CAPITOL FEDERAL FINANCIAL
Form 10-K
November 30, 2009

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K

(Mark One)

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

For the fiscal year ended September 30, 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
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
700 Kansas Avenue, Topeka, Kansas	66603
(Address of principal executive offices)	(Zip Code)

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

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

Common Stock, par value $0.01 per share	The NASDAQ Stock Market LLC
(Title of Class)	(Name of Each Exchange on Which Registered)

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

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15d of the Act.
Yes o No þ

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o (do not check if smaller reporting company) Smaller reporting company o

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

The aggregate market value of the voting and non-voting stock held by non-affiliates of the registrant, computed by reference to the average of the closing bid and asked price of such stock on the NASDAQ Stock Market as of March 31, 2009, was $755.9 million. The exclusion from such amount of the market value of the shares owned by any person shall not be deemed an admission by the Registrant that such person is an affiliate of the registrant.

As of November 13, 2009, there were issued and outstanding 74,099,355 shares of the Registrant's common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Parts II and IV of Form 10-K - Portions of the Annual Report to Stockholders for the year ended September 30, 2009. Part III of Form 10-K - Portions of the proxy statement for the Annual Meeting of Stockholders for the year ended September 30, 2009.

PRIVATE SECURITIES LITIGATION REFORM ACT—SAFE HARBOR STATEMENT

Capitol Federal Financial (the "Company"), and its wholly-owned subsidiary, Capitol Federal Savings Bank ("Capitol Federal Savings" or the "Bank"), may from time to time make written or oral "forward-looking statements", including statements contained in the Company's filings with the Securities and Exchange Commission ("SEC"). These forward-looking statements may be included in this Annual Report on Form 10-K 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;
- results of examinations of the Bank by its primary regulator, the Office of Thrift Supervision (the "OTS"), including the possibility that the OTS may, among other things, require the Bank to increase its 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.

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PART I

As used in this Form 10-K, 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.

Item 1. Business

General

The Company is a federally chartered mid-tier mutual holding company incorporated in March 1999. The Bank is a wholly-owned subsidiary of the Company, which is majority-owned by MHC, a federally chartered mutual holding company. The Company’s common stock is traded on the Global Select tier of the NASDAQ Stock Market under the symbol “CFFN.”

The Bank is the only operating subsidiary of the Company. The Bank is a federally-chartered and insured savings bank headquartered in Topeka, Kansas and is examined and regulated by the OTS. The OTS is its primary regulator. It is also regulated by the Federal Deposit Insurance Corporation (“FDIC”). We primarily serve the metropolitan areas of Topeka, Wichita, Lawrence, Manhattan, Emporia and Salina, Kansas and a portion of the metropolitan area of greater Kansas City through 33 traditional and nine in-store banking offices. At September 30, 2009, we had total assets of $8.40 billion, loans of $5.60 billion, deposits of $4.23 billion and total equity of $941.3 million.

We have been, and intend to continue to be, a community-oriented financial institution offering a variety of financial services to meet the needs of the communities we serve. We attract retail deposits from the general public and invest 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, 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 one- to four-family mortgage loans from correspondent lenders located within our market areas and select market areas in Missouri and from nationwide lenders, and invest in certain investment and mortgage-backed securities (“MBS”) funded through retail deposits, advances from Federal Home Loan Bank Topeka (“FHLB,”) and repurchase agreements. We may originate loans outside of our market area on occasion, and the majority of the whole loans we purchase from nationwide lenders are secured by properties located outside of our market areas.

Our revenues are derived principally from interest on loans, MBS and investment securities. Our primary sources of funds are retail deposits, borrowings, repayments on and maturities of loans and MBS, calls and maturities of investment securities, and funds generated by operations.

We offer a variety of deposit accounts having a wide range of interest rates and terms, which generally include savings accounts, money market accounts, interest bearing and non-interest bearing checking accounts, and certificates of deposit with terms ranging from 91 days to 96 months.

Our executive offices are located at 700 South Kansas Avenue, Topeka, Kansas 66603, and our telephone number at that address is (785) 235-1341.

Available Information

Our Internet website address is www.capfed.com. Financial information, including our 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 website. These reports are available on our website as soon as reasonably practicable after they are electronically filed with or furnished to the SEC. These reports are also available on the SEC's website at http://www.sec.gov.

Market Area and Competition

Our corporate office is located in Topeka, Kansas. We have a network of 42 branches located in 8 counties throughout the state of Kansas and one county in Missouri. We primarily serve the metropolitan areas of Topeka, Wichita, Lawrence, Manhattan, Emporia and Salina, Kansas and a portion of the metropolitan area of greater Kansas City. In addition to providing full service banking offices, we also provide our customers telephone and internet banking capabilities.

The Bank ranked first in deposit market share in the state of Kansas as reported in the FDIC "Summary of Deposits - Market Share Report" dated June 30, 2009. Deposit market share is measured by total deposits, without consideration for type of deposit. We do not have commercial deposit accounts because of our focus on retail deposits, while many of our competitors have both commercial and retail deposits in their total deposit base. Some of our competitors also offer products and services that we do not, such as trust services and private banking. In recent years, the Bank has experienced a slight decrease in market share due to the entrance of new competitors such as credit unions, newly chartered banks (de novo institutions), and increased banking locations by established financial institutions. Additionally, consumers have the ability to utilize financial institutions without a brick-and-mortar presence in our market area by way of online products and services. Management considers our strong retail banking network and our reputation for financial strength and customer service to be our major strengths in attracting and retaining customers in our market areas.

The Bank is consistently one of the top one- to four-family lenders with regard to loan volume in the state of Kansas. Through our strong relationships with real estate agents and marketing efforts which reflect our reputation and pricing, we attract mortgage loan business from walk-in customers, customers that apply online, and existing customers. Competition in originating one- to four-family mortgage loans primarily comes from other savings institutions, commercial banks, credit unions, and mortgage bankers. Other savings institutions, commercial banks, credit unions, and finance companies provide vigorous competition in consumer lending.

We purchase one- to four-family conventional mortgage loans from correspondent lenders located within our market areas and select market areas in Missouri, and from nationwide lenders. At September 30, 2009 loans purchased from nationwide lenders represented 12% of our total loan portfolio and were secured by properties located in each of the continental 48 states and Washington, D.C. At September 30, 2009, purchases from nationwide lenders in the following states comprised greater than 5% of nationwide purchased loans: Illinois 12%; Texas 8%; Florida 7%; and New York 7%.

During fiscal year 2009, the Bank opened three branches in our Kansas City and Wichita market areas, and has preliminary plans to open three additional branches in those same market areas during fiscal year 2010.

Lending Practices and Underwriting Standards

General. 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 real estate loans secured by multi-family dwellings. Additional lending volume has been generated by purchasing whole one- to four-family conventional 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 to 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, particularly in some of the states where we have purchased loans, 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" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K 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%. We have not experienced any performance problems with this group of purchased loans. See additional discussion regarding loans purchased during fiscal year 2009 in "Financial Condition – Loans Receivable" in the Annual Report to Stockholders attached as Exhibit 13 to this

Annual Report on Form 10-K.

The ability of financial institutions, including us, to originate or purchase large dollar volumes of one- to four-family real estate loans may be substantially reduced or restricted under certain economic and regulatory conditions, with a resultant decrease in interest income from these assets. At September 30, 2009, our one- to four-family residential real estate loan portfolio totaled $5.32 billion, which constituted 63.3% of our total assets. For a discussion of our market risk associated with loans see "Management's Discussion and Analysis of Financial Condition and Results of Operations - Quantitative and Qualitative Disclosure about Market Risk" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

Loans over $500 thousand must be underwritten by two Class V underwriters, which is our 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 ALCO and/or board of directors information about the creditworthiness of the borrower and the 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 value of the property must be supported by an independent appraisal report prepared in accordance with our appraisal policy. Loans over $500 thousand are priced above the standard mortgage rate.

Under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, the maximum amount which we could have loaned to any one borrower and the borrower's related entities at September 30, 2009 was $126.1 million. Our largest lending relationship to a single borrower or a group of related borrowers at September 30, 2009 consisted of 21 multi-family real estate projects, two single-family homes, and four commercial real estate projects located in Kansas, Iowa, and Texas. Total commitments and loans outstanding to this group of related borrowers was $56.4 million as of September 30, 2009. Most of the multi-family real estate loans qualify for the low income housing tax credit program. We have over 30 years of experience with this group of borrowers, who usually build and manage their own properties. Each of the loans to this group of borrowers was current and performing in accordance with repayment terms at September 30, 2009. See additional information under the heading "Multi-family and Commercial Real Estate Lending."

The second largest lending relationship at September 30, 2009, consisted of nine loans totaling $11.9 million. Four loans are secured by multi-family real estate units and five are secured by single-family homes. We have over 30 years of experience with the borrowers. All units were built and are presently being managed by the borrowers. Each of the loans to this group of borrowers was current and performing in accordance with repayment terms at September 30, 2009.

One- to Four-Family Residential Real Estate Lending. The Bank originates and services conventional mortgage loans, or loans not insured or guaranteed by a government agency. The Bank also originates Federal Housing Administration ("FHA") insured loan products which are generally sold, along with the servicing of these loans. New loans are originated through referrals from real estate brokers and builders, our marketing efforts, and our existing and walk-in customers. While the Bank originates both adjustable and fixed-rate loans, our ability to originate loans is dependent upon customer demand for loans in our market areas. Demand is affected by the local housing market, competition and the interest rate environment. During the 2009 and 2008 fiscal years, the Bank originated and refinanced $961.5 million and $631.8 million of one- to four-family fixed-rate mortgage loans, and $35.9 million and $77.7 million of one- to four-family adjustable-rate mortgage ("ARM") loans, respectively.

Repayment

The Bank's one- to four-family loans are primarily fully amortizing fixed- or ARM loans with contractual maturities of up to 30 years, except for interest-only ARM loans, which require only 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.

Pricing

Our pricing strategy for first mortgage loan products includes setting interest rates based on secondary market prices and competition within our local lending markets. ARM loans are offered with either a three-year, five-year or seven-year term to the initial repricing date. After the initial period, the interest rate for each ARM loan generally adjusts annually for the remainder of the term of the loan. A number of different indices are used to reprice our ARM loans.

Adjustable rate loans

Current adjustable-rate one- to four-family conventional mortgage 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. For three, five, or seven year ARM loans, borrowers are qualified based on the principal, interest, taxes and insurance payments at either the initial rate or the fully indexed accrual rate, whichever is greater. 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 interest-only ARM product was discontinued to reduce future credit risk exposure. Additionally, the Bank has not purchased any interest-only ARM loans since fiscal year 2006. 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 September 30, 2009, $256.2 million, or approximately 5% 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. The interest-only loans we purchased had borrowers with an average credit score of 737 at the time of purchase and an average loan-to-value ratio not exceeding 80% at the time of purchase.

Underwriting

One- to four-family loans are underwritten manually or by 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 ("LTV") ratio. 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. Loans that do not meet the automated underwriting standards are referred to a staff underwriter for manual underwriting. 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.

Mortgage Insurance

For loans with an LTV ratio in excess of 80% at the time of origination, the Bank offers customers the option of a conventional mortgage product with private mortgage insurance ("PMI") or an FHA mortgage product. For a conventional mortgage with an LTV in excess of 80%, PMI is required in order to reduce the Bank's loss exposure to less than 80% of either the appraised value or the purchase price of the property, whichever is less. The Bank will lend up to 97% of the lesser of the appraised value or purchase price for conventional one- to four-family loans, provided PMI is obtained. Management continuously monitors the claim paying ability of our PMI counterparties. At this time, we believe that our PMI counterparties have the ability to meet potential claim obligations we may file in the foreseeable future.

FHA loans generally have a LTV in excess of 80% at the time of origination, with mortgage insurance provided by the federal government. The loans are up to 97.5% of the lesser of the appraised value or purchase price and are originated and underwritten manually according to private investor and FHA guidelines. The Bank began offering FHA loans in late September 2009 to accommodate customers who may not qualify for a conventional mortgage loan. FHA loans are originated by the Bank with the intention of selling the loans on a flow basis to a private investor with servicing released.

Purchased loans

The Bank purchases approved conventional one- to four-family loans and the related servicing rights, on a loan-by-loan basis, from correspondent lenders. During the 2009 and 2008 fiscal years, the Bank purchased $141.6 million and $119.5 million, respectively, of one- to four-family loans from correspondent lenders. These loans generally have an interest rate 0.125% higher than loans we originate; however, we pay a premium for those loans.

The underwriting of loans purchased through correspondent lenders is generally performed by our underwriters, using our underwriting standards. The products offered by our correspondents are underwritten to standards that are at least as restrictive as the Bank's own internal products and underwriting standards. "No Doc" or "Stated Income, Stated Assets" loans are not permitted under our underwriting standards. Lenders are required to fully document all data sources for each application. Management believes these requirements reduce the credit risk associated with these loans. Lenders are located within the metropolitan Kansas City market area and select market areas in Missouri.

The Bank also purchases conventional one- to four-family loans from nationwide lenders. The servicing rights are generally retained by the lender. The underwriting standards are generally similar to the Bank's internal underwriting standards. "No Doc" or "Stated Income, Stated Assets" loans are not permitted under our underwriting standards. 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 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 internal Bank underwriter reviews at least 25% of the loan files to confirm loan terms, credit scores, debt service ratios, and property value documentation. Our standard contractual agreement with the lender includes recourse options for any breach of representation or warranty with respect to the loans purchased. In general, loans are purchased with servicing retained by the seller. The servicing of purchased loans is governed by a servicing agreement, which outlines collection policies and procedures, as well as oversight requirements, such as servicer certifications attesting to and providing proof of compliance with the servicer agreement. During fiscal years 2009 and 2008, the Bank purchased $191.8 million and $155 thousand, respectively, of one- to four-family loans from nationwide lenders.

Loan modification program

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. During fiscal year 2009, we modified $1.14 billion our originated loans.

Loan sales

Conventional one- to four-family loans may be sold on a bulk basis for portfolio restructuring or on a flow basis as loans are originated to reduce interest rate risk and/or maintain a certain liquidity position. The Bank generally retains the servicing on these loans. ALCO determines which conventional one- to four-family loans are to be originated as "Held for Sale" or "Held for Investment." Conventional one- to four-family loans originated as "Held for Sale" are to be sold in accordance with policies set forth by ALCO. Conventional one- to four-family loans originated as "Held for Investment" are generally not eligible for sale unless a specific segment of the portfolio is identified for asset restructuring purposes. Generally, the Bank will continue to service these loans.

Construction Lending. 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. 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. At September 30, 2009, we had $39.5 million in construction-to-permanent loans outstanding, including undisbursed loan funds, representing almost 1% of our total loan portfolio.

Consumer Lending. 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. At September 30, 2009, our consumer loan portfolio totaled $205.0 million, or 3.7% of our total loan portfolio.

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%. 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 PMI. 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. Home equity loans, including lines of credit and home improvement loans, comprised almost 3.5% of our total loan portfolio, or $195.6 million, at September 30, 2009. As of September 30, 2009, 71.6% of the home equity portfolio was adjustable-rate.

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 loans. However, consumer loans may entail greater risk than do one- to four-family 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.

Multi-family and Commercial Real Estate Lending. 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 ARM 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.

At September 30, 2009, multi-family and commercial real estate loans totaled $80.5 million, or 1.4% of our total loan portfolio.

We generally do not maintain a tax or insurance escrow account for multi-family or commercial real estate loans. In order to monitor the adequacy of cash flows on income-producing properties with a principal balance of $1.5 million or more, the borrower is notified annually to provide financial information including rental rates and income, maintenance costs and an update of real estate property tax payments, as well as personal financial information.

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 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."

The Bank is a participant with five other banking institutions on a $42.5 million commercial construction loan secured by a retail shopping center in Kansas. The Bank's original participant share was $15.0 million, which was to be disbursed as the improvements were completed. The loan was converted from a construction loan to a permanent loan in April 2009, but still had funds to advance for tenant finish. Due to economic factors, the lead bank and the borrower requested to restructure the project and reduce the overall commitment to $31.0 million, which reduced the Bank's commitment to $10.9 million as of August 2009. At September 30, 2009, the outstanding principal balance of the Bank's commitment was $7.6 million. The change involved completing construction for retail space that was already started, of which 81% is leased as of September 30, 2009, and postponing the development of additional space. This loan is part of our largest lending relationship to a single borrower or a group of related borrowers at September 30, 2009. Although the loan has performed per the terms of the agreement, the change in agreement has prompted management to classify the loan as "Special Mention" at September 30, 2009. See "Classified Assets."

Loan Portfolio. The following table presents information concerning the composition of our loan portfolio in dollar amounts and in percentages (before deductions for undisbursed loan funds, unearned loan fees and deferred costs, and the allowance for loan losses) as of the dates indicated.

	September 30,									
	2009		2008		2007		2006		2005	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)									
Real Estate Loans:										
One- to four-family	$5,321,935	94.2 %	$5,026,358	93.4 %	$4,992,398	93.4 %	$4,931,505	93.8 %	$5,189,006	94.5 %
Multi-family and commercial	80,493	1.4	56,081	1.0	60,625	1.1	56,774	1.1	49,563	0.9
Construction	39,535	0.7	85,178	1.6	74,521	1.4	45,452	0.8	45,312	0.8
Total real estate loans	5,441,963	96.3	5,167,617	96.0	5,127,544	95.9	5,033,731	95.7	5,283,881	96.2
Consumer and Other Loans:										
Home equity	195,557	3.5	202,956	3.8	208,642	3.9	212,938	4.1	198,135	3.6
Other	9,430	0.2	9,272	0.2	10,440	0.2	10,804	0.2	12,371	0.2
Total consumer and other loans	204,987	3.7	212,228	4.0	219,082	4.1	223,742	4.3	210,506	3.8
Total loans receivable	5,646,950	100.0%	5,379,845	100.0%	5,346,626	100.0%	5,257,473	100.0%	5,494,387	100.0%
Less:										
Undisbursed loan funds	20,649		43,186		42,481		22,605		14,803	
Unearned loan fees and deferred costs	12,186		10,088		9,893		9,318		10,856	
Allowance for losses	10,150		5,791		4,181		4,433		4,598	
Total loans receivable, net	$5,603,965		$5,320,780		$5,290,071		$5,221,117		$5,464,130	

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The following table presents the contractual maturity of our loan portfolio at September 30, 2009. Loans which have adjustable or renegotiable interest rates are shown as maturing in the period during which the contract is due. The table does not reflect the effects of possible prepayments or enforcement of due on sale clauses.

	One- to Four-Family		Real Estate Multi-family and Commercial		Construction and Development(2)		Home Equity (3)		Other		Total	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate
	(Dollars in thousands)											
Amounts due:												
Within one year(1)	$1,970	6.21%	$10,953	4.95%	$26,283	5.27%	$4,117	4.20%	$1,400	6.46%	$44,723	5.17%
After one year:												
Over one to two	3,263	5.67	27	7.00	13,252	5.07	1,188	4.77	1,288	7.61	19,018	5.33
Over two to three	9,234	5.63	1,083	6.24	--	--	2,163	5.21	1,043	6.73	13,523	5.70
Over three to five	49,830	5.28	571	6.51	--	--	3,931	5.37	5,224	5.60	59,556	5.33
Over five to ten	480,715	5.21	8,085	5.93	--	--	31,143	5.05	475	8.57	520,418	5.21
Over 10 to 15	826,055	5.07	11,872	6.35	--	--	60,990	4.90	--	--	898,917	5.07
After 15 years	3,950,868	5.31	47,902	6.25	--	--	92,025	6.40	--	--	4,090,795	5.35
Total due after one year	5,319,965	5.26	69,540	6.23	13,252	5.07	191,440	5.66	8,030	6.24	5,602,227	5.29
Total loans	$5,321,935	5.26%	$80,493	6.06%	$39,535	5.20%	$195,557	5.63%	$9,430	6.27%	5,646,950	5.29%
Less:												
Undisbursed loan funds											20,649	
Unearned loan fees and deferred costs											12,186	
Allowance for loan losses											10,150	
Total loans receivable,											$5,603,965	

net

(1) Includes demand loans, loans having no stated maturity, and overdraft loans.

(2) Construction loans are presented based upon the term to complete construction.

(3) For home equity loans, the maturity date calculated assumes the customer always makes the required minimum payment. Interest-only home equity lines of credit with an application date prior to May 30, 2008 assume a balloon payment of unpaid principal at 120 months. Interest-only home equity lines of credit with an application date on or after May 30, 2008 assume a balloon payment of unpaid principal at 12 months. All other home equity lines of credit assume a term of 240 months.

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The following table presents, as of September 30, 2009, the amount of loans, net of undisbursed loan funds, due after September 30, 2010, and whether these loans have fixed or adjustable interest rates.

	Fixed	Adjustable	Total
	(Dollars in thousands)		
Real Estate Loans:			
One- to four-family	$4,226,035	$1,093,930	$5,319,965
Multi-family and Commercial	66,867	2,673	69,540
Construction	12,707	545	13,252
Consumer and Other Loans:			
Home equity	55,544	135,896	191,440
Other	4,123	3,907	8,030
Total	$4,365,276	$1,236,951	$5,602,227

The following table shows our loan originations, loan purchases and participations, transfers, and repayment activity for the periods indicated. Purchased loans include loans purchased from correspondent and nationwide lenders. The table below does not include $1.14 billion of originated loans that were modified during fiscal year 2009 ..

	Year Ended September 30,		
	2009	2008	2007
	(Dollars in thousands)		
Originations by type:			
Adjustable-rate:			
Real estate - one- to four-family	$35,862	$77,679	$104,362
- multi-family and commercial	--	1,800	--
Home equity	91,053	87,614	87,022
Other	4,391	1,731	--
Total adjustable-rate loans originated	131,306	168,824	191,384
Fixed-rate:			
Real estate - one- to four-family	961,493	631,765	573,239
- multi-family and commercial	14,891	975	5,523
Home equity	10,069	14,475	25,285
Other	1,922	4,796	8,019
Total fixed-rate loans originated	988,375	652,011	612,066
Total loans originated	1,119,681	820,835	803,450
Purchases:			
Adjustable-rate:			
Real estate - one- to four-family	223,619	71,836	76,241
- multi-family and commercial	--	--	15,000
Fixed-rate:			
Real estate - one- to four-family	109,813	47,795	53,094
Total loans purchased	333,432	119,631	144,335
Transfer of modified loans to LHFS, net	(94,672)	--	--
Principal repayments	(1,083,731)	(899,178)	(855,980)

Decrease in other items, net	(7,605)	(8,069)	(2,652)
Net increase	$267,105	$33,219	$89,153

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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.

For one- to four-family loans and home equity loans, when a borrower fails to make a loan payment 15 days after the due date, a late charge is assessed and a notice is mailed. All delinquent balances are reviewed by collection personnel once the loan is 16 or more days past due. Attempts to contact the borrower occur by personal letter and, if no response is received, by telephone, with the purpose of establishing repayment arrangements for the borrower to bring the loan current. Repayment arrangements may be approved by a designated bank officer. Once a loan becomes 90 days delinquent, a demand letter is issued requiring the loan to be brought current or foreclosure procedures will be implemented. Once a loan becomes 120 days delinquent, and an acceptable repayment plan has not been established, the loan is forwarded to legal counsel to initiate foreclosure.

We monitor delinquencies on our purchased loan portfolio with reports we receive from the servicers. We monitor these servicer reports to ensure that the servicer is upholding the terms of the servicing agreement. The reports generally provide total principal and interest due and length of delinquency, and are used to prepare monthly management reports and perform delinquent loan trend analysis. Management also utilizes information from the servicers to monitor property valuations and identify the need to record specific valuation allowances. The servicers handle collection efforts per the terms of the servicing agreement. In the event of a foreclosure, the servicer obtains our approval prior to initiating foreclosure proceedings, and handles all aspects of the repossession and disposition of the repossessed property, which is also governed by the terms of the servicing agreement. We also monitor whether mortgagors who filed bankruptcy are meeting their obligation to pay the mortgage debt in accordance with the terms of the bankruptcy petition.

The following matrix shows the balance of one- to four-family 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 in September 2009 for 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 loans at September 30, 2009 was approximately 66%.

	Credit Score									
	Less than 660		661 to 700		701 to 750		751 and above		Total	
LTV ratio	Amount	% of total	Amount	% of total	Amount	% of total	Amount	% of total	Amount	% of total
	(Dollars in thousands)									
Less than 70%	$122,624	2.3 %	$157,038	3.0 %	$427,227	8.0 %	$1,953,728	36.7 %	$2,660,617	50.0 %
70% to 80%	118,695	2.3	130,138	2.4	417,022	7.8	1,210,400	22.7	1,876,255	35.2
More than 80%	75,919	1.4	78,920	1.5	215,991	4.1	414,233	7.8	785,063	14.8
	$317,238	6.0 %	$366,096	6.9 %	$1,060,240	19.9 %	$3,578,361	67.2 %	$5,321,935	100.0 %

Delinquent Loans. The following tables set forth our loans 30 - 89 days delinquent by type, number and amount as of the periods presented.

	Loans Delinquent for 30-89 Days at September 30,					
	2009		2008		2007	
	Number	Amount	Number	Amount	Number	Amount
	(Dollars in thousands)					
One- to four-family:						
Originated	159	$15,488	125	$13,244	149	$13,117
Purchased	41	10,556	37	7,083	26	3,854
Multi-family & commercial	--	--	--	--	--	--
Construction	--	--	--	--	--	--
Home equity	40	708	33	664	28	589
Other	15	89	21	118	29	172
	255	$26,841	216	$21,109	232	$17,732
Delinquent loans to total loans		0.48 %		0.40 %		0.34 %

Loans 30 to 89 days delinquent increased $5.7 million from $21.1 million at September 30, 2008 to $26.8 million at September 30, 2009. Of the 30-89 day delinquent purchased loans at September 30, 2009, approximately 50% are concentrated in Virginia, Illinois, Texas, Ohio, Pennsylvania and Missouri, with the remaining 50% spread across 14 other states. The following table presents the average percentage of loans, by principal balance, that entered the 30-89 days delinquent category during the past 12 months that paid off, returned to performing status, stayed 30-89 days delinquent, or progressed to the non-performing or REO categories.

	30-89 Day Delinquent Loan Trend Analysis					
	Paid Off	Performing	30-89 Days Delinquent	Non-Performing	REO	Total
Originated	5.2 %	37.8 %	35.9 %	18.9 %	2.2 %	100.0 %
Purchased	2.2 %	19.7 %	36.1 %	40.1 %	1.9 %	100.0 %

Total Portfolio Average	4.0 %	30.3 %	36.2 %	27.6 %	1.9 %	100.0 %

Non-performing Assets. The table below sets forth the number, amount and categories of non-performing assets. Non-performing assets consist of non-performing loans and real estate owned ("REO"). Non-performing loans are non-accrual loans that are 90 or more days delinquent or are in the process of foreclosure. The amount that was included in interest income on non-performing loans, before non-accruing status, was $473 thousand for the year ended September 30, 2009. The amount of additional interest income that would have been recorded on non-performing loans if they were not on non-accruing status was $603 thousand for the year ended September 30, 2009. REO includes assets acquired in settlement of loans.

	September 30,									
	2009		2008		2007		2006		2005	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
	(Dollars in thousands)									
Non-performing loans:										
One- to four-family:										
Originated	99	$ 9,248	70	$ 6,488	68	$ 4,941	56	$ 3,534	74	$ 4,471
Purchased	70	21,259	25	6,708	9	2,163	13	1,857	5	563
Multi-family & commercial	--	--	--	--	--	--	--	--	--	--
Construction	--	--	--	--	--	--	--	--	--	--
Consumer and Other Loans:										
Home equity	22	367	19	379	13	207	12	177	11	113
Other	8	45	11	91	7	41	3	41	4	11
	199	30,919	125	13,666	97	7,352	84	5,609	94	5,158
Real estate owned:										
One- to four-family:										
Originated (1)	51	5,702	36	2,228	30	2,036	34	2,401	30	1,368
Purchased	8	1,702	12	2,918	1	61	--	--	1	245
Multi-family & commercial	--	--	--	--	--	--	--	--	--	--
Construction	--	--	--	--	--	--	--	--	--	--
Consumer and Other Loans:										
Home equity	--	--	--	--	--	--	--	--	--	--
Other	--	--	--	--	--	--	1	8	1	40
	59	7,404	48	5,146	31	2,097	35	2,409	32	1,653
Total non-performing assets	258	$ 38,323	173	$ 18,812	128	$ 9,449	119	$ 8,018	126	$ 6,811
Non-performing loans as a percentage of total loans		0.55 %		0.26 %		0.14 %		0.11 %		0.09 %
Non-performing assets as a percentage of total assets		0. 46 %		0.23 %		0.12 %		0.10 %		0.08 %

(1) Real estate related consumer loans are included in the one- to four-family category as the underlying collateral is a one- to four-family property.

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At September 30, 2009, one-to four-family non-performing loans with LTV ratios greater than 80% comprised approximately 20% of total non-performing loans. Of these loans, approximately 80% have PMI which substantially reduces or eliminates the Bank's exposure to loss. The balance of one-to four-family non-performing loans with LTV ratios greater than 80% with no PMI was $1.3 million at September 30, 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%.

Non-performing loans increased $17.2 million from $13.7 million at September 30, 2008 to $30.9 million at September 30, 2009. Of the purchased non-performing loans at September 30, 2009, approximately 50% are concentrated in Arizona, Florida, and Nevada, with the remaining 50% spread across 21 other states. The increase in non-performing loans reflects the economic recession coupled with the continued deterioration of the housing market, particularly in some of the states in which we have purchased loans. The deteriorating 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 0.55% at September 30, 2009.

Impaired Loans. A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. Impaired loans totaled $41.4 million, $13.7 million, and $7.4 million for the fiscal years ended September 30, 2009, 2008, and 2007, respectively. All non-accrual loans and troubled debt restructurings ("TDRs") that have not been performing under the new terms for 12 consecutive months are considered to be impaired loans.

A TDR is the situation where, due to a borrower's financial difficulties, the Bank grants a concession to the borrower that the Bank would not otherwise have considered. The majority of the Bank's TDRs involve a restructuring of loan terms such as a temporary reduction in the payment amount to require only interest and escrow (if required) and extending the maturity date of the loan. At September 30, 2009, 2008, and 2007, the Bank had TDRs of $10.8 million, $918 thousand, and $230 thousand, respectively. We had no TDRs during the years ended September 30, 2006 and 2005. TDRs are not reported as non-performing loans, unless the restructured loans are more than 90 days delinquent. The balance of TDRs included in the impaired loan balance at September 30, 2009 was $10.8 million, of which 94%, or $10.2 million, were originated loans. Of the $10.8 million, $314 thousand was greater than 90 days delinquent and was included in the non-performing loan balance at September 30, 2009. The amount of interest recognized in interest income on total TDRs was $52 thousand for the year ended September 30, 2009. The amount of interest included in interest income on non-performing TDRs, before non-accruing status, was $6 thousand for the year ended September 30, 2009. The amount of additional interest income that would have been recorded on the non-performing TDR loans if they were not on non-accruing status was $5 thousand for the fiscal year ended September 30, 2009. Loans are removed from the TDR classification after 12 consecutive months of satisfactory repayment performance under the new loan terms.

Classified Assets. Federal regulations provide for the classification of loans and other assets, such as debt and equity securities considered by the OTS to be of lesser quality, as "special mention", "substandard", "doubtful" or "loss." Assets classified as "special mention" are performing loans on which known information about the collateral pledged or the possible credit problems of the borrowers have caused management to have doubts as to the ability of the borrowers to comply with present loan repayment terms and which may result in the future inclusion of such assets in the non-performing asset categories. TDRs that were performing prior to restructuring are reported as special mention until they have been performing for 12 consecutive months under the new loan terms. An asset is considered "substandard" if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. "Substandard" assets include those characterized by the "distinct possibility" that the insured institution will sustain "some loss" if the deficiencies are not corrected. TDRs that were more than 90 days delinquent at the time of restructuring are reported as substandard until they have been performing for 12 consecutive months under the new loan terms. Assets classified as "doubtful" have all of the weaknesses inherent as those classified "substandard," with the added characteristic that the weaknesses present make “collection or liquidation in full,” on the basis of currently existing facts, conditions and values “highly questionable and improbable.” Assets classified as “loss” are those considered “uncollectible” and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted.

When an insured institution classifies problem assets as either special mention, substandard or doubtful, it may establish specific valuation allowances in an amount deemed prudent by management and approved by the board of directors. General valuation allowances may be established to recognize the inherent risk associated with lending activities, but unlike specific valuation allowances, have not been allocated to specific problem assets within a portfolio of similar assets. When an insured institution classifies problem assets as "loss," it is required either to establish a specific valuation allowance for losses equal to 100% of that portion of the asset so classified or to charge off such amount. An institution's determination as to the classification of its assets and the amount of its allowance for loan losses is subject to review by the OTS and the FDIC, which may order the establishment of additional loss allowances.

In connection with the filing of the Bank's periodic reports with the OTS and in accordance with our asset classification policy, we regularly review the problem assets in our portfolio to determine whether any assets require classification in accordance with applicable regulations. The following table sets forth the balance of assets, less specific valuation allowances, classified as special mention, substandard, or doubtful at September 30, 2009.

	Special Mention		Substandard		Doubtful	
	Number	Amount	Number	Amount	Number	Amount
			(Dollars in thousands)			
Real Estate:						
One- to four-family						
Originated	46	$7,618	117	$12,295	--	$--
Purchased	1	262	70	17,056	--	--
Multi-family & commercial	1	10,953	--	--	--	--
Construction	--	--	--	--	--	--
Consumer and Other Loans:						
Home equity	6	71	25	564	--	--
Other	--	--	9	53	--	--
Total loans	54	18,904	221	29,968	--	--
Real estate owned						
Originated	--	--	51	5,702	--	--
Purchased	--	--	8	1,702	--	--
Total real estate owned	--	--	59	7,404	--	--
Total classified assets	54	$18,904	280	$37,372	--	$--

Allowance for Loan Losses and Provision for Loan Losses. Management maintains an allowance for loan losses to absorb known and inherent losses in the loan portfolio based on 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. 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. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K for a full discussion of our allowance for loan losses methodology. At September 30, 2009, our allowance for loan losses was $10.2 million, or 0.18% of the total loan portfolio and 33% of total non-performing loans. This compares with an allowance for loan losses of $5.8 million, or 0.11% of the total loan portfolio and 42% of total non-performing loans as of September 30, 2008.

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During fiscal year 2009, the Bank experienced 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. Based on these conditions, the Bank recorded a provision for loan losses of $6.4 million in fiscal year 2009. The $6.4 million provision primarily reflects an increase in the specific valuation allowances on purchased loans, an increase in the balance of non-performing purchased loans, an increase in the general valuation allowances primarily on 30-89 day delinquent purchased loans and an increase in charge-offs, also primarily related to purchased loans. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K for a full discussion of the changes in our allowance for loan losses methodology during fiscal year 2009.

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.

	Year Ended September 30,				
	2009	2008	2007	2006	2005
	(Dollars in thousands)				
Balance at beginning of period	$5,791	$4,181	$4,433	$4,598	$4,495
Charge-offs:					
One- to four-family loans-originated	226	86	8	95	91
One- to four-family loans-purchased	1781	321	--	--	--
Multi-family & commercial	--	--	--	--	--
Construction	--	--	--	--	--
Home equity	1	2	3	--	--
Other	24	32	16	37	56
Total charge-offs	2,032	441	27	132	147
Recoveries:					
One- to four-family	--	--	--	1	35
Multi-family & commercial	--	--	--	--	--
Construction	--	--	--	--	--
Home equity	--	--	--	--	--
Other	--	--	--	--	--
Total recoveries	--	--	--	1	35
Net charge-offs	2,032	441	27	131	112
Allowance on loans in the loan swap transaction	--	--	--	(281)	
Provision (recovery)	6,391	2,051	(225)	247	215
Balance at end of period	$10,150	$5,791	$4,181	$4,433	$4,598
Ratio of net charge-offs during the period to average loans outstanding (1)	0.04%	--%	--%	--%	--%
Ratio of net charge-offs during the period to average non-performing assets	7.11%	3.12%	0.31%	1.77%	1.31%
Allowance as a percentage of non-accruing loans	32.83%	42.37%	56.87%	79.03%	89.14%
Allowance as a percentage of total loans (end of period)	0.18%	0.11%	0.08%	0.08%	0.08%

(1) Ratios for the years ended September 30, 2008, 2007, 2006 and 2005 calculate to be less than 0.01%.

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 strict underwriting standards and the relative economic stability of the geographic areas in which the Bank originates loans.

The distribution of our allowance for loan losses at the dates indicated is summarized as follows:

	September 30,									
	2009		2008		2007		2006		2005	
	Amount of Loan Loss Allowance	Percent of Loans in Each Category to Total Loans	Amount of Loan Loss Allowance	Percent of Loans in Each Category to Total Loans	Amount of Loan Loss Allowance	Percent of Loans in Each Category to Total Loans	Amount of Loan Loss Allowance	Percent of Loans in Each Category to Total Loans	Amount of Loan Loss Allowance	Percent of Loans in Each Category to Total Loans
	(Dollars in thousands)									
One- to four-family										
Originated	$3,604	81.9 %	$3,075	80.7 %	$2,962	77.0 %	$2,819	72.9 %	$2,841	77.7 %
Purchased	5,972	12.3	2,307	13.6	773	17.1	977	21.3	773	17.1
Multi-family and commercial	227	1.4	54	1.1	57	1.1	54	1.1	270	0.9
Construction	22	0.7	41	0.6	69	0.6	258	0.4	129	0.5
Home equity	268	3.5	229	3.8	227	4.0	249	4.1	250	3.6
Other	57	0.2	85	0.2	93	0.2	76	0.2	83	0.2
	$10,150	100.0 %	$5,791	100.0 %	$4,181	100.0 %	$4,433	100.0 %	$4,346	100.0 %

Investment Activities

Federally chartered savings institutions have the authority to invest in various types of liquid assets, including U.S. Treasury obligations; securities of various federal agencies; government-sponsored enterprises, including callable agency securities and municipal bonds; certain certificates of deposit of insured banks and savings institutions; certain bankers' acceptances; repurchase agreements; and federal funds. Subject to various restrictions, federally chartered savings institutions may also invest their assets in investment grade commercial paper, corporate debt securities, and mutual funds whose assets conform to the investments that a federally chartered savings institution is otherwise authorized to make directly. As a member of the FHLB, the Bank is required to maintain a specified investment in the capital stock of the FHLB. See "Regulation - Federal Home Loan Bank System," "Capitol Federal Savings Bank," and "Qualified Thrift Lender Test" for a discussion of additional restrictions on our investment activities.

The Chief Investment Officer has the primary responsibility for the management of the Bank's investment portfolio, subject to the direction and guidance of the ALCO. The Chief Investment Officer considers various factors when making decisions, including the marketability, maturity, and tax consequences of the proposed investment. The composition of the investment portfolio will be affected by various market conditions, including the slope of the yield curve, the level of interest rates, the impact on the Bank's interest rate risk, the trend of net deposit flows, the volume of loan sales, the anticipated demand for funds via withdrawals, repayments of borrowings, and loan originations and purchases.

The general objectives of our investment portfolio are to provide liquidity when loan demand is high, to assist in maintaining earnings when loan demand is low, and to maximize earnings while satisfactorily managing liquidity risk, interest rate risk, reinvestment risk, and credit risk. Liquidity may increase or decrease depending upon the availability of funds and comparative yields on investments in relation to the return on loans. Cash flow projections are reviewed regularly and updated to assure that adequate liquidity is maintained. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Quantitative and Qualitative Disclosure about Market Risk" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

We classify securities as trading, available-for-sale ("AFS") or held-to-maturity ("HTM") at the date of purchase. Securities that are purchased and held principally for resale in the near future are classified as trading securities and are reported at fair value, with unrealized gains and losses reported in the consolidated statements of income. AFS securities are reported at fair value, with unrealized gains and losses reported as a component of accumulated other comprehensive income (loss) within stockholders' equity, net of deferred income taxes. HTM securities are reported at cost, adjusted for amortization of premium and accretion of discount. We have both the ability and intent to hold the HTM securities to maturity.

Management monitors the securities portfolio for other-than-temporary impairments ("OTTI") on an ongoing basis and performs a formal review quarterly. The process involves monitoring market events and other items that could impact issuers. Management assesses whether an OTTI is present when the fair value of a security is less than its amortized cost basis at the balance sheet date. Management determines whether OTTI losses should be recognized for impaired securities by assessing all known facts and circumstances surrounding the securities. If the Company intends to sell an impaired security or if it is more likely than not that the Company will be required to sell an impaired security before recovery of its amortized cost basis, OTTI has occurred and the difference between amortized cost and fair value will be recognized as a loss in earnings. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K for a full discussion of our OTTI policy. At September 30, 2009, no securities had been identified as other-than-temporarily impaired.

Investment Securities. Our investment securities portfolio consists of securities issued by government-sponsored enterprises (primarily issued by FNMA, FHLMC, and FHLB), taxable and non-taxable municipal bonds and trust preferred securities. At September 30, 2009, our investment securities portfolio totaled $480.7 million. The portfolio consists of securities classified as either HTM or AFS. See “Notes to Consolidated Financial Statements – Note 3 - Securities” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Financial Condition – Investment Securities” in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

During fiscal year 2009, our investment securities portfolio increased $338.3 million from $142.4 million at September 30, 2008 to $480.7 million at September 30, 2009. The increase was a result of purchases of $448.6 million. All of the purchases during fiscal year 2009 were fixed-rate and had a weighted average yield of 1.70% and a weighted average life of approximately one and a half years, due to the majority of the securities being callable. If market rates were to rise, the short-term nature of these securities may allow management the opportunity to reinvest the maturing funds at a higher yield.

Mortgage-Backed Securities. Our MBS portfolio consists primarily of securities issued by government-sponsored enterprises (primarily issued by FNMA and FHLMC). The principal and interest payments of MBS issued by FNMA and FHLMC are collateralized by the underlying mortgage assets with principal and interest payments guaranteed by the agencies. The underlying mortgage assets are conforming mortgages that comply with FNMA and FHLMC underwriting guidelines, as applicable, and are therefore not considered subprime. At September 30, 2009, our MBS portfolio totaled $1.99 billion.

A small portion of the MBS portfolio consists of non-agency collateralized mortgage obligations ("CMOs"). CMOs are special types of pass-through debt securities in which the stream of principal and interest payments on the underlying mortgages or MBS are used to create investment classes with different maturities and, in some cases, different amortization schedules, as well as a residual interest, with each such class possessing different risk characteristics. At September 30, 2009, we held CMOs totaling $52.7 million, none of which qualified as high risk mortgage securities as defined under OTS regulations. Our CMOs are currently classified as either HTM or AFS. We do not purchase residual interest bonds.

During fiscal year 2009, our MBS portfolio decreased $241.9 million from $2.23 billion at September 30, 2008, to $1.99 billion at September 30, 2009. The decrease in the portfolio was primarily a result of principal repayments that were not reinvested in their entirety in the MBS portfolio; rather, the funds were reinvested into short-term investment securities. Of the $191.2 million of MBS purchased during fiscal year 2009, $21.8 million were fixed-rate with a weighted average life of 3.84 years and a weighted average yield of 3.03% and $169.4 million were adjustable-rate with a weighted average yield of 2.72% and an average of 2.41 years until their first repricing opportunity. See "Notes to Consolidated Financial Statements – Note 3 - Securities" and "Management's Discussion and Analysis of Financial Condition and Results of Operations – Financial Condition – Mortgage-Backed Securities" in the Annual Report to Stockholders attached as Exhibit 13 to this Annual Report on Form 10-K.

MBS generally yield less than the loans that underlie such securities because of the servicing fee retained by the servicer and the cost of payment guarantees or credit enhancements that reduce credit risk. However, MBS are generally more liquid than individual mortgage loans and may be used to collateralize certain borrowings and public unit depositors of the Bank. In general, MBS issued or guaranteed by FNMA and FHLMC are weighted at no more than 20% for risk-based capital purposes compared to the 50% risk-weighting assigned to most non-securitized mortgage loans. On October 7, 2008, the OTS and other federal banking agencies proposed amendments to existing regulations that would reduce the risk weighting for MBS issued or guaranteed by FNMA and FHLMC from 20% to 10%.

When securities are purchased for a price other than par, the difference between the price paid and par is accreted to or amortized against the interest earned over the life of the security, depending on whether a discount or premium to par is paid. Movements in interest rates affect prepayment rates which, in turn, affect the average lives of MBS and the speed at which the discount or premium is accreted to or amortized against earnings.

While MBS issued or backed by FNMA and FHLMC carry a reduced credit risk compared to whole loans, these securities remain subject to the risk that a fluctuating interest rate environment, along with other factors such as the geographic distribution of the underlying mortgage loans, may alter the prepayment rate of the underlying mortgage loans and so affect both the prepayment speed, and value, of the securities. As noted above, the Bank, on some transactions, pays a premium over par value for MBS purchased. Large premiums may cause significant negative yield adjustments due to accelerated prepayments on the underlying mortgages.

The following table sets forth the composition of our investment and MBS portfolio at the dates indicated. Our investment securities portfolio at September 30, 2009 did not contain securities of any issuer with an aggregate book value in excess of 10% of our stockholders' equity, excluding those issued by government-sponsored enterprises.

	September 30,								
	2009			2008			2007		
	Carrying Value	% of Total	Fair Value	Carrying Value	% of Total	Fair Value	Carrying Value	% of Total	Fair Value
	(Dollars in thousands)								
AFS securities:									
MBS	$1,389,211	85.5 %	$1,389,211	$1,484,055	96.7 %	$1,484,055	$402,686	79.7 %	$402,686
U.S. government-sponsored enterprises	229,875	14.2	229,875	44,188	2.9	44,188	99,705	19.8	99,705
Trust preferred securities	2,110	0.1	2,110	2,655	0.2	2,655	--	--	--
Municipal bonds	2,799	0.2	2,799	2,743	0.2	2,743	2,719	0.5	2,719
Total AFS securities	1,623,995	100.0%	1,623,995	1,533,641	100.0%	1,533,641	505,110	100.0%	505,110
HTM securities:									
MBS	603,256	71.0 %	627,829	750,284	89.0 %	743,764	1,011,585	70.6 %	995,415
U.S. government-sponsored enterprises	175,394	20.7	175,929	37,397	4.4	36,769	401,431	28.0	398,598
Municipal bonds	70,526	8.3	73,000	55,376	6.6	55,442	20,313	1.4	20,342
Total HTM securities	849,176	100.0%	876,758	843,057	100.0%	835,975	1,433,329	100.0%	1,414,355
	$2,473,171		$2,500,753	$2,376,698		$2,369,616	$1,938,439		$1,919,465

The composition and maturities of the investment and MBS portfolio at September 30, 2009 are indicated in the following table by remaining contractual maturity, without consideration of call features or pre-refunding dates. Yields on tax-exempt investments are not calculated on a taxable equivalent basis.

	Less than 1 year		1 to 5 years		5 to 10 years		Over 10 years		Total		
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Fair Value
	(Dollars in thousands)										
AFS securities:											
MBS	$--	-- %	$ --	-- %	$102,329	4.98%	$1,286,882	4.56%	$1,389,211	4.59%	$1,389,211
U.S. government-sponsored enterprises	--	--	229,875	1.53	--	--	--	--	229,875	1.53	229,875
Trust preferred securities	--	--	--	--	--	--	2,110	1.96	2,110	1.96	2,110
Municipal bonds	--	--	385	3.54	1,158	3.70	1,256	3.90	2,799	3.77	2,799
Total AFS securities	--	--	230,260	1.54	103,487	4.97	1,290,248	4.55	1,623,995	4.15	1,623,995
HTM Securities:											
MBS	--	--	--	--	338,658	4.41	264,598	3.59	603,256	4.05	627,829
U.S. government-sponsored enterprises	--	--	175,394	2.01	--	--	--	--	175,394	2.01	175,929
Municipal bonds	247	2.78	20,992	2.55	32,563	3.39	16,724	2.74	70,526	2.98	73,000
Total HTM securities	247	2.78	196,386	2.07	371,221	4.32	281,322	3.54	849,176	3.54	876,758
	$247	2.78%	$426,646	1.78%	$474,708	4.46%	$1,571,570	4.37%	$2,473,171	3.94%	$2,500,753

Sources of Funds

General. Our sources of funds are deposits, borrowings, repayment of principal and interest on loans and MBS, interest earned on and maturities and calls of investment securities, and funds generated from operations.

Deposits. We offer a variety of retail deposit accounts having a wide range of interest rates and terms. Our deposits consist of savings accounts, money market accounts, interest-bearing and non-interest bearing checking accounts, and certificates of deposit. We rely primarily upon competitive pricing policies, marketing, and customer service to attract and retain deposits. The flow of deposits is influenced significantly by general economic conditions, changes in money market and prevailing interest rates, and competition. 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. In response to the economic recession, households have increased their personal savings rate which we believe has also contributed to our growth in deposits during fiscal year 2009.

The variety of deposit accounts we offer has allowed us to utilize strategic pricing to obtain funds and to respond with flexibility to changes in consumer demand. We endeavor to manage the pricing of our deposits in keeping with our asset and liability management, liquidity, and profitability objectives. Based on our experience, we believe that our deposits are stable sources of funds. Despite this stability, our ability to attract and maintain these deposits and the rates paid on them has been, and will continue to be, significantly affected by market conditions.

The following table sets forth our deposit flows during the periods indicated. Included in the table are brokered and public unit deposits which totaled $163.0 million, $180.6 million, and $193.0 million at September 30, 2009, 2008, and 2007, respectively.

	Year Ended September 30,		
	2009	2008	2007
	(Dollars in thousands)		
Opening balance	$3,923,883	$3,922,782	$3,900,431
Deposits	7,021,015	7,108,677	7,168,045
Withdrawals	6,818,534	7,242,121	7,289,077
Interest credited	102,245	134,545	143,383
Ending balance	$4,228,609	$3,923,883	$3,922,782
Net increase	$304,726	$1,101	$22,351
Percent increase	7.77 %	0.03 %	0.57 %

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The following table sets forth the dollar amount of deposits in the various types of deposit programs we offered for the periods indicated.

	Year Ended September 30,					
	2009		2008		2007	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
	(Dollars in thousands)					
Non-Certificates:						
Checking	$439,975	10.4 %	$400,461	10.2 %	$394,109	10.1 %
Savings	226,396	5.4	232,103	5.9	237,148	6.0
Money market	848,157	20.1	772,323	19.7	790,277	20.2
Total non-certificates	1,514,528	35.9	1,404,887	35.8	1,421,534	36.3