

MALVERN BANCORP, INC.
Form 10-K
December 29, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended: September 30, 2017

or

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

Commission File Number: 000-54835

MALVERN BANCORP, INC.

(Exact name of Registrant as specified in its charter)

Pennsylvania	45-5307782
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

42 E. Lancaster Avenue, Paoli, Pennsylvania	19301
(Address of Principal Executive Offices)	(Zip Code)

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

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

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

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

YES NO

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

YES NO

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

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

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

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

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

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

YES " NO x

The aggregate market value of the voting and non-voting common equity held by non-affiliates was approximately \$125.3 million, based on the last sale price on the NASDAQ Stock Market for the last business day of the Registrant's most recently completed second fiscal quarter.

The number of shares of the Issuer's common stock, par value \$0.01 per share, outstanding as of December 29, 2017 was 6,572,684.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 2018 Annual Meeting of Shareholders are incorporated by reference into Part III, Items 10-14 of this Form 10-K.

MALVERN BANCORP, INC.

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

PART I.

This report, in Item 1, Item 7 and elsewhere, includes forward-looking statements within the meaning of Sections 27A of the Securities Act of 1933, as amended, and 21E of the Securities Exchange Act of 1934, as amended, that involve inherent risks and uncertainties. This report contains certain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance and business of Malvern Bancorp, Inc. and its subsidiaries, including statements preceded by, followed by or that include words or phrases such as "believes," "expects," "anticipates," "plans," "trend," "objective," "continue," "remain," "pattern" or similar expressions or future or conditional verbs such as "will," "would," "should," "could," "might," "can," "may" or similar expressions. There are a number of important factors that could cause future results to differ materially from historical performance and these forward-looking statements. Factors that might cause such a difference include, but are not limited to: (1) competitive pressures among depository institutions may increase significantly; (2) changes in the interest rate environment may reduce interest margins; (3) prepayment speeds, loan origination and sale volumes, charge-offs and loan loss provisions may vary substantially from period to period; (4) general economic conditions may be less favorable than expected; (5) political developments, wars or other hostilities may disrupt or increase volatility in securities markets or other economic conditions; (6) legislative or regulatory changes or actions may adversely affect the businesses in which Malvern Bancorp, Inc. is engaged; (7) changes and trends in the securities markets may adversely impact Malvern Bancorp, Inc.; (8) a delayed or incomplete resolution of any regulatory issues could adversely impact our planning; (9) difficulties in integrating any businesses that we may acquire, which may increase our expenses and delay the achievement of any benefits that we may expect from such acquisitions; (10) the impact of reputation risk created by the developments discussed above on such matters as business generation and retention, funding and liquidity could be significant; and (11) the outcome of any regulatory or legal investigations and proceedings may not be anticipated. Further information on other factors that could affect the financial results of Malvern Bancorp, Inc. are included in Item 1A of this Annual Report on Form 10-K and in Malvern Bancorp's other filings with the Securities and Exchange Commission. These documents are available free of charge at the Commission's website at <http://www.sec.gov> and/or from Malvern Bancorp, Inc. Malvern Bancorp, Inc. assumes no obligation to update forward-looking statements at any time.

Item 1. Business

General

Malvern Bancorp, Inc., a Pennsylvania corporation (the "Company" or "Malvern Bancorp"), is the holding company for Malvern Federal Savings Bank ("Malvern Federal Savings" or the "Bank") and owns all of the issued and outstanding shares of the common stock of the Bank. The Bank is currently a federally chartered, FDIC-insured savings bank that was originally organized in 1887. In October 2017, the Bank filed an application with the Office of the Comptroller of the Currency (the "OCC") to convert from a federal savings bank to a national bank, with the name Malvern Bank, National Association. In connection with the charter conversion of the Bank, also in October 2017, the Company filed an application with the Federal Reserve Board (the "FRB") to convert to a bank holding company from a savings and loan holding company.

The conversions remain subject to the receipt of all required regulatory approvals. The Company and the Bank filed the conversion application in order to better match the Bank's regulatory charter to its current and planned business activity.

The Bank conducts business from its headquarters in Paoli, Pennsylvania, a suburb of Philadelphia, as well as eight other financial centers located throughout Chester and Delaware Counties, Pennsylvania and a Private Banking/Loan Production headquarters office in Morristown, New Jersey. The Bank also has a Private Banking/Loan Production office in Quakertown, Pennsylvania.

The Bank's principal business consists of attracting deposits from businesses and the general public primarily in Chester County, Pennsylvania and investing those deposits, together with borrowings and funds generated from operations, in one-to four-family residential real estate loans, construction and development loans, commercial and multi-family real estate loans, commercial business loans, home equity loans and lines of credit and other consumer loans, as well as investing in investment securities. In addition to Chester County, our lending efforts are focused in neighboring Bucks County, Montgomery County and Delaware County, which are also in southeastern Pennsylvania, New Jersey and the New York metropolitan marketplace. We also service client needs in the greater Philadelphia market area. Our primary market niche is providing personalized service to our client base.

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

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

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

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

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

The Bank has representative offices, which are not branches, in Palm Beach, Florida and Montchanin, Delaware.

SEC Reports and Corporate Governance

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

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

Market Area and Competition

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

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

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

Products and Services

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

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

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

The Bank, through its Malvern Associates insurance broker subsidiary, offers insurance services.

Deposits serve as the primary source of funding for our interest-earning assets, but also generate non-interest revenue through insufficient funds fees, stop payment fees, safe deposit rental fees, card income, including ATM fees and credit and debit card interchange, gift card fees, and other miscellaneous fees. In addition, the Bank generates additional non-interest revenue associated with residential loan origination and sale, loan servicing, late fees and merchant services.

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

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

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

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

The Bank's lending policies generally provide for lending inside of our primary market area. However, the Bank will make loans to persons outside of our primary market area when we deem it prudent to do so. In an effort to promote a high degree of asset quality, the Bank focuses primarily upon offering secured loans. However, the Bank does make unsecured loans to borrowers with high net worth and income profiles. The Bank generally requires loan customers to maintain deposit accounts with the Bank. In addition, the Bank generally provides for a minimum required rate of interest in its variable rate loans. We believe that having senior management on-site allows for an enhanced local presence and rapid decision-making that attracts borrowers. The Bank's lending limit to any one borrower is 15% of the Bank's capital base (defined as tangible equity plus the allowance for loan losses) for most loans (\$19.3 million) and 25% of the capital base for loans secured by readily marketable collateral (\$32.2 million). At September 30, 2017, the Bank's largest committed relationship totaled \$16.4 million.

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

Supervision and Regulation

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

As indicated above under "General," the Bank has filed an application with the OCC to convert from a federal savings bank to a national bank. The OCC will continue to be the primary regulator of the Bank after the conversion.

In connection with the proposed conversion of the Bank to a national bank, the Company filed an application with the FRB to convert from a savings and loan holding company to a bank holding company. The FRB will continue to be the primary regulator of the Company after such conversion.

The conversions remain subject to the receipt of all required regulatory approvals.

Dodd-Frank Act

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

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

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

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

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

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

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

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

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

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

Regulatory authority over savings and loan holding companies was transferred to the FRB. The FRB will continue to regulate the Company after its conversion to a bank holding company.

The Home Owners' Loan Act was amended to provide that leverage capital requirements and risk based capital requirements applicable to depository institutions and bank holding companies was extended to thrift holding companies. After the conversions, these requirements will continue to be applicable to the Bank and the holding company as a national bank and a bank holding company, respectively, but the Home Owners' Loan Act will no longer be applicable.

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

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

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

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

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

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

Item 402 of Regulation S-K has been amended to require companies to disclose the ratio of the Chief Executive Officer’s annual total compensation to the median annual total compensation of all other employees. This information must be reported for the first time for the first full fiscal year beginning on or after January 1, 2017.

Regulation of Malvern Bancorp, Inc.

Holding Company Acquisitions. Malvern Bancorp is currently a savings and loan holding company under the Home Owners' Loan Act, as amended, and is subject to examination and supervision by the FRB. Federal law generally prohibits a savings and loan holding company, without prior FRB approval, from acquiring the ownership or control of any other savings institution or savings and loan holding company, or all, or substantially all, of the assets or more than 5% of the voting shares of the savings institution or savings and loan holding company. These provisions also prohibit, among other things, any director or officer of a savings and loan holding company, or any individual who owns or controls more than 25% of the voting shares of such holding company, from acquiring control of any savings institution not a subsidiary of such savings and loan holding company, unless the acquisition is approved by the FRB.

The FRB may not approve any acquisition that would result in a multiple savings and loan holding company controlling savings institutions in more than one state, subject to two exceptions: (1) the approval of interstate supervisory acquisitions by savings and loan holding companies; and (2) the acquisition of a savings institution in another state if the laws of the state of the target savings institution specifically permit such acquisitions. The states vary in the extent to which they permit interstate savings and loan holding company acquisitions.

Once the Company is a bank holding company, it will be required to obtain the prior approval of the FRB before it may, by merger, purchase or otherwise, directly or indirectly acquire all or substantially all of the assets of any bank or bank holding company if, after such acquisition, it will own or control more than 5% of the voting shares of such bank or bank holding company.

Holding Company Activities. Malvern Bancorp currently operates as a unitary savings and loan holding company and is permitted to engage only in the activities permitted for financial institution holding companies or for multiple savings and loan holding companies. Multiple savings and loan holding companies are permitted to engage in the following activities: (i) activities permitted for a bank holding company under section 4(c) of the Bank Holding Company Act (unless the FRB prohibits or limits such 4(c) activities); (ii) furnishing or performing management services for a subsidiary savings association; (iii) conducting any insurance agency or escrow business; (iv) holding, managing, or liquidating assets owned by or acquired from a subsidiary savings association; (v) holding or managing properties used or occupied by a subsidiary savings association; (vi) acting as trustee under deeds of trust; or (vii) activities authorized by regulation as of March 5, 1987, to be engaged in by multiple savings and loan holding companies.

Under recently enacted legislation, savings and loan holding companies that have total assets over \$1 billion became subject to statutory capital requirements. As of September 30, 2017, Malvern Bancorp had total assets of \$1.05 billion and, accordingly, must meet the following four minimum capital ratios:

Capital Ratio	Regulatory Minimum	
Common Equity Tier 1 Capital	4.5	%
Tier 1 Leverage Capital	4.0	%
Tier 1 Risk-Based Capital	6.0	%
Total Risk-Based Capital	8.0	%

The leverage capital requirement is calculated as a percentage of total assets and the other three capital requirements are calculated as a percentage of risk-weighted assets. For a more detailed discussion of the capital rules, see “Recent Regulatory Capital Rules” under “Regulation of the Bank” below. The Bank and the Company are in compliance with all capital requirements applicable to them.

While there are no specific restrictions on the payment of dividends or other capital distributions for savings and loan holding companies, federal regulations do prescribe such restrictions on subsidiary savings institutions, as described below. The Bank is required to notify the FRB 30 days before declaring any dividend. In addition, the financial impact of a holding company on its subsidiary institution is a matter that is evaluated by the FRB and the agency has authority to order cessation of activities or divestiture of subsidiaries deemed to pose a threat to the safety and soundness of the institution.

As a national bank and a bank holding company, the Bank and the Company will be subject to the capital requirements promulgated by their respective regulators.

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

The Sarbanes-Oxley Act. As a public company, Malvern Bancorp is subject to the Sarbanes-Oxley Act of 2002 which addresses, among other issues, corporate governance, auditing and accounting, executive compensation, and enhanced and timely disclosure of corporate information. As directed by the Sarbanes-Oxley Act, our principal executive officer and principal financial officer are required to certify that our quarterly and annual reports do not contain any untrue statement of a material fact. The rules adopted by the Securities and Exchange Commission under the Sarbanes-Oxley Act have several requirements, including having these officers certify that: they are responsible for establishing, maintaining and regularly evaluating the effectiveness of our internal control over financial reporting; they have made certain disclosures to our auditors and the audit committee of the Board of Directors about our internal control over financial reporting; and they have included information in our quarterly and annual reports about their evaluation and whether there have been changes in our internal control over financial reporting or in other factors that could materially affect internal control over financial reporting.

Volcker Rule Regulations

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

Regulation of the Bank

General. As the Bank is currently a federally chartered savings bank, it is subject to the regulation of the OCC, as its primary federal regulator, and the FDIC, as the insurer of its deposit accounts, and, to a limited extent, the FRB. As the primary federal regulator of the Bank, the OCC has extensive authority over the operations of federally chartered savings institutions. As part of this authority, the Bank is required to file periodic reports with the OCC and is subject to periodic examinations by the OCC and the FDIC. The investment and lending authorities of savings institutions are

prescribed by federal laws and regulations, and such institutions are prohibited from engaging in any activities not permitted by such laws and regulations. Such regulation and supervision is primarily intended for the protection of depositors and the Deposit Insurance Fund, administered by the FDIC.

The OCC's enforcement authority over all savings institutions includes, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to initiate injunctive actions. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with the OCC.

After the conversion of the Bank to a national bank, it will continue to be subject to the regulation of the OCC, as its primary federal regulator, the FDIC will continue to be the insurer of its deposit accounts, and the FRB will be the primary regulator of the Company, as a bank holding company.

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

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

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

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

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

Regulatory Capital Requirements. Federally insured savings institutions are required to maintain minimum levels of regulatory capital. The OCC has established capital standards consisting of a "tangible capital requirement," a "leverage capital requirement" and "a risk-based capital requirement." The OCC also is authorized to impose capital requirements in excess of these standards on individual institutions on a case-by-case basis.

In July of 2013 the respective U.S. federal banking agencies issued final rules implementing Basel III and the Dodd-Frank Act capital requirements to be fully phased in on a global basis on January 1, 2019. The regulations establish a new tangible common equity capital requirement, increase the minimum requirement for the current Tier 1 risk-weighted asset (“RWA”) ratio, phase out certain kinds of intangibles treated as capital and certain types of instruments and change the risk weightings of certain assets used to determine required capital ratios. The new common equity Tier 1 capital component requires capital of the highest quality – predominantly composed of retained earnings and common stock instruments. For community banks such as the Bank, a common equity Tier 1 capital ratio of 4.5% became effective on January 1, 2015. The new capital rules also increased the current minimum Tier 1 capital ratio from 4.0% to 6.0% beginning on January 1, 2015. In addition, in order to make capital distributions and pay discretionary bonuses to executive officers without restriction, an institution must also maintain greater than 2.5% in common equity attributable to a capital conservation buffer to be phased in from January 1, 2016 until January 1, 2019. The new rules also increased the risk weights for several categories of assets, including an increase from 100% to 150% for certain acquisition, development and construction loans and more than 90-day past due exposures. The new capital rules maintain the general structure of the prompt corrective action rules, but incorporate the new common equity Tier 1 capital requirement and the increased Tier 1 RWA requirement into the prompt corrective action framework.

Savings institutions such as the Bank are currently required to satisfy the following capital requirements:

- Tangible capital requirement – “tangible” capital equal to at least 1.5% of adjusted total assets;

· Common equity Tier 1 capital requirement – generally consists of retained earnings and common stock instruments equal to at least 4.5% of “risk weighted” assets;

Tier 1 capital requirement – equal to at least 6.0%;

Leverage capital requirement – “core” capital equal to at least 3.0% of adjusted total assets for the most highly rated institutions;

An additional “cushion” of at least 100 basis points of core capital for all but the most highly rated savings associations effectively increasing their minimum Tier 1 leverage ratio to 4.0% or more; and

Risk-based capital requirement – “total” capital (a combination of core and “supplementary” capital) equal to at least 8.0% of “risk-weighted” assets.

Core capital generally consists of common stockholders' equity (including retained earnings). Tangible capital generally equals core capital minus intangible assets, with only a limited exception for purchased mortgage servicing rights. The Bank had no intangible assets at September 30, 2017. Both core and tangible capital are further reduced by an amount equal to a savings institution's debt and equity investments in subsidiaries engaged in activities not permissible to national banks (other than subsidiaries engaged in activities undertaken as agent for customers or in mortgage banking activities and subsidiary depository institutions or their holding companies). These adjustments do not affect the Bank's regulatory capital.

In determining compliance with the risk-based capital requirement, a savings institution is allowed to include both core capital and supplementary capital in its total capital, provided that the amount of supplementary capital included does not exceed the savings institution's core capital. Supplementary capital generally consists of general allowances for loan losses up to a maximum of 1.25% of risk-weighted assets, together with certain other items. In determining the required amount of risk-based capital, total assets, including certain off-balance sheet items, are multiplied by a risk weight based on the risks inherent in the type of assets. The risk weights range from 0% for cash and securities issued by the U.S. Government or unconditionally backed by the full faith and credit of the U.S. Government to 100% for loans (other than qualifying residential loans weighted at 80%) and repossessed assets.

Savings institutions must value securities available for sale at amortized cost for regulatory capital purposes. This means that in computing regulatory capital, savings institutions should add back any unrealized losses and deduct any unrealized gains, net of income taxes, on debt securities reported as a separate component of GAAP capital.

The table below sets forth the Bank's capital position relative to the OCC's regulatory capital requirements at September 30, 2017. As indicated in the table, the Bank exceeded all of its regulatory capital requirements. Malvern Bancorp, Inc. is now subject to the regulatory capital ratios imposed by the Dodd-Frank Act on savings and loan holding companies because it had assets in excess of \$1.0 billion as of September 30, 2017.

	Actual		Required for Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions		Excess Over Well-Capitalized Provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)							
Tier 1 leverage capital (to adjusted tangible assets)	\$ 120,902	12.02 %	\$ 40,234	4.00 %	\$ 50,292	5.00	\$ 70,610	7.02 %
Common equity Tier 1 (to risk-weighted assets)	\$ 120,902	14.75	36,894	4.50	53,292	6.50	67,610	8.25
Tier 1 risk-based capital (to risk-weighted assets)	\$ 120,902	14.75	49,192	6.00	65,590	8.00	55,312	6.75
Total risk-based capital (to risk-weighted assets)	\$ 129,369	15.78	65,590	8.00	81,987	10.00	47,382	5.78

Any savings institution that fails any of the capital requirements is subject to possible enforcement actions by the OCC or the FDIC. Such actions could include a capital directive, a cease and desist order, civil money penalties, the establishment of restrictions on the institution's operations, termination of federal deposit insurance and the appointment of a conservator or receiver. The OCC's capital regulation provides that such actions, through enforcement proceedings or otherwise, could require one or more of a variety of corrective actions.

Prompt Corrective Action. The following table shows the amount of capital associated with the different capital categories set forth in the prompt corrective action regulations.

Capital Category	Total Risk-Based Capital	Tier 1 Risk-Based Capital	Common Equity Tier 1 Capital	Tier 1 Leverage Capital
Well capitalized	10% or more	8% or more	6.5% or more	5% or more
Adequately capitalized	8% or more	6% or more	4.5% or more	4% or more
Undercapitalized	Less than 8%	Less than 6%	Less than 4.5%	Less than 4%
Significantly undercapitalized	Less than 6%	Less than 4%	Less than 3%	Less than 3%

In addition, an institution is “critically undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. Under specified circumstances, a federal banking agency may reclassify a well capitalized institution as adequately capitalized and may require an adequately capitalized institution or an undercapitalized institution to comply with supervisory actions as if it were in the next lower category (except that the FDIC may not reclassify a significantly undercapitalized institution as critically undercapitalized).

Capital Distributions. OCC regulations govern capital distributions by savings institutions, which include cash dividends, stock repurchases and other transactions charged to the capital account of a savings institution to make capital distributions. A savings institution must file an application for OCC approval of the capital distribution if either (1) the total capital distributions for the applicable calendar year exceed the sum of the institution's net income for that year to date plus the institution's retained net income for the preceding two years, (2) the institution would not be at least adequately capitalized following the distribution, (3) the distribution would violate any applicable statute, regulation, agreement or OCC-imposed condition, or (4) the institution is not eligible for expedited treatment of its filings. If an application is not required to be filed, savings institutions which are a subsidiary of a savings and loan holding company (as well as certain other institutions) must still file a notice with the OCC at least 30 days before the board of directors declares a dividend or approves a capital distribution if either (1) the institution would not be well capitalized following the distribution; (2) the proposed distribution would reduce the amount or retire any part of the institution's common or preferred stock or (3) the savings institution is a subsidiary of a savings and loan holding company and the proposed dividend is not a cash dividend. If a savings institution, such as the Bank, that is the subsidiary of a savings and loan holding company, has filed a notice with the FRB for a cash dividend and is not required to file an application or notice with the OCC for any of the reasons described above, then the savings institution is only required to provide an informational copy to the OCC of the notice filed with the FRB.

An institution that either before or after a proposed capital distribution fails to meet its then applicable minimum capital requirement or that has been notified that it needs more than normal supervision may not make any capital distributions without the prior written approval of the OCC. In addition, the OCC may prohibit a proposed capital distribution, which would otherwise be permitted by OCC regulations, if the OCC determines that such distribution would constitute an unsafe or unsound practice.

Under federal rules, an insured depository institution may not pay any dividend if payment would cause it to become undercapitalized or if it is already undercapitalized. In addition, federal regulators have the authority to restrict or prohibit the payment of dividends for safety and soundness reasons. The FDIC also prohibits an insured depository institution from paying dividends on its capital stock or interest on its capital notes or debentures (if such interest is required to be paid only out of net profits) or distributing any of its capital assets while it remains in default in the payment of any assessment due the FDIC. The Bank is currently not in default in any assessment payment to the FDIC.

Qualified Thrift Lender Test. All savings institutions are required to meet a qualified thrift lender, or QTL, test to avoid certain restrictions on their operations. A savings institution can comply with the QTL test by either qualifying as a domestic building and loan association as defined in the Internal Revenue Code or meeting the QTL test of the OCC.

Currently, the OCC's QTL test requires that 65% of an institution's "portfolio assets" (as defined) consist of certain housing and consumer-related assets on a monthly average basis in nine out of every 12 months. To be a qualified thrift lender under the IRS test, the savings institution must meet a "business operations test" and a "60 percent assets test," each defined in the Internal Revenue Code.

The Bank did not meet the QTL requirements effective December 31, 2016, and has filed an application with the OCC to convert to a national bank. In addition, the Company has filed an application with the FRB to convert to a bank holding company. The Company and the Bank filed the conversion applications in order to better match the Bank's regulatory charter to its current and planned business activity. Upon conversion to a national bank, the Bank will no longer be required to meet the QTL test.

Limitations on Transactions with Affiliates. Transactions between savings associations and any affiliate are governed by Sections 23A and 23B of the Federal Reserve Act as made applicable to savings associations by Section 11 of the Home Owners' Loan Act. An affiliate of a savings association includes any company or entity which controls the savings institution or that is controlled by a company that controls the savings association. In a holding company context, the holding company of a savings association (such as Malvern Bancorp) and any companies which are controlled by such holding company are affiliates of the savings association. Generally, Section 23A limits the extent to which the savings association or its subsidiaries may engage in "covered transactions" with any one affiliate to an amount equal to 10% of such association's capital stock and surplus, and contains an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such capital stock and surplus. Section 23B applies to "covered transactions" as well as certain other transactions and requires that all transactions be on terms substantially the same, or at least as favorable, to the savings association as those provided to a non-affiliate. The term "covered transaction" includes the making of loans to, purchase of assets from and issuance of a guarantee to an affiliate and similar transactions. Section 23B transactions also include the provision of services and the sale of assets by a savings association to an affiliate. In addition to the restrictions imposed by Sections 23A and 23B, Section 11 of the Home Owners' Loan Act prohibits a savings association from (i) making a loan or other extension of credit to an affiliate, except for any affiliate which engages only in certain activities which are permissible for bank holding companies, or (ii) purchasing or investing in any stocks, bonds, debentures, notes or similar obligations of any affiliate, except for affiliates which are subsidiaries of the savings association.

In addition, Sections 22(g) and (h) of the Federal Reserve Act as made applicable to savings associations by Section 11 of the Home Owners' Loan Act, place restrictions on loans to executive officers, directors and principal shareholders of the savings association and its affiliates. Under Section 22(h), loans to a director, an executive officer and to a greater than 10% shareholder of a savings association, and certain affiliated interests of either, may not

exceed, together with all other outstanding loans to such person and affiliated interests, the savings association's loans to one borrower limit (generally equal to 15% of the association's unimpaired capital and surplus). Section 22(h) also requires that loans to directors, executive officers and principal shareholders be made on terms substantially the same as offered in comparable transactions to other persons unless the loans are made pursuant to a benefit or compensation program that (i) is widely available to employees of the association and (ii) does not give preference to any director, executive officer or principal shareholder, or certain affiliated interests of either, over other employees of the savings association. Section 22(h) also requires prior board approval for certain loans. In addition, the aggregate amount of extensions of credit by a savings association to all insiders cannot exceed the association's unimpaired capital and surplus. Furthermore, Section 22(g) places additional restrictions on loans to executive officers. The Bank currently is subject to Sections 22(g) and (h) of the Federal Reserve Act and at September 30, 2017, was in compliance with the above restrictions.

Community Reinvestment Act. All federal savings associations have a responsibility under the Community Reinvestment Act and related regulations to help meet the credit needs of their communities, including low- and moderate-income neighborhoods. An institution's failure to comply with the provisions of the Community Reinvestment Act could result in restrictions on its activities. The Bank received a "satisfactory" Community Reinvestment Act rating in its most recently completed examination.

Anti-Money Laundering. All financial institutions, including savings and loan associations are subject to federal laws that are designed to prevent the use of the U.S. financial system to fund terrorist activities. Financial institutions operating in the United States are required to develop new anti-money laundering compliance programs, due diligence policies and controls to ensure the detection and reporting of money laundering. Such compliance programs are intended to supplement existing compliance requirements, also applicable to financial institutions, under the Bank Secrecy Act and the Office of Foreign Assets Control Regulations. The Bank has established policies and procedures to ensure compliance with these provisions, and their impact on our operations has not been material.

Federal Home Loan Bank System. The Bank is a member of the Federal Home Loan Bank of Pittsburgh, which is one of 12 regional Federal Home Loan Banks that administers the home financing credit function of savings institutions. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the board of directors of the FHLB. At September 30, 2017, the Bank had \$118.0 million of FHLB advances and \$150.0 million available on its line of credit with the FHLB.

As a member, the Bank is required to purchase and maintain stock in the FHLB of Pittsburgh in an amount equal to at least 1.0% of its aggregate unpaid residential mortgage loans or similar obligations at the beginning of each year. At September 30, 2017, Malvern Federal Savings Bank had \$5.6 million in FHLB stock, which was in compliance with this requirement.

The Federal Home Loan Banks are required to provide funds for the resolution of troubled savings institutions and to contribute to affordable housing programs through direct loans or interest subsidies on advances targeted for community investment and low-and moderate-income housing projects. The FHLB has communicated that it believes the calculation of risk-based capital under the current rules of the FHFA significantly overstates the market risk of the FHLB's private-label mortgage-backed securities in the current market environment and that it has enough capital to cover the risks reflected in the FHLB's balance sheet. As a result, an "other than temporary impairment" has not been recorded for the Bank's investment in FHLB stock. However, continued deterioration in the FHLB's financial position may result in impairment in the value of those securities. Management will continue to monitor the financial condition of the FHLB as it relates to, among other things, the recoverability of the Bank's investment.

Federal Reserve System. The Federal Reserve Board requires all depository institutions to maintain reserves against their transaction accounts (primarily NOW and Super NOW checking accounts) and non-personal time deposits. Because required reserves must be maintained in the form of vault cash or a noninterest-bearing account at a Federal Reserve Bank, the effect of this reserve requirement is to reduce an institution's earning assets. At September 30, 2017, the Bank had met its reserve requirement.

Employees

As of September 30, 2017, we had a total of 81 full-time equivalent employees. No employees are represented by a collective bargaining group, and we believe that our relationship with our employees is excellent.

Item 1A. Risk Factors.

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

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

Our financial condition and results of operations are affected by the ability of our borrowers to repay their loans, and in a timely manner. Lending money is a significant part of the banking business. Borrowers, however, do not always repay their loans. The risk of non-payment is assessed through our underwriting and loan review procedures based on several factors including credit risks of a particular borrower, changes in economic conditions, the duration of the loan and in the case of a collateralized loan, uncertainties as to the future value of the collateral and other factors. Despite our efforts, we do and will experience loan losses, and our financial condition and results of operations will be adversely affected. Our non-performing assets were approximately \$1.2 million at September 30, 2017. Our allowance for loan losses was approximately \$8.4 million at September 30, 2017. Our loans between thirty and eighty-nine days delinquent totaled \$5.0 million at September 30, 2017.

The changing economic environment may continue to create volatility and impact our operations and results.

Developments in the economy both specific and non-specific to the financial services industry have resulted in uncertainty in the financial markets in general and a related general economic uncertainty globally. As a consequence of the most recent protracted United States recessionary period, business activities across a wide range of industries have faced serious difficulties which have altered the way the industry approaches its markets. In recent fiscal periods, however; there have been bright spots in economic recovery; an increase in employment, in the housing market and in consumer spending, to cite some major factors. This is buoyed by, geo-political issues, fiscal and monetary policy shifts in the U.S. and the overall sustainability of positive sectors of the markets.

As a result of these factors affecting the overall economy, many lending institutions, including us, are cautious about the volatility and impact in the performance of their loans, including residential, construction, commercial and consumer loans. In addition, the values of real estate collateral supporting many commercial loans and home mortgages, while they have improved, remain subject to shifting dynamics in the broader markets. Moreover, competition among depository institutions for deposits and quality loans has increased significantly while the significant decline in economic growth has led to a slowdown in banking related activities. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial services industry. In particular, we may face the following risks in connection with these events:

• we potentially face increased regulation of our industry and compliance with such regulation may increase our costs and limit our ability to pursue business opportunities;

- customer demand for loans secured by real estate could be reduced due to weaker economic conditions, an increase in unemployment, a decrease in real estate values or an increase in interest rates;

the process we use to estimate losses inherent in our credit exposure requires difficult, subjective and complex judgments, including forecasts of economic conditions and how these economic conditions might impair the ability of our borrowers to repay their loans; and

- the value of the portfolio of investment securities that we hold may be adversely affected.

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

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

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

Different types of assets and liabilities may react differently, and at different times, to changes in market interest rates. We expect that we will periodically experience gaps in the interest rate sensitivities of our assets and liabilities. That means either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets, an increase in market rates of interest could reduce our net interest income. Likewise, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could reduce our net interest income. We are unable to predict changes in market interest rates, which are affected by many factors beyond our control, including inflation, deflation, recession, unemployment, money supply, domestic and international events and changes in the United States and other financial markets.

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

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

As of September 30, 2017, the primary composition of our total loan portfolio was as follows:

- commercial real estate loans of \$437.8 million, or 52.0% of total loans;
- construction and development loans of \$54.0 million, or 6.4% of total loans;
- commercial and industrial loans of \$116.3 million, or 13.8% of total loans;
- residential real estate loans of \$192.5 million, or 22.9% of total loans and
 - consumer loans of \$41.6 million, or 4.9% of total loans

Commercial real estate loans, which comprised 52.0% of our total loan portfolio as of September 30, 2017, expose us to a greater risk of loss than do residential mortgage loans. Commercial real estate loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to residential loans. Consequently, an adverse development with respect to one commercial loan or one credit relationship exposes us to a significantly greater risk of loss compared to an adverse development with respect to one residential mortgage loan. Any significant failure to pay on time by our customers or a significant default by our customers would materially and adversely affect us.

Although the economy in our market area generally, and the real estate market in particular, is improving, we can give you no assurance that it will continue to grow or that the rate of growth will accelerate to historic levels. Many factors could reduce or halt growth in our local economy and real estate market. Accordingly, it may be more difficult for commercial real estate borrowers to repay their loans in a timely manner in the current economic climate, as commercial real estate borrowers' ability to repay their loans frequently depends on the successful development of their properties. The deterioration of one or a few of our commercial real estate loans could cause a material increase in our level of nonperforming loans, which would result in a loss of revenue from these loans and could result in an increase in the provision for loan and lease losses and/or an increase in charge-offs, all of which could have a material adverse impact on our net income. We also may incur losses on commercial real estate loans due to declines in occupancy rates and rental rates, which may decrease property values and may decrease the likelihood that a borrower may find permanent financing alternatives. Given the continued weaknesses in the commercial real estate market in general, there may be loans where the value of our collateral has been negatively impacted. Any weakening of the commercial real estate market may increase the likelihood of default of these loans, which could negatively impact our loan portfolio's performance and asset quality. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, we could incur material losses. Any of these events could

increase our costs, require management time and attention, and materially and adversely affect us.

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

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

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

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

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

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

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

As we previously disclosed, in November 21, 2017, we were advised by BDO USA, LLP (“BDO”), our independent registered public accounting firm, that BDO had concluded that a material weakness in our internal controls over financial reporting existed, and that BDO’s report on the effectiveness of the Company’s internal control over financial reporting as of September 30, 2016 in Item 9A of the Company’s fiscal 2016 10-K that the Company’s internal control over financial reporting was effective as of September 30, 2016, should no longer be relied upon. BDO also informed us at that time that BDO’s audit report on the Company’s consolidated financial statements as of September 30, 2016 and 2015, and for each of the years in the two year period ended September 30, 2016, and BDO’s completed interim reviews of the Company’s consolidated interim financial statements as of and for the periods ended December 31, 2016, March 31, 2017 and June 30, 2017 (collectively, the “Specified Financial Statements”), should no longer be relied upon. We have restated the Specified Financial Statements, which were included in amendments to the Company’s fiscal 2016 10-K and 10-Qs for the first three quarters of fiscal 2017 that we have filed with the SEC. The matters described above related to our income tax account balances. As a result of the foregoing, management has determined that its internal control over financial reporting as of September 30, 2017 was not effective. See Item 9A herein. While management believes that it has remediated the underlying causes of this material weakness, if our remediation efforts do not operate effectively or if we are unsuccessful in implementing or following our remediation efforts, this may result in untimely or inaccurate reporting of our financial results.

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

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

The effects of the current economic conditions have been particularly severe in our primary market areas.

Substantially all of our loans are to individuals, businesses and real estate developers in Chester County, Pennsylvania and neighboring areas in southern Pennsylvania, New Jersey and the New York metropolitan marketplace. Our business depends significantly on general economic conditions in these market areas. While these areas at present show stable trends and good economic conditions, a change in these trends and/or an economic downturn in the local real estate market could harm our financial condition and results of operation in the following ways:

• Loan delinquencies may increase further;

• Problem assets and foreclosures may increase further;

• Demand for our products and services may decline;

• The carrying value of our other real estate owned may decline further; and

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Collateral for loans made by us, especially real estate, may continue to decline in value, in turn reducing a customer's borrowing power, and reducing the value of assets and collateral associated with our loans.

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

We are subject to extensive regulation, supervision and examination by the FRB, our primary federal regulator, the OCC, the Bank's primary federal regulator, and by the Federal Deposit Insurance Corporation, as insurer of the Bank's deposits. Such regulation and supervision governs the activities in which an institution and its holding company may engage and are intended primarily for the protection of the insurance fund and the depositors and borrowers of the Bank rather than for holders of our common stock. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of our assets and determination of the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our operations.

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

As of September 30, 2017, the fair value of our investment securities portfolio was approximately \$49.5 million. We have historically taken a conservative investment strategy, with concentrations of securities that are backed by government sponsored enterprises. Factors beyond our control can significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. These factors include, but are not limited to, rating agency actions in respect of the securities, defaults by the issuer or with respect to the underlying securities, and changes in market interest rates and continued instability in the capital markets. Any of these factors, among others, could cause other-than-temporary impairments and realized and/or unrealized losses in future periods and declines in other comprehensive income, which could have a material adverse effect on us. The process for determining whether impairment of a security is other-than-temporary usually requires complex, subjective judgments about the future financial performance and liquidity of the issuer and any collateral underlying the security in order to assess the probability of receiving all contractual principal and interest payments on the security.

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

Our ability to manage growth will depend upon our ability to continue to attract, hire and retain skilled employees. The loss of members of our senior management team, including those officers named in the summary compensation

table of our proxy statement, could have a material adverse effect on our results of operations and ability to execute our strategic goals. Our success will also depend on the ability of our officers and key employees to continue to implement and improve our operational and other systems, to manage multiple, concurrent customer relationships and to hire, train and manage our employees.

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

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

In addition, we outsource a majority of our data processing to certain third-party providers. If these third-party providers encounter difficulties, or if we have difficulty communicating with them, our ability to adequately process and account for transactions could be affected, and our business operations could be adversely affected. Threats to information security also exist in the processing of customer information through various other vendors and their personnel.

The occurrence of any system failures, interruption, or breach of security could damage our reputation and result in a loss of customers and business thereby subjecting us to additional regulatory scrutiny, or could expose us to litigation and possible financial liability. Furthermore, we may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures arising from operational and security risks. Any of these events could have a material adverse effect on our financial condition and results of operations.

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

On December 22, 2017, the Tax Cuts and Jobs Act (the “Act”) was signed into law. We are in the process of analyzing the Act and its possible effects on the Company and the Bank. The Act reduces the corporate tax rate to 21 percent from 35 percent, among other things. It could also require us to write down our deferred tax assets, which would reduce our net income during the first quarter of fiscal 2018. We cannot determine at this time the amount of any such write down, or the full effects of the Act on our business and financial results.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

At September 30, 2017, the Bank owns and maintains the premises in which the headquarters and six full-service financial centers are located, and leases a financial center in Glen Mills, Pennsylvania and in Villanova, Pennsylvania and a private banking office in Morristown, New Jersey. The Bank also leases representative offices in Montchanin, Delaware and Palm Beach, Florida. The location of each of the offices is as follows:

Paoli Headquarters	42 East Lancaster Avenue, Paoli, PA 19301
Paoli Financial Center	34 East Lancaster Avenue, Paoli, PA 19301
Malvern Financial Center	100 West King Street, Malvern, PA 19355
Exton Financial Center	109 North Pottstown Pike, Exton, PA 19341
Coventry Financial Center	1000 Ridge Road, Pottstown, PA 19465
Berwyn Financial Center	650 Lancaster Avenue, Berwyn, PA 19312

Lionville Financial Center	537 West Uwchlan Avenue, Downingtown, PA 19335
Glen Mills Financial Center	940 Baltimore Pike, Glen Mills, PA 19342
Villanova Private Banking Office	801 East Lancaster Avenue, Villanova, PA 19085
Morristown Private Banking Office	163 Madison Avenue, 3 rd Floor, Morristown, NJ 07960
Montchanin Representative Office	16 W. Rockland Road, Montchanin, Delaware 19710
Palm Beach Representative Office	205 Worth Avenue, Suite 308, Palm Beach, Florida 33480

Item 3. Legal Proceedings.

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

Item 4. Mine Safety Disclosures.

Not Applicable.

PART II.

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

The common stock of the Company is traded on the NASDAQ Global Select Market under the symbol "MLVF". As of September 30, 2017, the Company had 427 stockholders of record, not including the number of persons or entities whose stock is held in nominee or "street" name through various brokerage firms and banks. On September 30, 2017, the closing sale price was \$26.75.

The following table sets forth the high and low closing sales price of a share of the Company's common stock for the years ended September 30, 2017 and 2016.

	Year Ended September 30,			
	2017		2016	
	High	Low	High	Low
First Quarter	\$21.25	\$16.36	\$17.70	\$15.31
Second Quarter	\$22.00	\$19.35	\$17.65	\$15.67
Third Quarter	\$24.60	\$21.10	\$16.50	\$15.40
Fourth Quarter	\$26.95	\$22.50	\$17.20	\$15.00

For the years ended September 30, 2017 and 2016, no cash dividends per share of common stock were declared by the Company.

Stockholders Return Comparison

Set forth below is a line graph presentation comparing the cumulative stockholder return on the Company's common stock, on a dividend reinvested basis, against the cumulative total returns of the Standard & Poor's Composite, the SNL Mid-Atlantic Bank Index and the SNL Mid-Atlantic Thrift Index for the period from October 12, 2012 through September 30, 2017.

Item 6. Selected Financial Data.

The following tables set forth selected consolidated financial data as of the dates and for the periods presented. The selected consolidated statement of financial condition data as of September 30, 2017 and 2016 and the selected consolidated summary of operating data for the years ended September 30, 2017, 2016 and 2015 have been derived from our audited consolidated financial statements and related notes that we have included elsewhere in this Annual Report. The selected consolidated statement of financial condition data as of September 30, 2015, 2014 and 2013 and the selected consolidated summary of operating data for the years ended September 30, 2014 and 2013 have been derived from audited consolidated financial statements that are not presented in this Annual Report.

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

All numbers set forth below reflect the restatements described under Item 7 herein.

	At September 30,				
	2017	2016	2015	2014	2013
	(Dollars in thousands)				
Summary of Operating Data:					
Total interest and dividend income	\$33,782	\$25,244	\$20,462	\$20,167	\$22,301
Total interest expense	9,446	6,732	5,248	5,071	6,944
Net interest income	24,336	18,512	15,214	15,096	15,357
Provision for loan losses	2,791	947	90	263	11,235
Net interest income after provision for loan losses	21,545	17,565	15,124	14,833	4,122
Total other income	2,341	2,333	2,535	2,155	2,860
Total other expenses	15,147	13,922	13,961	16,644	19,775
Income tax expense (benefit)	2,922	(6,174)	(970)	(367)	6,010
Net income (loss)	\$5,817	\$12,150	\$4,668	\$711	\$(18,803)
Earnings (loss) per share	\$0.90	\$1.90	\$0.73	\$0.11	\$(2.96)
Dividends per share	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Statement of Financial Condition Data					
Securities available for sale	\$14,587	\$66,387	\$128,354	\$100,943	\$124,667
Securities held to maturity	34,915	40,551	57,221	-	-
Loans held for sale	-	-	-	-	10,367
Loans receivable, net	834,331	574,160	391,307	386,074	401,857

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Total assets	1,046,012	821,272	655,690	542,264	601,554
Deposits	790,396	602,046	465,522	412,953	484,596
FHLB borrowings	118,000	118,000	103,000	48,000	38,000
Other short-term borrowing	5,000	—	—	—	—
Shareholders' equity	102,520	96,157	82,749	77,160	75,406
Allowance for loan losses	8,405	5,434	4,667	4,589	5,090
Non-accrual loans in portfolio	1,038	1,617	1,399	2,391	1,901
Non-performing assets in portfolio	1,211	2,313	2,567	4,355	5,863
Performing troubled debt restructurings in portfolio	2,238	2,039	1,091	1,009	1,346
Non-performing assets and performing troubled debt restructurings in portfolio	3,449	4,352	3,658	5,364	7,209
Performance Ratios:					
Return on average assets	0.62	% 1.61	% 0.75	% 0.12	% (2.79)%
Return on average equity	5.93	14.07	5.79	0.94	(20.24)
Interest rate spread ⁽¹⁾	2.57	2.53	2.48	2.59	2.25
Net interest margin ⁽²⁾	2.72	2.65	2.62	2.74	2.43
Non-interest expenses to average total assets	1.62	1.85	2.25	2.84	2.93
Efficiency ratio ⁽³⁾	57.39	67.22	77.62	96.74	110.95
Asset Quality Ratios:					
Non-accrual loans as a percent of gross loans	0.12	0.28	0.35	0.62	0.47
Non-performing assets as a percent of total assets	0.12	0.28	0.39	0.80	0.97
Non-performing assets and performing troubled debt restructurings as a percent of total assets	0.33	0.53	0.56	0.99	1.20
Allowance for loan losses as a percent of gross loans	1.00	0.94	1.18	1.18	1.26
Allowance for loan losses as a percent of non-performing loans	694.04	234.93	333.60	191.93	267.75
Net (recovery) charge-offs to average loans outstanding	(0.02)	0.04	0.00	0.19	3.07
Capital Ratios⁽⁴⁾:					
Total risk-based capital to risk weighted assets	15.78	15.42	17.30	20.87	18.97
Tier 1 risk-based capital to risk weighted assets	14.75	14.50	16.21	19.62	17.72
Tangible capital to tangible assets	N/A	N/A	N/A	12.17	10.91
Tier 1 leverage (core) capital to adjustable tangible assets	12.02	10.98	11.01	12.17	10.91
Shareholders' equity to total assets	9.80	11.71	12.62	14.23	12.54

- (1) Represents the difference between the weighted average yield on interest earning assets and the weighted average cost of interest bearing liabilities.
- (2) Net interest income divided by average interest earning assets.
Efficiency ratio, which is a non-GAAP financial measure, is computed by dividing other expense, less non-core items, by net interest income on a tax equivalent basis plus other income, excluding net securities gains (losses).
- (3) Included in non-core items are costs which include expenses related to the Company's corporate restructuring initiatives. The Company believes these adjustments are necessary to provide the most accurate measure of core operating results as a means to evaluate comparative results. See table below for the calculation of the efficiency ratio.
- (4) Other than shareholders' equity to total assets, all capital ratios are for the Bank only.

The following table presents the calculation of efficiency ratio.

	At September 30,				
	2017	2016	2015	2014	2013
	(Dollars in thousands)				
Other expense	\$15,147	\$13,922	\$13,961	\$16,644	\$19,775
Less: non-core items	159	111	439	—	—
Other expense, excluding non-core items	14,988	13,811	13,522	16,644	19,775
Net interest income (tax-equivalent basis)	24,512	18,777	15,400	15,152	15,442
Other income, excluding net investment securities gains	1,878	1,768	2,020	2,052	2,381
Total	26,390	20,545	17,420	17,204	17,823
Efficiency ratio	56.79 %	67.22 %	77.62 %	96.74 %	110.95 %

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

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

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

See Page 1 of this Annual Report on Form 10-K for information regarding forward-looking statements.

Explanatory Note

As previously reported in a Form 8-K filed on November 28, 2017 (the “Item 4.02 8-K”), on November 21, 2017, the Company was advised by BDO USA, LLP (“BDO”), its independent registered public accounting firm, that the Company should disclose that BDO’s audit report on the Company’s consolidated financial statements as of September 30, 2016 and 2015, and for each of the years in the two year period ended September 30, 2016, and BDO’s completed interim reviews of the Company’s consolidated interim financial statements as of and for the periods ended December 31, 2016, March 31, 2017 and June 30, 2017 (collectively, the “Specified Financial Statements”), should no longer be relied upon. As a result of the foregoing, the Company restated the Specified Financial Statements, which were included in amendments to the Company’s fiscal 2016 10-K and 10-Qs for the first three quarters of fiscal 2017 that the Company filed with the SEC.

The matters described above relate to the Company’s income tax account balances. The effect of these matters is to increase net income for fiscal 2016 by approximately \$208,000, fiscal 2015 by approximately \$970,000 and fiscal 2014 by approximately \$388,000. For the fiscal year ended September 30, 2017, the net effect is a decrease to net income of approximately \$796,000 and an increase in tax liability account of \$796,000. These matters have no effect on the Company’s cash position, net interest margin, pre tax income or the Company’s operating expenses.

See Item 9A herein.

All numbers in this Annual Report on Form 10-K reflect the restatements referred to above.

Critical Accounting Policies and Estimates

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

Allowance for Loan Losses

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

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

The evaluation also details historical losses by loan category and the resulting loan loss rates which are projected for current loan total amounts. Loss estimates for specified problem loans are also detailed. In addition, OCC, as an integral part of their examination process, periodically review our allowance for loan losses. The OCC may require us to make additional provisions for loan losses based upon information available to them at the time of their examination. All of the factors considered in the analysis of the adequacy of the allowance for loan losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required that could materially adversely impact earnings in future periods.

Other Real Estate Owned

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

Fair Value Measurements

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

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

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

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

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

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

Fair value measurements for assets where there exists limited or no observable market data and, therefore, are based primarily upon the Company's or other third-party's estimates, are often calculated based on the characteristics of the asset, the economic and competitive environment and other such factors. Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset. Additionally, there may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, that could significantly affect the results of current or future valuations. At September 30, 2017, the Company had \$137,000 of assets that were measured at fair value on a non-recurring basis using Level 3 measurements.

Income Taxes

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

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

Realization of a deferred tax asset requires us to exercise significant judgment and is inherently uncertain because it requires the prediction of future occurrences. Our net deferred tax asset amounted to \$6.7 million and \$8.8 million at September 30, 2017 and at September 30, 2016, respectively. Our total deferred tax assets decreased to \$7.0 million at September 30, 2017 compared to \$9.4 million at September 30, 2016. The Company's DTA allowance as of September 30, 2016 of \$61,000 has decreased by \$61,000 to zero at September 30, 2017.

Due to the improvement in the Company's earnings performance, both on a book and taxable income basis, the Company achieved three consecutive fiscal years of positive book income for the fiscal year ended September 30, 2017 and has already exhibited eight consecutive quarters of positive taxable income as of the quarter ended September 30, 2017.

Other-Than-Temporary Impairment of Securities

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

Derivatives

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

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

Overview and Strategy

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

Improving Core Earnings. With interest rates falling to historically low levels, it has become increasingly difficult for financial institutions to maintain acceptable levels of net interest income. Until recently, with the Bank unable to grow its asset base and loan portfolio, increasing interest income has been a challenge. This lack of growth in the loan portfolio through fiscal year-end 2014, combined with higher deposit and borrowing costs, have all contributed to a decline in the Banks' net interest margin. In an effort to achieve consistent sustainable earnings, i.e. improve the net interest margin, we are implementing specific product and pricing strategies designed to increase the yield on loans and reduce the cost of funding. In fiscal 2014, we resumed originating commercial real estate loans and commercial business loans, which have higher yields than single-family residential mortgage loans, on a relatively modest basis in accordance with our business plan and our strengthened loan underwriting and loan administration policies and procedures. We also have established a funding composition plan, which is designed to increase checking accounts, primarily non-interest-bearing accounts, as well as savings and money market accounts. We are attempting to increase our core deposits, which we define as all deposit accounts other than certificates of deposit. At September 30, 2017, our core deposits amounted to 65.6% of total deposits (\$518.6 million), compared to 58.4% of total deposits (\$351.8 million) at September 30, 2016. We have continued our promotional efforts to increase core deposits. We review our deposit products on an ongoing basis and we are considering additional deposit products and are currently offering more flexible delivery options, such as mobile banking, as part of our efforts to increase core deposits. We expect to increase our commercial checking accounts and we plan to enhance our cross-marketing as part of our efforts to gain additional deposit relationships with our loan customers.

Maintain Low Levels of Problem Assets. We are continuing in our efforts to maintain low levels of problem assets. At September 30, 2017, our total non-performing assets in portfolio were \$1.2 million or 0.12% of total assets, reflecting a reduction of \$4.7 million, or 79.4%, compared to \$5.9 million of total non-performing assets at September

30, 2013 (when total non-performing assets amounted to 0.97% of total assets). The October 2013 bulk sale of problem loans resulted in a dramatic reduction of the Company's non-performing assets. The bulk sale was undertaken as an efficient mechanism for disposing of non-performing and underperforming assets and improving the Bank's credit quality in the process. As a result of the sale, the Company significantly reduced its exposure to sectors that experienced economic weakness and significant declines in collateral valuations and has substantially reduced the amount of non-accruing loans.

Growing Our Loan Portfolio and Resuming Commercial Real Estate and Construction and Development Lending. We have resumed, on a relatively modest basis, the origination of commercial real estate loans and construction and development loans in our market area. Such loans are being underwritten in accordance with our strengthened loan underwriting standards and our enhanced credit review and administration procedures. We continue to believe that we can be a successful niche lender to small and mid-sized commercial borrowers and homebuilders in our market area. In light of the improvements in economic conditions and real estate values, we believe that the resumption of commercial real estate and construction and development lending in a planned, deliberative fashion with the loan underwriting and administrative enhancements that we have implemented in recent periods, together with modest loan growth, will increase our interest income and our returns in future periods.

Increasing Market Share Penetration. The Company continues to move forward with momentum in expanding our presence in key markets in 2017. We continue to execute on our business plans and are positioning the Company to take advantage of the growth activity we are achieving in our markets, which included our new wealth management locations in Palm Beach, Florida and Montchanin, Delaware. With the entry into Florida and Delaware markets, we are working to solidify and expand the service relationship with our new customers. We remain excited by the potential to create incremental shareholder value from our strategic growth. We believe that our earnings performance demonstrates the Company's commitment to achieving meaningful growth, an essential component of providing consistent and favorable long-term returns to our shareholders. However, while we continue to see an improvement in balance sheet strength and core earnings performance, we remain cautious about the credit stability of the broader markets. We operate in a competitive market area for banking products and services. In recent years, we have been working to increase our deposit share in Chester and Delaware counties and we increased our marketing and promotional efforts. During fiscal year 2017, we continued to execute on our business plans and have positioned the Company to take advantage of the growth activity we are achieving in our markets, which includes our two new private banking/loan production offices in Villanova, Pennsylvania and Morristown, New Jersey. Our business plans call for us to achieve the transition to a commercial bank balance sheet. With entry into New Jersey lending market, we are working to solidify and expand the service relationship with our new customers. In our effort to increase market share as well as non-interest income, we plan to evaluate increasing our business in non-traditional products, such as wealth management.

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

Introduction

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

Results of Operations

Net income for the year ended September 30, 2017 was \$5.8 million as compared to \$12.2 million earned in fiscal 2016 and \$4.7 million earned in fiscal 2015. Our net income for fiscal 2017 decreased by 52.1 percent compared to fiscal 2016. For fiscal 2017, the fully diluted earnings per common share was \$0.90 as compared with \$1.90 per share in fiscal 2016 and \$0.73 per share in fiscal 2015. However, net income prior to income tax expense (benefit) showed \$8.7 million in 2017 and \$6.0 million in 2016, an increase of \$2.8 million or 46.2%.

For the year ended September 30, 2017, the Company's return on average shareholders' equity ("ROE") was 5.93 percent and its return on average assets ("ROA") was 0.62 percent. The comparable ratios for the year ended September 30, 2016, were ROE of 14.07 percent and ROA of 1.61 percent.

Earnings for fiscal 2017 benefitted from increase in net income, as well as an increase in non interest income. The increases in non interest income, primarily in service charges and other fees, rental income and an increase in net gain on sale of loans, which were partially offset by an decrease in net gain on sale of investments and a decrease in earnings on bank owned life insurance. The increase in non-interest expenses was due to increases in salaries and benefits, occupancy expenses, advertising expenses, data processing expense, professional fees and other operating expenses. The increase was offset by decreases in FDIC insurance.

Use of Non-GAAP Disclosures

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

Net Interest Income

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

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

(Dollars in thousands)	Year Ended September 30, 2017			2016			2015		
	Amount	Increase (Decrease) from Prior Year	Percent Change	Amount	Increase (Decrease) from Prior Year	Percent Change	Amount	Increase (Decrease) from Prior Year	Percent Change
Interest income:									
Loans, including fees	\$30,850	\$9,634	45.41	\$21,216	\$4,724	28.64	\$16,492	\$(1,251)	(7.05)
Investment securities	2,206	(1,624)	(42.40)	3,830	57	1.51	3,773	1,470	63.83
Dividends, restricted stock	257	7	2.80	250	(61)	(19.61)	311	188	152.85
Interest-bearing cash accounts	631	418	196.24	213	141	195.83	72	18	33.33
Total interest income	33,944	8,435	33.07	25,509	4,861	23.54	20,648	425	2.10
Interest expense:									
Deposits	6,236	1,699	37.45	4,537	1,106	32.24	3,431	(538)	(13.56)
Short-term borrowings	34	34	100.00	—	—	—	—	—	—
Long-term borrowings	2,176	(19)	(0.87)	2,195	378	20.80	1,817	715	64.88
Borrowings	1,000	1,000	100.00	—	—	—	—	—	—
Total interest expense	9,446	2,714	40.31	6,732	1,484	28.28	5,248	177	3.49
Net interest income on a fully tax-equivalent basis	24,498	5,721	30.47	18,777	3,377	21.93	15,400	248	1.64
Tax-equivalent adjustment ⁽¹⁾	(162)	103	38.87	(265)	(79)	42.47	(186)	(130)	232.14
Net interest income, as reported under GAAP	\$24,336	\$5,824	31.46	\$18,512	\$3,298	21.68	\$15,214	\$118	0.78

⁽¹⁾ Computed using a federal income tax rate of 34 percent for Years ended September 30, 2017, 2016 and 2015.

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

Net interest income, on a tax-equivalent basis, for the year ended September 30, 2017 increased \$5.7 million, or 30.5 percent, to \$24.5 million, from \$18.8 million for fiscal 2016. The Company's net interest margin increased seven basis points to 2.72 percent in fiscal 2017 from 2.65 percent for the fiscal year ended September 30, 2016. From fiscal 2015 to fiscal 2016, net interest income on a tax equivalent basis increased by \$3.4 million and the net interest margin increased by three basis points. During fiscal 2017, our net interest margin was impacted by increases in the yield on investments and interest-bearing cash accounts, as well as increase in the cost of deposits and borrowings and decreases in the yield on loans and FHLB stock.

The increase in net interest income during fiscal 2017 was attributable in part to the slight increase in short-term interest rates that continued to remain at historic low levels throughout 2017. The Company experienced growth of \$7.6 million in non-interest bearing deposits during fiscal 2017 and \$157.3 million in interest-bearing demand, savings, money market and time deposits under \$100,000 during fiscal 2017 as customers' desire for safety and liquidity continued to remain as one of their primary investment concerns. During the twelve months ended September 30, 2017, the Company's net interest spread increased by four basis points reflecting a 17 basis points increase in the average yield on interest-earning assets as well as a 13 basis points increase in the average interest rates paid on interest-bearing liabilities.

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

For the year ended September 30, 2016, average interest-earning assets increased by \$122.7 million to \$709.5 million, as compared with the year ended September 30, 2015. The fiscal 2016 change in average interest-earning asset volume was primarily due to increased loan volume. Average interest-bearing liabilities increased by \$123.7 million in fiscal 2016 compared to fiscal 2015, due primarily to an increase in average interest-bearing deposits of \$99.7 million and a \$24.0 million increase in average borrowings.

The factors underlying the year-to-year changes in net interest income are reflected in the tables presented on pages 27 and 28, each of which have been presented on a tax-equivalent basis (assuming a 34 percent tax rate for fiscal 2017, 2016 and 2015). The table on page 30 (Average Statements of Condition with Interest and Average Rates) shows the Company's consolidated average balance of assets, liabilities and shareholders' equity, the amount of income produced from interest-earning assets and the amount of expense incurred from interest-bearing liabilities, and net interest income as a percentage of average interest-earning assets.

Net Interest Margin

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

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

(In thousands)	Fiscal 2017/2016			Fiscal 2016/2015		
	Increase (Decrease)			Increase (Decrease)		
	Due to Change in:			Due to Change in:		
	Average	Average	Net	Average	Average	Net
	Volume	Rate	Change	Volume	Rate	Change
Interest-earning assets:						
Loans, including fees	\$9,628	\$ 6	\$9,634	\$5,313	\$ (589)	\$ 4,724
Investment securities	(1,656)	32	(1,624)	(202)	259	57
Interest-bearing cash accounts	116	302	418	12	129	141
Dividends, restricted stock	9	(3)	6	62	(123)	(61)
Total interest-earning assets	8,097	337	8,434	5,185	(324)	4,861
Interest-bearing liabilities:						
Money market deposits	599	597	1,196	246	357	603
Savings deposits	(1)	6	5	—	3	3
Certificates of deposit	440	(72)	368	432	12	444
Other interest-bearing deposits	20	110	130	3	53	56
Total interest-bearing deposits	1,058	641	1,699	681	425	1,106
Borrowings	403	611	1,014	475	(97)	378
Total interest-bearing liabilities	1,461	1,252	2,713	1,156	328	1,484
Change in net interest income	\$6,636	\$ (915)	\$5,721	\$4,029	\$ (652)	\$ 3,377

Interest income on a tax-equivalent basis for the year ended September 30, 2017 increased by approximately \$8.4 million or 33.1 percent as compared with the year ended September 30, 2016. This increase was due primarily to increases in the balances of the Company's loans. Interest income on a tax-equivalent basis for the year ended September 30, 2016 increased by approximately \$4.9 million or 23.5 percent as compared with the year ended September 30, 2015. This increase was due primarily to increases in the balances of the Company's loans.

The average balance of the Company's loan portfolio increased \$230.5 million in fiscal 2017 to \$738.5 million from \$508.0 million in fiscal 2016, primarily driven by an increase in commercial real estate loans.

The average loan portfolio represented approximately 82.0 percent of the Company's interest-earning assets (on average) during fiscal 2017 and 71.6 percent for fiscal 2016. Average investment securities decreased during fiscal 2017 by \$64.8 million compared to fiscal 2016. The average yield on interest-earning assets increased from 3.60 percent in fiscal 2016 to 3.77 percent in fiscal 2017.

Interest expense for the year ended September 30, 2017 was principally impacted by both volume and rate mix related factors. The changes resulted in increased expense of \$2.7 million due to an increase in deposits and borrowings in fiscal 2017. Average interest-bearing liabilities increased \$158.5 million from fiscal 2016 to fiscal 2017. For the year ended September 30, 2016, interest expense increased \$1.5 million as compared with fiscal 2015, principally reflecting an increase in deposits and borrowings. Average interest-bearing liabilities increased \$123.7 million from fiscal 2015 to fiscal 2016.

The Company's net interest spread on a tax-equivalent basis (i.e., the average yield on average interest-earning assets, calculated on a tax equivalent basis, minus the average rate paid on interest-bearing liabilities) increased four basis points to 2.57 percent in fiscal 2017 from 2.53 percent for the year ended September 30, 2016. The increase in fiscal 2017 reflected an increase of spreads between yields earned on investments and interest-bearing cash accounts and rates paid for supporting funds. The net interest spread increased five basis points in fiscal 2016 as compared with fiscal 2015, primarily as a result of an increase of spreads between yields earned on investments and interest-bearing cash accounts and rates paid for supporting funds.

The cost of total average interest-bearing liabilities increased to 1.20 percent, an increase of 13 basis points, for the year ended September 30, 2017, from 1.07 percent for the year ended September 30, 2016, which followed an increase of three basis points from 1.04 percent for the year ended September 30, 2015.

The following table, "Average Statements of Condition with Interest and Average Rates", on a tax-equivalent basis presents for the years ended September 30, 2017, 2016 and 2015, the Company's average assets, liabilities and shareholders' equity. The Company's net interest income, net interest spreads and net interest income as a percentage of interest-earning assets (net interest margin) are also reflected.

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	Year Ended September 30,			2016			2015		
	2017								
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)								
ASSETS									
Interest earning assets:									
Loans receivable ⁽¹⁾	\$738,496	\$30,850	4.18 %	\$507,973	\$21,216	4.18 %	\$384,125	\$16,492	4.29 %
Investment securities	85,030	2,206	2.59	149,812	3,830	2.56	158,282	3,773	2.38
Deposits in other banks	71,754	631	0.88	46,429	213	0.46	39,975	72	0.18
FHLB stock	5,436	257	4.72	5,243	250	4.77	4,369	311	7.12
Total interest earning assets ⁽¹⁾	900,716	33,944	3.77	709,457	25,509	3.60	586,751	20,648	3.52
Non-interest earning assets									
Cash and due from banks	1,789			15,585			7,003		
Bank owned life insurance	18,683			18,165			18,492		
Other assets	20,151			14,177			13,592		
Allowance for loan losses	(6,930)			(4,968)			(4,610)		
Total non-interest earning assets	33,693			42,959			34,477		
Total assets	\$934,409			\$752,416			\$621,228		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest bearing liabilities:									
Money Market accounts	\$234,204	\$2,069	0.88 %	\$138,997	\$874	0.63 %	\$72,467	\$271	0.37 %
Savings accounts	43,937	37	0.08	45,060	32	0.07	44,975	29	0.06
Certificate accounts	270,054	3,861	1.43	239,810	3,492	1.46	209,994	3,048	1.45
Other interest- bearing deposits	102,936	269	0.26	90,054	139	0.15	86,814	83	0.10
Total deposits	651,131	6,236	0.96	513,921	4,537	0.88	414,250	3,431	0.83
Borrowed funds	136,885	3,210	2.34	115,598	2,195	1.90	91,588	1,817	1.98
Total interest-bearing liabilities	788,016	9,446	1.20	629,519	6,732	1.07	505,838	5,248	1.04
Non-interest bearing liabilities									
Demand deposits	40,759			31,263			28,650		
Other liabilities	6,044			5,262			6,775		

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Total non-interest-bearing liabilities	46,803		36,525		35,425
Shareholders' equity	99,590		86,372		79,965
Total liabilities and shareholders' equity	\$934,409		\$752,416		\$621,228
Net interest income (tax-equivalent basis)		\$24,498		\$18,777	\$15,400
Net interest spread		2.57 %		2.53 %	2.48 %
Net interest margin		2.72 %		2.65 %	2.62 %
Tax-equivalent adjustment ⁽²⁾		(162)		(265)	(186)
Net Interest income		\$24,336		\$18,512	\$15,214

(1) Includes non-accrual loans during the respective periods. Calculated net of deferred loan fees and loan discounts.

(2) The tax-equivalent adjustment was computed based on a statutory Federal income tax rate of 34 percent for fiscal years 2017, 2016 and 2015.

Investment Portfolio

For the year ended September 30, 2017, the average volume of investment securities decreased by \$64.8 million to approximately \$85.0 million or 9.4 percent of average earning assets, from \$149.8 million on average, or 21.1 percent of average earning assets, in fiscal 2016. At September 30, 2017, the total investment portfolio amounted to \$49.5 million, a decrease of \$57.4 million from September 30, 2016. The decrease in the investment portfolio was done in the ordinary course of business policy, with the proceeds used to fund loan growth. It was primarily the result of available-for-sale investment securities sold during fiscal 2017. At September 30, 2017, the principal components of the investment portfolio were government agency obligations, Federal agency obligations including mortgage-backed securities, obligations of U.S. states and political subdivision, corporate bonds and notes, and equity securities.

During the year ended September 30, 2017, volume related factors decreased investment revenue by \$1.7 million, while rate related factors increased investment revenue by \$32,000. The tax-equivalent yield on investments increased by three basis points to 2.59 percent from a yield of 2.56 percent during the year ended September 30, 2016. The decrease in the investment portfolio was attributed to the sales, amortization, and calls recorded during fiscal 2017. The yield on the portfolio increased in fiscal 2017 compared to fiscal 2016 due primarily to higher rates earned on taxable securities.

During fiscal 2015, the Company reclassified at fair value approximately \$57.5 million in available-for-sale investment securities to the held-to-maturity category. The net unrealized loss at date of transfer amounted to \$115,000. This is being amortized over the remaining life of the securities as an adjustment of yield, offsetting the related amortization of the premium or accretion of the discount on the transferred securities. No gains or losses were recognized at the time of reclassification. Management considers the held-to-maturity classification of these investment securities to be appropriate as the Company has the positive intent and ability to hold these securities to maturity.

As of September 30, 2017, the estimated fair value of the available-for-sale securities disclosed below was primarily dependent upon the movement in market interest rates, particularly given the negligible inherent credit risk associated with these securities. These investment securities are comprised of securities that are rated investment grade by at least one bond credit rating service. Although the fair value will fluctuate as the market interest rates move, management believes that these fair values will recover as the underlying portfolios mature and are reinvested in market rate yielding investments. As of September 30, 2017, the Company held two government agency securities, two municipal bonds, three corporate securities, 36 mortgage-backed securities and one single issuer trust preferred security which were in an unrealized loss position. The Company does not intend to sell and expects that it is not more likely than not that it will be required to sell these securities until such time as the value recovers or the securities mature. Management does not believe any individual unrealized loss as of September 30, 2017 represents other-than-temporary impairment.

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

For fiscal 2017, proceeds of investment securities sold amounted to approximately \$51.1 million. Gross realized gains on investment securities sold amounted to approximately \$464,000, while gross realized losses amounted to approximately \$1,000, for the period. For fiscal 2016, proceeds of investment securities sold amounted to approximately \$62.8 million. Gross realized gains on investment securities sold amounted to approximately \$595,000, while gross realized losses amounted to approximately \$30,000, for the period. For fiscal 2015, proceeds of investment securities sold amounted to approximately \$70.4 million. Gross realized gains on investment securities sold amounted to approximately \$610,000, while gross realized losses amounted to approximately \$95,000, for the period.

The varying amount of sales from the available-for-sale portfolio over the past few years, and the significant volume of such sales in fiscal 2017, reflect the significant volatility present in the market. Given the historic low interest rates prevalent in the market, it is necessary for the Company to protect itself from interest rate exposure. Securities that once appeared to be sound investments can, after changes in the market, become securities that the Company has the flexibility to sell to avoid losses and mismatches of interest-earning assets and interest-bearing liabilities at a later time.

The table below illustrates the maturity distribution and weighted average yield on a tax-equivalent basis for investment securities at September 30, 2017 on a contractual maturity basis.

	One year or less	More than One Year through Five Years	More than Five Years through Ten Years	More than Ten Years	Total						
	Amortized Cost	Amortized Cost	Amortized Cost	Amortized Cost	Amortized Cost	Amortized Cost	Amortized Cost	Amortized Cost	Fair Value	Fair Value	Weighted Average Yield
	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield	Weighted Average Yield			
	Yield										
	(Dollars in thousands)										
Available for Sale Securities:											
State and municipal obligations	\$-	- %	\$4,207	1.87 %	\$2,330	1.90 %	\$455	3.40 %	\$6,992	\$7,029	1.98 %
Single issuer trust preferred security	-	-	-	-	-	-	1,000	1.948	1,000	934	1.94
Corporate debt securities	-	-	-	-	6,627	2.89	-	-	6,627	6,374	2.89
Mutual fund	-	-	250	2.00	-	-	-	-	250	250	2.00
Total	\$-	- %	\$4,457	1.88 %	\$8,957	2.63 %	\$1,455	2.39 %	\$14,869	\$14,587	2.38 %
Held to Maturity Securities:											
U.S. government agencies and obligations	\$-	- %	1,999	1.29 %	\$-	- %	\$-	- %	\$1,999	1,991	1.29 %
State and municipal obligations	-	-	-	-	1,895	2.24	7,679	1.49	9,574	9,663	1.64
Corporate debt securities	-	-	-	-	3,818	3.82	-	-	3,818	3,844	3.82
Mortgage-backed securities	-	-	-	-	-	-	19,524	1.79	19,524	19,068	1.78
Total	\$-	- %	\$1,999	1.29 %	\$5,713	3.30 %	\$27,203	1.70 %	34,915	34,566	1.94 %
Total Investment Securities	\$-	- %	\$6,456	1.70 %	\$14,670	2.89 %	\$28,658	1.74 %	\$49,784	\$49,153	2.07 %

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

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

(In thousands)	2017	2016	2015
Investment Securities Available-for-Sale:			
U.S. government agencies	\$—	\$—	\$815
State and municipal obligations	7,029	25,307	42,083
Single issuer trust preferred security	934	878	850
Corporate debt securities	6,374	40,202	69,982
Mutual Fund	250	—	—
Mortgage-backed securities:			
Federal National Mortgage Association	—	—	8,692
Federal Home Loan Mortgage Company	—	—	5,932
Collateralized mortgage obligations	—	—	—
Total available-for-sale	\$ 14,587	\$ 66,387	\$ 128,354
Investment Securities Held-to-Maturity:			
U.S. government agencies	\$ 1,999	\$ 2,999	\$ 14,301
State and municipal obligations	9,574	9,826	10,075
Corporate debt securities	3,818	3,916	4,011
Mortgage-backed securities:			
Collateralized mortgage obligations, fixed- rate	19,524	23,810	28,834
Total held-to-maturity	\$ 34,915	\$ 40,551	\$ 57,221
Total investment securities	\$ 49,502	\$ 106,938	\$ 185,575

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

Loan Portfolio

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

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

At September 30, 2017, total gross loans amounted to \$842.1 million, an increase of \$263.8 million or 45.6 percent as compared to September 30, 2016. For the year ended September 30, 2017, growth of \$264.4 million in commercial loans and \$25.4 million in construction and development loans were partially offset by decreases of \$16.7 million in residential mortgage loans and \$9.3 million in total consumer loans. Even though the Company continues to be challenged by the competition for lending relationships that exists within its market, growth in volume has been achieved through successful lending sales efforts to build on continued customer relationships.

The average balance of our total loans increased \$230.5 million or 45.4 percent for the year ended September 30, 2017 as compared to September 30, 2016, while the average yield on loans remained the same in fiscal 2017 compared with fiscal 2016. The increase in average total loan volume was due primarily to the volume of new loan originations. During fiscal 2017 compared to fiscal 2016, the volume-related factors during the period contributed to an increase of interest income on loans of \$9.6 million, while the rate-related changes increased interest income by \$6,000.

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

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	September 30,				
	2017	2016	2015	2014	2013
	(In thousands)				
Residential mortgage	\$192,500	\$209,186	\$214,958	\$231,324	\$239,900
Construction and Development:					
Residential and commercial	35,622	18,579	5,677	5,964	6,672
Land	18,377	10,013	2,142	1,033	2,439
Total construction and development	53,999	28,592	7,819	6,997	9,111
Commercial:					
Commercial real estate	437,760	231,439	87,686	71,579	70,571
Multi-family	39,768	19,515	7,444	1,032	1,971
Farmland	1,723	-	-	-	-
Other	74,837	38,779	13,380	5,480	5,573
Total commercial	554,088	289,733	108,510	78,091	78,115
Consumer:					
Home equity lines of credit	16,509	19,757	22,919	22,292	20,431
Second mortgages	22,480	29,204	37,633	47,034	54,532
Other	2,570	1,914	2,359	2,839	2,648
Total consumer	41,559	50,875	62,911	72,165	77,611
Total loans	842,146	578,386	394,198	388,577	404,737
Deferred loan fees and costs, net	590	1,208	1,776	2,086	2,210
Allowance for loan losses	(8,405)	(5,434)	(4,667)	(4,589)	(5,090)
Loans receivable, net	\$834,331	\$574,160	\$391,307	\$386,074	\$401,857

At September 30, 2017, our net loan portfolio totaled \$834.3 million or 79.8% of total assets. Our principal lending activity has been the origination of loans collateralized by one-to four-family, also known as “single-family,” residential real estate loans located in our market area. In light of the increased levels of our non-performing and problem assets in recent fiscal years, we have taken certain actions to strengthen and enhance our loan underwriting policies and procedures and our loan administration and oversight policies and procedures. We have revised both our consumer loan policy and our commercial loan policy to address certain minimum loan-to-value (“LTV”) ratios, maximum gross debt ratios and minimum debt coverage ratio policy requirements. We have invested in and implemented software which facilitates our ability to internally review and grade loans in our portfolio and to monitor loan performance. Our Credit Review Department’s primary focus has been to review and maintain the loan portfolio, along with the review of underwriting of all new credits.

At times, the Company purchases single-family residential mortgage loans and consumer loans from a network of mortgage brokers. These loans are underwritten at the Bank and closed in the Bank’s name.

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

The loans receivable portfolio is segmented into residential mortgage loans, construction and development loans, commercial loans and consumer loans. The residential mortgage loan segment has one class, one-to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial construction loans and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built and occupied by the home-owner. Commercial construction loans are made for the purpose of acquiring, developing and constructing a commercial use structure and for acquisition, development and construction of residential properties by residential developers. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

Residential Lending. Residential mortgage originations are secured primarily by properties located in the Company’s primary market area and surrounding areas. At September 30, 2017, \$192.5 million, or 22.9%, of our total loans in portfolio consisted of single-family residential mortgage loans.

Our single-family residential mortgage loans generally are underwritten on terms and documentation conforming to guidelines issued by Freddie Mac and Fannie Mae. Applications for one-to four-family residential mortgage loans are taken by our loan origination officers and are accepted at any of our banking offices and are then referred to the lending department at our main office in order to process the loan, which consists primarily of obtaining all documents required by Freddie Mac and Fannie Mae underwriting standards, and completing the underwriting, which includes making a determination whether the loan meets our underwriting standards such that the Bank can extend a loan commitment to the customer. We generally have retained for portfolio a substantial portion of the single-family residential mortgage loans that we originate. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 10 to 30 years. We also offer adjustable rate mortgage (“ARM”) loans where the interest rate either adjusts on an annual basis or is fixed for the initial one, three or five years and then adjusts annually. However, due to the low interest rate environment and demand for fixed rate products, we have not originated a significant amount of ARM loans in recent years. At September 30, 2017, \$44.4 million, or 23.1%, of our one-to four-family residential mortgage loans consisted of ARM loans.

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

Construction and Development Loans. The amount of our outstanding construction and development loans in portfolio increased to \$54.0 million or 6.4% of gross loans at September 30, 2017 from \$28.6 million or 4.9% of total loans as of September 30, 2016. From October 2009 through September 30, 2013, we ceased originating any new construction and development loans, with certain limited exceptions. During fiscal 2014, we resumed originating construction loans to builders and developers in our market area, on a relatively modest basis consistent with our business plan filed with the OCC. We generally limit construction loans to builders and developers with whom we have an established relationship, or who are otherwise known to officers of the Bank. Our construction loans also include single-family residential construction loans which may if approved convert to permanent, long-term mortgage loans upon completion of construction (“construction/perm” loans). During the initial or construction phase, these construction/perm loans require payment of interest only, which generally is tied to prime rate, as the home is being constructed. On residential construction to perm loans the interest rate is as approved. Upon the earlier of the completion of construction or one year, these loans if approved by the appropriate approving authority convert to long-term (generally 30 years), amortizing, fixed-rate single-family mortgage loans.

Our current portfolio of construction loans generally have a maximum term as approved based upon the underwriting (for individual, owner-occupied dwellings), and loan-to-value ratios less than 80%. Residential construction loans to developers are made on either a pre-sold or speculative (unsold) basis. Limits are placed on the number of units that can be built on a speculative basis based upon the reputation and financial position of the builder, his/her present obligations, the location of the property and prior sales in the development and the surrounding area. Generally, a limit of two unsold homes (one model home and one speculative home) is placed per project.

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

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

Our loan portfolio included nine loans secured by unimproved real estate and lots (“land loan”), with an outstanding balance of \$18.4 million, constituting 2.2% of total loans, at September 30, 2017.

In order to mitigate some of the risks inherent to construction lending, we inspect properties under construction, review construction progress prior to advancing funds, work with builders with whom we have established relationships, require annual updating of tax returns and other financial data of developers and obtain personal guarantees from the principals. At September 30, 2017, \$657,000, or 7.8 percent, of our allowance for loan losses was attributed to construction and development loans. We had no loans in non-performing construction and development loans in portfolio at September 30, 2017 and at September 30, 2016. At September 30, 2017 and 2016, we had \$94,000 and \$109,000, respectively, in construction and development loans that were performing troubled debt restructurings.

Commercial Lending. At September 30, 2017, our loans in portfolio secured by commercial real estate amounted to \$437.8 million and constituted 52.0 percent of our gross loans at such date. During the year ended September 30, 2017, the commercial real estate loan portfolio increased by \$206.3 million, or 89.2 percent. During fiscal 2017, we had zero charge-offs of commercial real estate loans, as compared to \$99,000 in charge-offs at fiscal 2016.

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

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

Commercial and multi-family real estate loans generally present a higher level of risk than loans secured by one-to four-family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced (for example, if leases are not obtained or renewed, a bankruptcy court modifies a lease term, or a major tenant is unable to fulfill its lease obligations), the borrower's ability to repay the loan may be impaired. As of September 30, 2017, we had no non-accruing commercial real estate mortgage loans and an aggregate of \$2.0 million of our commercial real estate loans at such date were classified for regulatory reporting purposes as substandard. As of September 30, 2017, \$2.8 million, or 32.9% of our allowance for loan losses was allocated to commercial real estate mortgage loans. In addition, at September 30, 2017 and 2016, we had no real estate owned which were acquired from foreclosures on, or our acceptance of a deed-in-lieu of foreclosure, on commercial real estate loans. As of September 30, 2017, our commercial real estate loans held in portfolio were deemed performing troubled debt restructurings were \$554,000 compared to \$1.8 million at September 30, 2016.

At September 30, 2017, our loan portfolio included 15 loans with an aggregate book value of \$39.8 million secured by multi-family (more than four units) properties, constituting 4.7% of our gross loans at such date. As of September 30, 2017, we had no non-accruing multi-family loans.

At September 30, 2017, we had \$74.8 million in commercial business loans (8.9% of gross loans outstanding) in portfolio. Our commercial business loans generally have been made to small to mid-sized businesses located in our market area. The commercial business loans in our portfolio assist us in our asset/liability management since they generally provide shorter maturities and/or adjustable rates of interest in addition to generally having higher rates of return which are designed to compensate for the additional credit risk associated with these loans. The commercial business loans which we have originated may be either a revolving line of credit or for a fixed term of generally 10 years or less. Interest rates are adjustable, indexed to a published prime rate of interest, or fixed. Generally, equipment, machinery, real property or other corporate assets secure such loans. Personal guarantees from the business principals are generally obtained as additional collateral.

Generally, commercial business loans are characterized as having higher risks associated with them than single-family residential mortgage loans. As of September 30, 2017, we had no non-accruing commercial business loans in our loan portfolio. At such date, \$416,000 or 5.0% of the allowance for loan losses was allocated to commercial business loans.

At September 30, 2017 and 2016, we held no commercial business loans in portfolio that were deemed performing troubled debt restructurings.

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

Consumer Lending. In our efforts to provide a full range of financial services to our customers, we offer various types of consumer loans. Our consumer loans amounted to \$41.6 million or 4.9% of our total loan portfolio at September 30, 2017. The largest components of our consumer loans are loans secured by second mortgages, consisting primarily of home equity loans, which amounted to \$22.5 million at September 30, 2017, and home equity lines of credit, which amounted to \$16.5 million at such date. Our consumer loans also include automobile loans, unsecured personal loans and loans secured by deposits. Consumer loans are originated primarily through existing and walk-in customers and direct advertising.

Our home equity lines of credit are variable rate loans tied to the prime rate. Our second mortgages may have fixed or variable rates, although they generally have had fixed rates in recent periods. Our second mortgages have a maximum term to maturity of 15 years. Both our second mortgages and our home equity lines of credit generally are secured by the borrower's primary residence. However, our security generally consists of a second lien on the property. Our lending policy provides that the maximum loan-to-value ratio on our home equity lines of credit is 80%, when Malvern Federal Savings has the first mortgage. However, the maximum loan-to-value ratio on our home equity lines of credit is reduced to 75%, when the Bank does not have the first mortgage. At September 30, 2017, the unused portion of our home equity lines of credit was \$26.4 million.

Consumer loans generally have higher interest rates and shorter terms than residential loans; however, they have additional credit risk due to the type of collateral securing the loan or in some cases the absence of collateral. In the year ended September 30, 2017, we charged-off \$223,000 of consumer loans mostly consisting of second mortgage loans. We are continuing to evaluate and monitor the credit conditions of our consumer loan borrowers and the real estate values of the properties securing our second mortgage loans as part of our on-going efforts to assess the overall credit quality of the portfolio in connection with our review of the allowance for loan losses. As of September 30, 2017, we had an aggregate of \$212,000 of non-accruing second mortgage loans and home equity lines of credit, representing an improvement of \$140,000 over the amount of non-accruing second mortgage loans and home equity lines of credit at September 30, 2016. At September 30, 2017, \$868,000 of our consumer loans were classified as substandard consumer loans. At September 30, 2017, an aggregate of \$516,000 of our allowance for loan losses was allocated to second mortgages and home equity lines of credit.

The following table presents the contractual maturity of our loans held in portfolio at September 30, 2017. The table does not include the effect of prepayments or scheduled principal amortization. Loans having no stated repayment schedule or maturity and overdraft loans are reported as being due in one year or less.

	At September 30, 2017, Maturing			Total
	In One Year or Less	After One Years Through Five Years	After Five Years	
	(In thousands)			
Residential mortgage	\$328	\$ 6,417	\$ 185,755	\$ 192,500
Construction and Development:				
Residential and commercial	22,430	10,307	2,885	35,622
Land	13,461	2,698	2,218	18,377
Total construction and development	35,891	13,005	5,103	53,999
Commercial:				
Commercial real estate	14,020	94,265	329,475	437,760
Farmland	—	—	1,723	1,723
Multi-family	6,000	15,215	18,553	39,768
Other	17,563	41,735	15,539	74,837

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Total commercial	37,583	151,215	365,290	554,088
Consumer:				
Home equity lines of credit	—	—	16,509	16,509
Second mortgages	45	3,463	18,972	22,480
Other	173	2,039	358	2,570
Total consumer	218	5,502	35,839	41,559
Total	\$74,020	\$ 176,139	\$591,987	\$842,146
Loans with:				
Fixed rates	\$7,265	\$ 24,649	\$268,182	\$300,096
Variable rates	66,755	151,490	323,805	542,050
Total	\$74,020	\$ 176,139	\$591,987	\$842,146

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

Allowance for Loan Losses and Related Provision

The purpose of the allowance for loan losses (“allowance”) is to absorb the impact of probable losses inherent in the loan portfolio. Additions to the allowance are made through provisions charged against current operations and through recoveries made on loans previously charged-off. The allowance for loan losses is maintained at an amount considered adequate by management to provide for potential credit losses based upon a periodic evaluation of the risk characteristics of the loan portfolio. In establishing an appropriate allowance, an assessment of the individual borrowers, a determination of the value of the underlying collateral, a review of historical loss experience and an analysis of the levels and trends of loan categories, delinquencies and problem loans are considered. Such factors as the level and trend of interest rates, current economic conditions and peer group statistics are also reviewed. At fiscal 2017 year-end, the level of the allowance was \$8.4 million as compared to a level of \$5.4 million at September 30, 2016. The Company made loan loss provisions of \$2.8 million in fiscal 2017 compared with \$947,000 in fiscal 2016 and \$90,000 in fiscal 2015. The level of the allowance during the respective annual fiscal periods of 2017, 2016 and 2015 reflects the change in average volume, credit quality within the loan portfolio, the level of charge-offs, loan volume recorded during the periods and the Company’s focus on the changing composition of the commercial and residential real estate loan portfolios.

At September 30, 2017, the allowance for loan losses amounted to 1.00 percent of total loans. In management’s view, the level of the allowance at September 30, 2017 is adequate to cover losses inherent in the loan portfolio. Management’s judgment regarding the adequacy of the allowance constitutes a “Forward Looking Statement” under the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from management’s analysis, based principally upon the factors considered by management in establishing the allowance.

Although management uses the best information available, the level of the allowance for loan losses remains an estimate, which is subject to significant judgment and short-term change. Various regulatory agencies, as an integral part of their examination process, periodically review the Company’s allowance for loan losses. Such agencies may require the Company to increase the allowance based on their analysis of information available to them at the time of their examination. Furthermore, the majority of the Company’s loans are secured by real estate in the State of Pennsylvania. Future adjustments to the allowance may be necessary due to economic factors impacting Pennsylvania real estate and further deterioration of the economic climate, as well as, operating, regulatory and other conditions beyond the Company’s control. The allowance for loan losses as a percentage of total loans amounted to 1.00 percent, 0.94 percent and 1.18 percent at September 30, 2017, 2016 and 2015, respectively.

Net recoveries were \$180,000 in fiscal 2017, compared to net charge-offs of \$180,000 in fiscal 2016 and net charge-offs of \$12,000 in fiscal 2015. During fiscal 2017, the Company experienced a decrease in charge-offs and an increase in recoveries compared to fiscal 2016. Charge-offs were lower in most of the portfolio segments in fiscal 2017 than in fiscal 2016 and recoveries were primarily higher in consumer loan portfolio segment in fiscal 2017 than in fiscal 2016. Consumer loan recoveries were \$148,000 higher in fiscal 2017 compared to fiscal 2016.

Five-Year Statistical Allowance for Loan Losses

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

	September 30,				
	2017	2016	2015	2014	2013
	(Dollars in thousands)				
Average loans outstanding	\$738,496	\$507,973	\$384,125	\$407,169	\$447,196
Total loans at end of period	\$842,146	\$578,386	\$394,198	\$388,577	\$404,737
Analysis of the Allowance of Loan Losses					
Balance at beginning of year	\$5,434	\$4,667	\$4,589	\$5,090	\$7,581
Charge-offs:					
Residential mortgage	—	9	—	83	994
Construction and Development:					
Residential and commercial	—	91	1	37	5,768
Land	—	—	—	—	99
Commercial:					
Commercial real estate	—	99	48	183	6,315
Multi-family	—	—	—	—	—
Other	—	—	—	—	94
Consumer:					
Home equity lines of credit	—	—	—	14	—
Second mortgages	218	291	138	618	1,042
Other	5	70	34	6	9
Total charge-offs	223	560	221	941	14,321
Recoveries:					
Residential mortgage	2	17	17	23	199
Construction and Development:					
Residential and commercial	90	243	98	1	—
Commercial:					
Commercial real estate	40	3	9	9	117
Other	9	3	3	3	23
Consumer:					
Home equity lines of credit	18	1	2	1	17
Second mortgages	232	100	69	136	235
Other	12	13	11	4	4
Total recoveries	403	380	209	177	595
Net (recoveries) charge-offs	(180)	180	12	764	13,726
Provision for loan losses	2,791	947	90	263	11,235
Balance at end of year	\$8,405	\$5,434	\$4,667	\$4,589	\$5,090
	(0.02)%	0.04 %	0.00 %	0.19 %	3.07 %

Ratio of net (recovery) charge-offs
 during the year to average loans
 outstanding during the
 year

Allowance for loan losses as a percentage of total loans at end of year	1.00	%	0.94	%	1.18	%	1.18	%	1.26	%
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For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

Implicit in the lending function is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan being made, the creditworthiness of the borrower and prevailing economic conditions. The allowance for loan losses has been allocated in the table below according to the estimated amount deemed to be reasonably necessary to provide for the possibility of losses being incurred within the following categories of loans at September 30, for each of the past five years.

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

	September 30, 2017		2016		2015		2014		2013		
	Loans to Total Amount Loans		Loans to Total Amount Loans		Loans to Total Amount Loans		Loans to Total Amount Loans		Loans to Total Amount Loans		
	(Dollars in thousands)										
Residential mortgage	\$1,004	22.8 %	\$1,201	36.2 %	\$1,486	54.5 %	\$1,672	59.5 %	\$1,414	59.3 %	
Construction and Development:											
Residential and commercial	523	4.2	199	3.2	30	1.5	291	1.5	164	1.6	
Land loans	132	2.2	97	1.7	35	0.5	13	0.3	56	0.6	
Commercial:											
Commercial real estate	3,581	52.0	1,874	40.0	1,235	22.2	1,248	18.4	1,726	17.4	
Farmland	9	0.2									
Multi-family	224	4.7	109	3.4	104	1.9	29	0.3	40	0.5	
Other	541	8.9	158	6.7	108	3.4	50	1.4	59	1.4	
Consumer:											
Home equity lines of credit	90	2.0	116	3.4	139	5.8	168	5.8	137	5.0	
Second mortgages	402	2.7	467	5.0	761	9.6	1,033	12.1	1,393	13.5	
Other	27	0.3	34	0.4	24	0.6	23	0.7	22	0.7	
Total allocated	6,533	100.0	4,255	100.0	3,922	100.0	4,527	100.0	5,011	100.0	
Unallocated	1,872	-	1,179	-	745	-	62	-	79	-	
Balance at end of period	\$8,405	100.0 %	\$5,434	100.0 %	\$4,667	100.0 %	\$4,589	100.0 %	\$5,090	100.0 %	

In assessing the adequacy of the ALLL, it is recognized that the process, methodology and underlying assumptions require a significant degree of judgment. The estimation of credit losses is not precise; the range of factors considered is wide and is significantly dependent upon management's judgment, including the outlook and potential changes in

the economic environment. At present, components of the commercial loan segments of the portfolio are new originations and the associated volumes continue to see increased growth. At the same time, historical loss levels have decreased as factors in assessing the portfolio. The combination of these factors has given rise to an increase in the unallocated level within the allowance. Any unallocated portion of the allowance reflects management's estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about the borrower's financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors.

Asset Quality

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

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

Non-Performing and Past Due Loans and OREO

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

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

	At September 30,				
	2017	2016	2015	2014	2013
	(In thousands)				
Non-accrual loans	\$1,038	\$1,617	\$1,399	\$2,391	\$1,901
Accruing loans past due 90 days or more	173	696	—	—	—
Total non-performing loans	1,211	2,313	1,399	2,391	1,901
Other real estate owned	—	—	1,168	1,964	3,962
Total non-performing assets	\$1,211	\$2,313	\$2,567	\$4,355	\$5,863
Troubled debt restructured loans — performing	\$2,238	\$2,039	\$1,091	\$1,009	\$1,346

At September 30, 2017, non-performing assets totaled \$1.2 million, or 0.12% of total assets, as compared with \$2.3 million, or 0.28%, at September 30, 2016. The reduction in non-performing assets from September 30, 2017 was attributable to four loans with an outstanding balance of approximately \$435,000 at September 30, 2016 which were returned to accruing status during fiscal 2017, as well as, an aggregate balance of \$413,000 of paid-offs loans, principal payments of \$180,000, offset in part by the addition of three single residential loans (totaling approximately \$318,000) and two consumer loans (totaling approximately \$151,000) into non-accrual status.

Troubled debt restructured loans, totaled \$2.3 million and \$2.2 million at September 30, 2017 and at September 30, 2016. A total of \$2.2 and \$2.0 million of troubled debt restructured loans were performing pursuant to the terms of their respective modifications at September 30, 2017 and September 30, 2016, respectively. At September 30, 2017, one troubled debt restructured loan with an outstanding balance of approximately \$22,000, was deemed non-performing, while one loan with an outstanding balance of \$139,000 was deemed non-performing at September 30, 2016. The performing troubled debt restructured loans increased by \$199,000 at September 30, 2017 compared to September 30, 2016 primarily due to four residential mortgage loans with an aggregate outstanding balance of \$1.2 million and two second mortgage loans with an outstanding balance of approximately \$126,000 being classified as a performing TDRs during fiscal 2017, as well as one residential mortgage loan with an outstanding balance of \$153,000 at September 30, 2017 returned to accruing status. These increases were offset by two commercial loans with an aggregate outstanding balance of approximately \$1.3 million at September 30, 2016, being paid off during fiscal 2017.

Total non-performing assets decreased \$254,000 from September 30, 2015 to September 30, 2016. The reduction in non-performing assets from September 30, 2015 was attributable to two commercial loans to one borrower with an outstanding balance of approximately \$492,000 at September 30, 2015 which were returned to accruing status during fiscal 2016, as well as, \$117,000 in charge-offs, payments of \$212,000, offset in part by the addition of seven single residential loans (totaling approximately \$658,000), one commercial real estate loan (totaling approximately \$193,000) and six consumer loans (totaling approximately \$186,000) into non-accrual status. In addition, the

Company reduced other real estate owned at September 30, 2016 to zero as compared to \$1.2 million at September 30, 2015. The decrease was attributable to three single residential loans and one commercial real estate loan sold during the fiscal 2016. The decrease in REO at September 30, 2016 compared to September 30, 2015, was due to \$1.2 million of sales of REO, at a net gain of \$19,000, as well as \$20,000 in reduction to fair value which are reflected in other REO expense during fiscal 2016.

Other Income

The following table presents the principal categories of non-interest income for each of the years in the three-year period ended September 30, 2017.

	Year Ended September 30,			% Change	Year Ended September 30,		
	2017	2016	Increase (Decrease)		2016	2015	Increase (Decrease)
	(Dollars in thousands)						
Service charges and other fees	\$992	\$ 923	\$ 69	7.36	% \$923	\$989	\$ (66) (6.67)%
Rental income-other	227	&nbs					