36.9% for the quarter ended December 31, 2008.





The table below presents the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities, comparing the quarter ended March 31, 2009 to the quarter ended December 31, 2008. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in volume, which are changes in the average balance multiplied by the previous year's average rate and (2) changes in rate, which are changes in the average rate multiplied by the average balance from the previous year. The net changes attributable to the combined impact of both rate and volume have been allocated proportionately to the changes due to volume and the changes due to rate.

|  | Quarter Ended                        |            |            |
|--|--------------------------------------|------------|------------|
|  | March 31, 2009 vs. December 31, 2008 |            |            |
|  | Increase (Decrease) Due to           |            |            |
|  | Volume                               | Rate       | Total      |
|  | (Dollars in thousands)               |            |            |
| <b>Interest-earning assets:</b>                |                                      |            |            |
| Loans receivable                               | \$ 876                               | \$ (146)   | \$ 730     |
| MBS  | (962)                                | (352)      | (1,314)    |
| Investment securities                          | (95)                                 | (276)      | (371)      |
| Capital stock of FHLB                          | 23                                   | (25)       | (2)        |
| Cash and cash equivalents                      | 57                                   | (38)       | 19         |
| Total interest-earning assets                  | \$ (101)                             | \$ (837)   | \$ (938)   |
| <b>Interest-bearing liabilities:</b>           |                                      |            |            |
| Savings  | \$ (8)                               | \$ (260)   | \$ (268)   |
| Checking                                       | (2)                                  | --         | (2)        |
| Money market                                   | 57                                   | (577)      | (520)      |
| Certificates                                   | 417                                  | (1,701)    | (1,284)    |
| FHLB advances                                  | (229)                                | (2,663)    | (2,892)    |
| Other borrowings                               | --                                   | (616)      | (616)      |
| Total interest-bearing liabilities             | \$ 235                               | \$ (5,817) | \$ (5,582) |
| Net change in net interest and dividend income | \$ (336)                             | \$ 4,980   | \$ 4,644   |

### Liquidity and Capital Resources

Liquidity management is both a daily and long-term function of our business management. The Bank's most available liquid assets, represented by cash and cash equivalents, available-for-sale mortgage-related and investment securities, and short-term investment securities, are products of its operating, investing and financing activities. The Bank's primary sources of funds are deposits, FHLB advances, other borrowings, repayments on and maturities of outstanding loans and MBS, other short-term investments, and funds provided from operations. While scheduled payments from the amortization of loans and MBS and payments on short-term investments are relatively predictable sources of funds, deposit flows and prepayments on loans and MBS are greatly influenced by general interest rates, economic conditions and competition and are less predictable sources of funds. The most significant liquidity challenge we currently face is the variability in cash flows as a result of mortgage modification and refinance activity. To the extent possible, the Bank manages the cash flows of its loan and deposit portfolios by the rates it offers customers. Sources of funds are used primarily to meet ongoing operations, to pay maturing certificates of deposit and savings withdrawals, and to fund loan commitments. At March 31, 2009, approximately \$1.55 billion of the \$2.61 billion in certificates of deposit were scheduled to mature within one year. Included in that amount are

\$95.9 million of brokered deposits and \$92.0 million in public unit deposits. Based on past experience and our pricing strategy, we expect that a majority of the maturing retail deposits will renew, although no assurance can be given in this regard. Management will continue to monitor the wholesale deposit market for attractive opportunities.

The Bank has paid competitive rates for its deposits while not “paying-up” in rates to grow its deposit base beyond the Bank’s need for funding. The Bank’s borrowings have been used primarily to invest in U.S. government agency securities in order to improve the earnings of the Bank and to help with the management of its interest rate risk while maintaining its capital ratios in excess of regulatory standards for well-capitalized financial institutions. In addition, the Bank’s focus on managing risk has provided it liquidity capacity by remaining below borrowing limits at FHLB and through the uncollateralized balance of its government agency MBS and investment securities available as collateral for borrowings.

The Bank has used FHLB advances to provide funds for lending and investment activities. FHLB lending guidelines set borrowing limits as part of their underwriting standards. At March 31, 2009, the Bank's ratio of the face amount of advances to total assets, as reported to the Office of Thrift Supervision ("OTS"), was 30%. Our advances are secured by a blanket pledge of our loan portfolio, as collateral, supported by quarterly reporting to FHLB Topeka. Advances in excess of 40% of total assets, but not exceeding 55% of total assets, may be approved by the president of FHLB Topeka based upon a review of documentation supporting the use of the advances. Currently, the blanket pledge is sufficient collateral for our outstanding FHLB advances. It is possible that increases in our borrowings or decreases in our loan portfolio could require the Bank to pledge securities as collateral on the FHLB advances. The Bank's policy allows borrowing from FHLB of up to 55% of total assets.

The Bank has used repurchase agreements primarily to fund purchases of MBS and to repay maturing FHLB advances. The repurchase agreements are treated as secured borrowings and are reported as a liability of the Company on a consolidated basis. The Bank has pledged securities with a market value of \$768.6 million as collateral. At the maturity date of these borrowings, the pledged securities will be delivered back to the Bank. The Bank may enter into additional repurchase agreements as management deems appropriate. At March 31, 2009, repurchase agreements were 8% of total assets. The Bank's policy allows for repurchase agreements to total up to 15% of total assets.

In 2004, the Company issued \$53.6 million in Junior Subordinated Deferrable Interest Debentures ("Debentures") in connection with a trust preferred securities offering. The Company received, net, \$52.0 million from the issuance of the Debentures and an investment of \$1.6 million in Capitol Federal Financial Trust I (the "Trust"). The Company did not down-stream the proceeds to be used by the Bank for Tier 1 capital because the Bank exceeded all regulatory requirements to be a well-capitalized institution. Instead, the Company deposited the proceeds into certificate accounts at the Bank to be used to further the Company's general corporate and capital management strategies, which could include the payment of dividends.

At March 31, 2009, cash and cash equivalents totaled \$52.0 million, a decrease of \$35.1 million from September 30, 2008. The cash was used to fund loan originations and purchase securities. The Company maintains access to additional liquidity through its management of the level of borrowings from the FHLB and counterparties of repurchase agreements through the availability of high quality collateral for borrowings. At March 31, 2009, \$1.02 billion of securities were eligible but unused for collateral. Securities eligible for collateral consist of unpledged securities with current balances of \$10.0 million or greater. The Company also has access to the brokered deposit market but does not currently consider the cost of this funding source to be balanced with investment opportunities.

The Bank is a member of the Deposit Insurance Fund (the "DIF"), which is administered by the Federal Deposit Insurance Corporation ("FDIC"). Deposits are insured up to the applicable limits by the FDIC and such insurance is backed by the full faith and credit of the United States Government. As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of and to require reporting by FDIC-insured institutions. Recent bank failures have decreased the DIF to levels below its required reserve ratio. The FDIC is required to replenish the fund by increasing deposit insurance premiums when the reserve ratio is below \$1.15 for every \$100 insured. In order to replenish the DIF, the FDIC has increased deposit insurance premiums to a level designed to restore the DIF to required levels within seven years, and has proposed a one-time special assessment of 20 basis points to be collected on September 30, 2009, based upon deposits at June 30, 2009. The FDIC also instituted the Transaction Account Guarantee Program ("TAGP"). The TAGP extended the FDIC's insurance to full coverage of noninterest-bearing transaction accounts for participating institutions through the end of 2009 at an annualized rate of 10 basis points on deposit balances in excess of the \$250 thousand insurance limit currently in place. The Bank is a participant in the TAGP, but does not expect this program to have a material impact on the FDIC assessment. An institution (or its successor) insured by the FDIC on December 31, 1996 which had previously paid assessments was eligible for certain

credit against deposit insurance assessments. This credit had offset the majority of the Bank's FDIC premium expense in past fiscal years but it is expected to be fully utilized during the third quarter of fiscal year 2009. As a result of these factors, the Bank is anticipating an increase in deposit insurance premiums in fiscal year 2009. Management estimates the increase to be approximately \$2.9 million for fiscal year 2009 not allowing for the proposed special assessment by the FDIC.

It is management's and the board of directors' intention to continue to pay regular quarterly dividends of \$0.50 per share for the foreseeable future. MHC, which owns a majority of the outstanding shares of CFFN common stock, generally waives its right to receive dividends paid on the common stock. See additional discussion and calculation of public shares in "Item 2, Management's Discussion and Analysis – Stockholders' Equity." At March 31, 2009, CFFN, at the holding company level, had \$113.9 million in cash and certificates of deposit at the Bank to be used to further the Company's general corporate and capital management strategies, which could include the payment of dividends.

The long-term ability of the Company to pay dividends to its stockholders is based primarily upon the ability of the Bank to make capital distributions to the Company. Under OTS safe harbor regulations, the Bank may distribute to the Company capital not exceeding net income for the current calendar year and the prior two calendar years. For several periods prior to December 31, 2008, the Bank could not distribute capital to the Company without waivers of the safe harbor regulation, which it received. The waiver was recently required as a result of lower earnings in prior periods compared to the timing of dividend payments by the Bank to the Company. Currently, the Bank has authorization from the OTS to distribute capital from the Bank to the Company through the quarter ending June 30, 2009. However, as of December 31, 2008, the Bank was no longer required to obtain a waiver, as the Bank's capital distributions to the Company no longer exceeded the net income requirements noted above.

On October 3, 2008, the Emergency Economic Stabilization Act ("EESA") was signed into law. EESA authorizes the Treasury Department to purchase from financial institutions and their holding companies up to \$700 billion in mortgage loans, MBS, and certain other financial instruments, including debt and equity securities issued by financial institutions and their holding companies in a Troubled Asset Relief Program ("TARP"). The purpose of TARP is to restore confidence and stability to the U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. The Treasury Department has allocated \$250 billion towards the TARP Capital Purchase Program ("CPP"). Under the CPP, Treasury will purchase debt or equity securities from participating institutions. Since expanding lending is the primary purpose of CPP, management and the board of directors believe the Company is already well positioned to meet the CPP's objective and therefore did not participate in the CPP. The other provisions in the EESA did not have a material impact on the Company's financial position, results of operations, cash flows, or liquidity.

## Off Balance Sheet Arrangements, Commitments and Contractual Obligations

The Company, in the normal course of business, makes commitments to buy or sell assets or to incur or fund liabilities. Commitments may include, but are not limited to:

- the origination, purchase, or sale of loans,
- the purchase or sale of investment securities and MBS,
- extensions of credit on home equity loans and construction loans,
  - terms and conditions of operating leases, and
  - funding withdrawals of deposit accounts.

The Company's contractual obligations related to operating leases and debentures have not changed significantly from September 30, 2008. The following table summarizes our other contractual obligations as of March 31, 2009.

|   | Total        | Less than<br>1 year | Maturity Range<br>1 – 3<br>years | 3 – 5<br>years | More than<br>5 years |
|---|--------------|---------------------|----------------------------------|----------------|----------------------|
| Certificates of Deposit                     | \$ 2,612,035 | \$ 1,545,581        | \$ 945,691                       | \$ 119,767     | \$ 996               |
| Weighted average rate                       | 3.45%        | 3.18%               | 3.88%                            | 3.53%          | 4.11%                |
| FHLB Advances                               | 2,446,000    | 320,000             | 876,000                          | 975,000        | 275,000              |
| Weighted average rate                       | 3.98%        | 4.37%               | 4.18                             | 3.62           | 4.18%                |
| Repurchase Agreements                       | 660,000      | --                  | 395,000                          | 145,000        | 120,000              |
| Weighted average rate                       | 3.97%        | --%                 | 3.94%                            | 3.81%          | 4.24%                |
| Commitments to originate<br>and             |              |                     |                                  |                |                      |
| purchase mortgage loans                     | 215,962      | 215,962             | --                               | --             | --                   |
| Weighted average rate                       | 5.08%        | 5.08%               | --%                              | --%            | --%                  |
| Commitments to fund<br>unused home          |              |                     |                                  |                |                      |
| equity lines of credit                      | 271,893      | 271,893             | --                               | --             | --                   |
| Weighted average rate                       | 4.43%        | 4.43%               | --%                              | --%            | --%                  |
| Unadvanced portion of<br>construction loans | 27,058       | 27,058              | --                               | --             | --                   |

A percentage of commitments to originate mortgage loans are expected to expire unfunded, so the amounts reflected in the table above are not necessarily indicative of future liquidity requirements. Additionally, the Bank is not obligated to honor commitments to fund unused home equity lines of credit if a customer is delinquent or otherwise in violation of the loan agreement.

The maturity schedule for our certificate of deposit portfolio at March 31, 2009 is located under "Item 3. Quantitative and Qualitative Disclosure About Market Risk." We anticipate that we will continue to have sufficient funds, through repayments and maturities of loans and securities, deposits and borrowings, to meet our current commitments.



The following table presents the maturity of FHLB advances at par and repurchase agreements as of March 31, 2009. The balance of FHLB advances excludes the deferred gain on the terminated interest rate swaps and the deferred prepayment penalty. Management will continue to monitor the Bank's investment opportunities and balance those opportunities with the cost of FHLB advances or other funding sources.

| Maturity by Fiscal year | FHLB Advances Amount<br>(Dollars in thousands) | Repurchase Agreements Amount | Weighted Average Contractual Rate | Weighted Average Effective Rate |
|-------------------------|--|------------------------------|-----------------------------------|---------------------------------|
| 2009                    | \$ 320,000                                     | \$ --                        | 4.37%                             | 4.37%                           |
| 2010                    | 350,000  | 45,000                       | 4.33                              | 4.33                            |
| 2011                    | 276,000  | 200,000                      | 4.42                              | 4.42                            |
| 2012                    | 350,000  | 150,000                      | 3.67                              | 3.67                            |
| 2013                    | 525,000  | 145,000                      | 3.74                              | 4.00                            |
| 2014                    | 350,000  | 100,000                      | 3.48                              | 4.21                            |
| 2015                    | 100,000  | 20,000                       | 4.02                              | 5.13                            |
| 2016                    | 175,000  | --                           | 4.32                              | 5.08                            |
| Total                   | \$ 2,446,000                                   | \$ 660,000                   | 3.98%                             | 4.23%                           |

The following table presents the maturity of FHLB advances and other borrowings for the next four quarters as of March 31, 2009. There are no maturities of repurchase agreements for the next four quarters.

| Maturity by Quarter End | Amount<br>(Dollars in thousands) | Weighted Average Rate |
|-------------------------|----------------------------------|-----------------------|
| June 30, 2009           | \$ --                            | --%                   |
| September 30, 2009      | 320,000                          | 4.37                  |
| December 31, 2009       | --                               | --                    |
| March 31, 2010          | --                               | --                    |
|                         | \$ 320,000                       | 4.37%                 |

#### Contingencies

In the normal course of business, the Company and its subsidiary are named defendants in various lawsuits and counter claims. In the opinion of management, after consultation with legal counsel, none of the currently pending suits are expected to have a materially adverse effect on the Company's consolidated financial statements for the current interim or future periods.



## Capital

Consistent with our goal to operate a sound and profitable financial organization, we actively seek to maintain a “well-capitalized” status in accordance with regulatory standards. Total equity under GAAP for the Bank was \$841.7 million at March 31, 2009, or 10% of total Bank assets on that date. As of March 31, 2009, the Bank exceeded all capital requirements of the OTS. Due to our strong capital position and current ability to access liquidity in excess of needs, the Company did not participate in the TARP’s CPP.

The following table presents the Bank’s regulatory capital ratios at March 31, 2009 based upon regulatory guidelines.

|                           | Bank<br>Ratios | Regulatory<br>Requirement<br>For “Well-<br>Capitalized”<br>Status |
|---------------------------|----------------|---|
| Tangible equity           | 9.9%           | N/A   |
| Core capital              | 9.9%           | 5.0%  |
| Tier I risk-based capital | 23.0%          | 6.0%  |
| Total risk-based capital  | 23.2%          | 10.0%   |

A reconciliation of the Bank’s equity under GAAP to regulatory capital amounts as of March 31, 2009 is as follows (dollars in thousands):

|                                     |            |
|-------------------------------------|------------|
| Total equity as reported under GAAP | \$ 841,707 |
| Unrealized gains on AFS securities  | (24,622)   |
| Other                               | (370)      |
| Total tangible and core capital     | 816,715    |
| Allowance for loan losses           | 4,846      |
| Total risk based capital            | \$ 821,561 |

## Item 3. Quantitative and Qualitative Disclosure About Market Risk

For a complete discussion of the Company’s asset and liability management policies, as well as the potential impact of interest rate changes upon the market value of the Company’s portfolios, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Asset and Liability Management and Market Risk” in the Company’s Annual Report to Stockholders for the year ended September 30, 2008, attached as Exhibit 13 to the Company’s Annual Report on Form 10-K for the year ended September 30, 2008.

The general objective of our interest rate risk management is to determine and manage an appropriate level of interest rate risk while maximizing net interest income, in a manner consistent with our policy to reduce, to the extent possible, the exposure of our net interest income to changes in market interest rates. ALCO regularly reviews the interest rate risk exposure of the Bank by forecasting the impact of hypothetical, alternative interest rate environments on net interest income and market value of portfolio equity (“MVPE”) at various dates. The MVPE is defined as the net of the present value of the cash flows of an institution’s existing assets, liabilities and off-balance sheet instruments. The present values are determined in alternative interest rate environments providing potential changes in net interest income and MVPE under those alternative interest rate environments. The Bank’s analysis of its MVPE at March 31, 2009 indicates a decrease in its risk exposure compared to September 30, 2008 primarily due to lower interest rates at March 31, 2009 compared to September 30, 2008. The Bank’s analysis of the sensitivity of its net

interest income to parallel changes in interest rates at March 31, 2009 indicates a decrease in sensitivity since September 30, 2008.

For each period end presented in the following table, the estimated percentage change in the Bank's net interest income based on the indicated instantaneous, parallel and permanent change in interest rates is presented. The percentage change in each interest rate environment represents the difference between estimated net interest income

in the 0 basis point interest rate environment (“base case”, assumes the forward market and product interest rates implied by the yield curve are realized) and estimated net interest income in each alternative interest rate environment (assumes market and product interest rates have a parallel shift in rates across all maturities by the indicated change in rates). At March 31, 2009, the three-month Treasury bill yield was less than one percent, so the -100 and -200 basis point scenarios are not presented. Estimations of net interest income used in preparing the table below are based upon the assumptions that the total composition of interest-earning assets and interest-bearing liabilities does not change materially and that any repricing of assets or liabilities occurs at anticipated product and market rates for the alternative rate environments as of the dates presented. The estimation of net interest income does not include any projected gain or loss related to the sale of loans or securities, or income derived from non-interest income sources, but does include the use of different prepayment assumptions in the alternative interest rate environments. It is important to consider that the estimated changes in net interest income are for a cumulative four-quarter period. These do not reflect the earnings expectations of management.

#### Percentage Change in Net Interest Income

| Change (in<br>Basis<br>Points)<br>in Interest<br>Rates(1) | At                |                         |                          |
|---|-------------------|-------------------------|--------------------------|
|   | March 31,<br>2009 | December<br>31,<br>2008 | September<br>30,<br>2008 |
| 000bp   | --                | --                      | --                       |
| +100bp  | 3.52%             | 1.15%                   | -2.20%                   |
| +200bp  | 3.58%             | -1.02%                  | -5.08%                   |
| +300bp  | 3.26%             | -3.42%                  | -8.62%                   |

(1) Assumes an instantaneous, permanent and parallel change in interest rates at all maturities.

The increase in estimated net interest income in all scenarios at March 31, 2009 compared to December 31, 2008 is primarily due to the decrease in the amount of liabilities expected to reprice in the upcoming year. The amount of liabilities expected to reprice decreased because FHLB advances that were scheduled to mature in the upcoming year were exchanged for new FHLB advances with longer maturities, as discussed in “Notes to Financial Statements-- Note 4 – FHLB Advances.”

Liabilities expected to reprice also decreased due to the maturity of \$300.0 million of FHLB advances during the quarter that were replaced with new long-term borrowings. At March 31, 2009 and December 31, 2008, the low level of interest rates, particularly mortgage rates, resulted in the WAL of mortgage related assets to be relatively short as borrowers have a financial incentive to refinance their mortgages into lower interest rates. As interest rates rise, this incentive for borrowers is reduced, resulting in less expected cash flow from mortgage related assets. At March 31, 2009, the amount of assets repricing in the four-quarter period is greater than the amount of liabilities in all of the interest rate shock scenarios, despite the decrease in cash flows from mortgage related assets as interest rate increase. At December 31, 2008 net interest income decreased in the +200 and +300 basis point scenarios. Cash flows from mortgage related assets decreased to such a degree that the amount of total assets expected to reprice was less than the amount of liabilities scheduled to reprice, thus having a negative impact to the net interest income.

The following table sets forth the estimated percentage change in MVPE at each period end presented based on the indicated instantaneous, parallel and permanent change in interest rates. The MVPE is defined as the net of the present value of the cash flows of an institution's existing assets, liabilities and off-balance sheet instruments. The percentage change in each interest rate environment represents the difference between MVPE in the base case and MVPE in each alternative interest rate environment. At March 31, 2009, the three-month Treasury bill was less than one percent, so the -100 and -200 basis point scenarios are not presented. The estimations of MVPE used in preparing the table below are based upon the assumptions that the total composition of interest-earning assets and interest-bearing liabilities does not change, that any repricing of assets or liabilities occurs at current product or market rates for the alternative rate environments as of the dates presented, and that different prepayment rates are used in each alternative interest rate environment. The estimated MVPE results from the valuation of cash flows from financial assets and liabilities over the anticipated lives of each for each interest rate environment. The table presents the effects of the change in interest rates on our assets and liabilities as they mature, repay or reprice, as shown by the change in the MVPE in changing interest rate environments.

## Percentage Change in MVPE

| Change (in<br>Basis<br>Points)<br>in Interest<br>Rates(1) | At                |                         |                          |
|---|-------------------|-------------------------|--------------------------|
|   | March 31,<br>2009 | December<br>31,<br>2008 | September<br>30,<br>2008 |
| 000bp   | --                | --                      | --                       |
| +100bp  | 0.70%             | 3.67%                   | -6.99%                   |
| +200bp  | -6.51%            | -9.06%                  | -19.37%                  |
| +300bp  | -18.34%           | -28.68%                 | -34.88%                  |

(1) Assumes an instantaneous, permanent and parallel change in interest rates at all maturities.

Changes in the estimated market values of our financial assets and liabilities drive changes in estimates of MVPE. The market value of shorter term-to-maturity financial instruments is less sensitive to changes in interest rates than the market value of longer term-to-maturity financial instruments. Because of this, our certificates of deposit (which have relatively short average lives) tend to display less sensitivity to changes in interest rates than do our mortgage-related assets (which have relatively long average lives). However, the average life expected on our mortgage-related assets varies under different interest rate environments because borrowers have the ability to prepay their mortgage loans. Prepayment assumptions change on mortgage-related assets under various interest rate environments because many borrowers look to obtain financing at the lowest cost available. Generally, there is no penalty to prepay a mortgage loan we have originated or purchased. If interest rates decrease, the borrower has an economic incentive to lower their mortgage payment (through a lower interest rate) with only the fees associated on the new mortgage or loan modification. In a decreasing interest rate environment, prepayments increase and the average life of a mortgage shortens compared to higher interest rate environments. When interest rates increase, the economic incentive for borrowers to refinance or modify their mortgage payment is reduced, resulting in lower prepayment assumptions and longer average lives.

The MVPE increased in the +100 basis point interest rate scenario at March 31, 2009, however, to a lesser extent than the increase at December 31, 2008. The MVPE increased in the +100 basis point scenario because the WAL of the assets are shorter than the liabilities, resulting in a larger decrease in the market value of liabilities than assets as interest rates increased. The increase in the MVPE was smaller at March 31, 2009 as a result of an increase in the WAL of mortgage related assets during this period. Longer weighted average lives result in greater price sensitivity to changes in interest rates. As a result, loss on mortgage related assets in the +100 basis point scenario was greater as of

March 31, 2009 than December 31, 2008. In the +200 and +300 basis point scenarios, the WAL of the mortgage related assets extended to such a point that the price sensitivity for mortgage related assets were similar at the end of both periods. The WAL of the liabilities increased during the current quarter primarily due to the refinancing of FHLB advances during the quarter into new advances with a longer term to maturity. Therefore, the change in the MVPE is less negative at March 31, 2009 due to the increase in the weighted average of the liability portfolio which helps to reduce risk during periods of rising interest rates.

Gap Table: The following gap table summarizes the anticipated maturities or repricing of our interest-earning assets and interest-bearing liabilities as of March 31, 2009, based on the information and assumptions set forth in the notes below. Cash flow projections for mortgage loans and MBS are calculated based on current interest rates. Prepayment projections are subjective in nature, involve uncertainties and assumptions and, therefore, cannot be determined with a high degree of accuracy. Although certain assets and liabilities may have similar maturities or periods to repricing, they may react differently to changes in market interest rates. Assumptions may not reflect how actual yields and costs respond to market changes. The interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types of assets and liabilities may lag behind changes in market interest rates. Certain assets, such as ARM loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. In the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in calculating the gap table. For additional information regarding the impact of changes in interest rates, see the Percentage Change in Net Interest Income and Percentage Change in MVPE tables above.

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| March 31, 2009  | Within<br>Three<br>Months | Three<br>Months To<br>One Year | More Than<br>One Year<br>to Three<br>Years | More Than<br>Three<br>Years to<br>Five Years | Over Five<br>Years | Total        |
|---|---------------------------|--------------------------------|--|--|--------------------|--------------|
| Interest-earning assets:<br>(Dollars in thousands)  |                           |                                |  |  |                    |              |
| Loans receivable(1):  |                           |                                |  |  |                    |              |
| Mortgage loans:   |                           |                                |  |  |                    |              |
| Fixed   | \$ 438,844                | \$ 1,041,454                   | \$ 1,088,281                               | \$ 447,823                                   | \$ 796,918         | \$ 3,813,320 |
| Adjustable  | 194,872                   | 695,210                        | 445,572                                    | 32,604                                       | 2,266              | 1,370,524    |
| Other loans   | 135,781                   | 30,109                         | 23,308                                     | 7,361  | 9,447              | 206,006      |
| Securities:   |                           |                                |  |  |                    |              |
| Non-mortgage securities(2)  |                           |                                |  |  |                    |              |
|   | 30,578                    | 79,601                         | 70,322                                     | 17,297                                       | 18,618             | 216,416      |
| MBS(3)  | 359,851                   | 790,296                        | 572,845                                    | 195,853                                      | 243,933            | 2,162,778    |
| Other interest-earning assets   | 34,244                    | --                             | --   | --   | --                 | 34,244       |
| Total interest-earning assets   | 1,194,170                 | 2,636,670                      | 2,200,328                                  | 700,938                                      | 1,071,182          | 7,803,288    |
| Interest-bearing liabilities:   |                           |                                |  |  |                    |              |
| Deposits:   |                           |                                |  |  |                    |              |
| Savings (4)   | 106,385                   | 8,056                          | 18,968                                     | 15,012                                       | 81,484             | 229,905      |
| Checking (4)  | 10,257                    | 34,348                         | 108,706                                    | 62,396                                       | 232,379            | 448,086      |
| Money market (4)  | 37,291                    | 103,193                        | 189,948                                    | 151,192                                      | 344,864            | 826,488      |
| Certificates  | 418,388                   | 1,127,193                      | 945,691                                    | 119,767                                      | 996                | 2,612,035    |
| Borrowings (5)  | 53,609                    | 320,000                        | 1,271,000                                  | 1,120,000                                    | 395,000            | 3,159,609    |
| Total interest-bearing liabilities  | 625,930                   | 1,592,790                      | 2,534,313                                  | 1,468,367                                    | 1,054,723          | 7,276,123    |
| Excess(deficiency) of interest-earning assets over interest-bearing liabilities                 |                           |                                |  |  |                    |              |
|   | \$ 568,240                | \$ 1,043,880                   | \$ (333,985)                               | \$ (767,429)                                 | \$ 16,459          | \$ 527,165   |
| Cumulative excess(deficiency) of interest-earning assets over interest-bearing liabilities      |                           |                                |  |  |                    |              |
|   | \$ 568,240                | \$ 1,612,120                   | \$ 1,278,135                               | \$ 510,706                                   | \$ 527,166         |              |
| Cumulative excess(deficiency) of interest-earning assets over interest-bearing liabilities as a |                           |                                |  |  |                    |              |
|   | 6.87%                     | 19.50%                         | 15.46%                                     | 6.18%  | 6.38%              |              |

|   |         |       |         |         |       |
|---|---------|-------|---------|---------|-------|
| percent of total assets at<br>March 31, 2009              |         |       |         |         |       |
| Cumulative<br>excess(deficiency) at<br>September 30, 2008 | (0.10)% | 1.90% | (1.19)% | (4.16)% | 9.05% |



(1) Adjustable-rate loans are included in the period in which the rate is next scheduled to adjust or in the period in which repayments are expected to occur prior to their next rate adjustment, rather than in the period in which the loans are due. Fixed-rate loans are included in the periods in which they are scheduled to be repaid, based on scheduled amortization and prepayment assumptions. Balances have been reduced for non-performing loans, which totaled \$22.4 million at March 31, 2009.

(2) Based on contractual maturities, or terms to call date or pre-refunding dates as of March 31, 2009, and excludes the unrealized loss adjustment of \$2.0 million on AFS investment securities.

(3) Reflects estimated prepayments of MBS in our portfolio, and excludes the unrealized gain adjustment of \$41.6 million on AFS MBS.

(4) Although our checking, savings and money market accounts are subject to immediate withdrawal, management considers a substantial amount of such accounts to be core deposits having significantly longer effective maturities. The decay rates (the assumed rate at which the balance of existing accounts would decline) used on these accounts are based on assumptions developed based upon our actual experience with these accounts. If all of our checking, savings and money market accounts had been assumed to be subject to repricing within one year, interest-bearing assets which were estimated to mature or reprice within one year would have exceeded interest-earning liabilities with comparable characteristics by \$407.2 million, for a cumulative one-year gap of 4.92% of total assets.

(5) Borrowings exclude \$35.2 million of deferred prepayment penalty costs and \$803 thousand of deferred gain on the terminated interest rate swaps.

The change in the one-year gap to 19.50% at March 31, 2009 from 1.90% at September 30, 2008 was a result of a significant decrease in interest rates, particularly mortgage interest rates. The decrease in mortgage interest rates increased projected cash flows from mortgage loan prepayments which resulted in shorter average lives and quicker repricing of interest-earning assets at March 31, 2009 compared to September 30, 2008.

Changes in portfolio composition. The following table presents the distribution of our investment and MBS portfolios, at cost, at the dates indicated. Overall, fixed-rate securities comprised approximately 55% of these portfolios at March 31, 2009. The WAL is the estimated remaining maturity after historical prepayment speeds and projected call option assumptions have been applied. The increase in the WAL between September 30, 2008 and March 31, 2009 was due largely to a slowdown in prepayment speeds on adjustable-rate MBS during the year. The decrease in the yield between September 30, 2008 and March 31, 2009 was a result of a decrease in the yield of adjustable-rate MBS that reset during the year as well as calls and maturities of higher yielding investment securities.

|                                     | March 31, 2009 |       |       | December 31, 2008 |       |       | September 30, 2008 |       |       |
|-------------------------------------|----------------|-------|-------|-------------------|-------|-------|--------------------|-------|-------|
|                                     | Balance        | WAL   | Yield | Balance           | WAL   | Yield | Balance            | WAL   | Yield |
| (Dollars in thousands)              |                |       |       |                   |       |       |                    |       |       |
| Fixed-rate investments:             |                |       |       |                   |       |       |                    |       |       |
| Agency bonds                        | \$ 152,067     | 0.75  | 1.68% | \$ 45,036         | 0.24  | 3.22% | \$ 82,552          | 5.55  | 4.28% |
| MBS                                 | 1,105,095      | 4.03  | 4.84  | 1,164,744         | 5.08  | 4.88  | 1,207,086          | 4.92  | 4.88  |
| Municipal bonds                     | 60,537         | 4.27  | 3.31  | 58,806            | 4.17  | 3.41  | 58,062             | 4.81  | 3.39  |
| Total fixed-rate investments        | 1,317,699      | 3.66  | 4.41  | 1,268,586         | 4.87  | 4.75  | 1,347,700          | 4.95  | 4.78  |
| Adjustable-rate investments:        |                |       |       |                   |       |       |                    |       |       |
| MBS                                 | 1,057,683      | 7.15  | 4.60  | 986,908           | 6.68  | 4.75  | 1,034,734          | 5.21  | 4.76  |
| Trust preferred securities          | 3,812          | 28.23 | 2.98  | 3,842             | 28.48 | 3.66  | 3,859              | 28.73 | 4.48  |
| Total adjustable-rate investments   | 1,061,495      | 7.25  | 4.59  | 990,750           | 6.79  | 4.75  | 1,038,593          | 5.32  | 4.76  |
| Total investment portfolio, at cost | \$ 2,379,194   | 5.26  | 4.49% | \$ 2,259,336      | 5.71  | 4.75% | \$ 2,386,293       | 5.11  | 4.77% |

The certificate of deposit portfolio increased \$93.0 million from September 30, 2008 to March 31, 2009 and the average cost of the portfolio decreased 46 basis points between the two reporting dates. The decrease in the average cost was due to repricing to market rates. Certificates maturing in one year or less at March 31, 2009 were \$1.55 billion with an average cost of 3.18%. The following table presents the maturity of certificates of deposit at the dates indicated.

|                               | March 31, 2009 |       | December 31, 2008 |       | September 30, 2008 |       | June 30, 2008 |       |
|-------------------------------|----------------|-------|-------------------|-------|--------------------|-------|---------------|-------|
|                               | Amount         | Rate  | Amount            | Rate  | Amount             | Rate  | Amount        | Rate  |
| (Dollars in thousands)        |                |       |                   |       |                    |       |               |       |
| Certificates maturing within: |                |       |                   |       |                    |       |               |       |
| 0 to 3 months                 | \$ 418,388     | 3.02% | \$ 333,638        | 3.14% | \$ 494,370         | 4.53% | \$ 454,875    | 4.71% |
| 3 to 6 months                 | 413,795        | 3.16  | 363,499           | 3.28  | 327,479            | 3.26  | 489,029       | 4.57  |
| 6 months to one year          | 713,398        | 3.28  | 741,881           | 3.54  | 658,537            | 3.43  | 567,943       | 3.40  |
| One year to two years         | 582,138        | 3.97  | 496,201           | 4.15  | 631,061            | 4.26  | 638,300       | 4.10  |
| After two years               | 484,316        | 3.69  | 493,310           | 3.90  | 407,549            | 3.93  | 347,496       | 4.19  |
| Total certificates            | \$ 2,612,035   | 3.45% | \$ 2,428,529      | 3.64% | \$ 2,518,996       | 3.91% | \$ 2,497,643  | 4.16% |
| Average maturity (in years)   | 1.11           |       | 1.15              |       | 1.09               |       | 1.03          |       |

Item 4. Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15(d)-15(e) under the Securities Exchange Act of 1934, as amended, the "Act") as of March 31, 2009. Based upon this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that as of March 31, 2009, such disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports it files or submits under the Act is accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) to allow timely decisions regarding required disclosure, and is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Changes in Internal Control Over Financial Reporting

During the quarter ended March 31, 2009, there were no changes in the Company's internal control over financial reporting as defined by Rule 13a-15(d) of the Act that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

We are not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business. We believe that these routine legal proceedings, in the aggregate, are immaterial to our financial condition and results of operations.

Item 1A. Risk Factors

There have been no material changes to our risk factors since September 30, 2008. For a summary of other risk factors relevant to our operations, see Part I, Item 1A in our 2008 Annual Report on Form 10-K.

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

See “Liquidity and Capital Resources - Capital” in “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations” regarding the OTS restrictions on dividends from the Bank to the Company.

The following table summarizes our share repurchase activity during the three months ended March 31, 2009 and additional information regarding our share repurchase program. Our current repurchase plan of 500,000 shares was announced on May 26, 2006. The plan has no expiration date and had 130,368 shares remaining as of March 31, 2009. The Company intends to repurchase shares from time to time, depending on market conditions, at prevailing market prices in open-market and other transactions. The shares would be held as treasury stock for general corporate use.

| Period                      | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total Number of<br>Shares Purchased<br>as<br>Part of Publicly<br>Announced Plans | Maximum Number<br>of Shares that May<br>Yet Be Purchased<br>Under the Plan |
|-----------------------------|---|------------------------------------|--|--|
| January 1, 2009<br>through  |   |                                    |  |  |
| January 31, 2009            | 36,201                                    | \$43.25                            | 36,201   | 130,368  |
| February 1, 2009<br>through |   |                                    |  |  |
| February 28, 2009           | --  | --                                 | --   | 130,368  |
| March 1, 2009<br>through    |   |                                    |  |  |
| March 31, 2009              | --  | --                                 | --   | 130,368  |
| Total                       | 36,201                                    |                                    | 36,201   |  |

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## Item 3. Defaults Upon Senior Securities

Not applicable.

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

The Annual Meeting of Stockholders for the fiscal year ended September 30, 2008 was held January 14, 2009. Two matters were presented to stockholders. The results were previously included in Part 2, Item 4 in the Form 10-Q for the period ended December 31, 2008.

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## Item 5. Other Information

Not applicable.

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## Item 6. Exhibits

See Index to Exhibits.



SIGNATURES

Pursuant to the requirement of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CAPITOL FEDERAL FINANCIAL

Date: May 5, 2009

By: /s/ John B. Dicus  
John B. Dicus, Chairman, President and  
Chief Executive Officer

Date: May 5, 2009

By: /s/ Kent G. Townsend  
Kent G. Townsend, Executive Vice President and  
Chief Financial Officer

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INDEX TO EXHIBITS

| Exhibit<br>Number | Document   |
|-------------------|--|
| 2.0               | Plan of Reorganization and Stock Issuance Plan*  |
| 3(i)              | Federal Stock Charter of Capitol Federal Financial*  |
| 3(ii)             | Bylaws of Capitol Federal Financial filed on November 29, 2007 as Exhibit 3(ii) to<br>the Annual Report on Form 10-K and incorporated herein by reference  |
| 4(i)              | Form of Stock Certificate of Capitol Federal Financial*  |
| 4(ii)             | The Registrant agrees to furnish to the Securities and Exchange Commission, upon request, the<br>instruments defining the rights of the holders of the Registrant's long-term<br>debt.                                       |
| 10.1(i)           | Registrant's Thrift Plan filed on November 29, 2007 as Exhibit 10.1(i) to<br>the Annual Report on Form 10-K and incorporated herein by reference   |
| 10.1(ii)          | Registrant's Stock Ownership Plan filed on November 29, 2007 as Exhibit 10.1(ii) to<br>the Annual Report on Form 10-K and incorporated herein by reference   |
| 10.2              | Registrant's 2000 Stock Option and Incentive Plan (the "Stock Option Plan")<br>filed on April 13,<br>2000 as Appendix A to Registrant's Revised Proxy Statement (File No.<br>000-25391) and incorporated herein by reference |
| 10.3              | Registrant's 2000 Recognition and Retention Plan (the "RRP") filed on April 13,<br>2000 as<br>Appendix B to Registrant's Revised Proxy Statement (File No. 000-25391)<br>and incorporated herein by reference                |
| 10.4              | Capitol Federal Financial Deferred Incentive Bonus Plan, as amended  |
| 10.5              | Form of Incentive Stock Option Agreement under the Stock Option Plan filed<br>on February 4, 2005<br>as Exhibit 10.5 to the December 31, 2004 Form 10-Q and incorporated herein<br>by reference                              |
| 10.6              | Form of Non-Qualified Stock Option Agreement under the Stock Option Plan<br>filed on February 4,<br>2005 as Exhibit 10.6 to the December 31, 2004 Form 10-Q and incorporated<br>herein by reference                          |
| 10.7              | Form of Restricted Stock Agreement under the RRP filed on February 4, 2005<br>as Exhibit 10.7 to the<br>December 31, 2004 Form 10-Q and incorporated herein by reference   |
| 10.8              | Description of Named Executive Officer Salary and Bonus Arrangements<br>filed on December 1,<br>2008 as Exhibit 10.8 to the Annual Report on Form 10-K and incorporated<br>herein by reference                               |
| 10.9              | Description of Director Fee Arrangements filed on February 4, 2009 as<br>Exhibit 10.9 to the December 31, 2008 Form 10-Q and incorporated herein by<br>reference   |
| 10.10             | Short-term Performance Plan filed on December 14, 2005 as Exhibit 10.10 to<br>the Annual   |



Report on Form 10-K for the fiscal year ended September 30, 2005 and incorporated herein by reference

- 11 Statement re: computation of earnings per share\*\*
- 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 made by John B. Dicus, Chairman, President and Chief Executive Officer
- 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 made by Kent G. Townsend, Executive Vice President and Chief Financial Officer
- 32 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 made by John B. Dicus, Chairman, President and Chief Executive Officer, and Kent G. Townsend, Executive Vice President and Chief Financial Officer

\*Incorporated by reference from Capitol Federal Financial's Registration Statement on Form S-1 (File No. 333-68363) filed on February 11, 1999, as amended and declared effective on the same date.

\*\*No statement is provided because the computation of per share earnings on both a basic and fully diluted basis can be clearly determined from the Financial Statements included in this report.

