

Magyar Bancorp, Inc.  
Form 10-Q  
May 14, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Under Section 13 or 15(d)

of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2012

Commission File Number **000-51726**

**Magyar Bancorp, Inc.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of Incorporation or Organization)

**20-4154978**

(I.R.S. Employer Identification Number)

**400 Somerset Street, New Brunswick, New Jersey**

(Address of Principal Executive Office)

**08901**

(Zip Code)

**(732) 342-7600**

(Issuer's Telephone Number including area code)

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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 past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

(Do not check if a  
smaller reporting  
company)

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

Yes  No

State the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at May 1, 2012
Common Stock, \$0.01 Par Value	5,806,624

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MAGYAR BANCORP, INC.

Form 10-Q Quarterly Report

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

**MAGYAR BANCORP, INC. AND SUBSIDIARY**

## Consolidated Balance Sheets

(In Thousands, Except Share and Per Share Data)

	March 31, 2012	September 30, 2011
	(Unaudited)	
Assets		
Cash	\$897	\$1,066
Interest earning deposits with banks	10,745	13,968
Total cash and cash equivalents	11,642	15,034
Investment securities - available for sale, at fair value	26,963	25,312
Investment securities - held to maturity, at amortized cost (fair value of \$46,262 and \$45,713 at March 31, 2012 and September 30, 2011, respectively)	45,499	45,000
Federal Home Loan Bank of New York stock, at cost	2,199	2,299
Loans receivable, net of allowance for loan losses of \$4,008 and \$3,848 at March 31, 2012 and September 30, 2011, respectively	380,859	381,254
Bank owned life insurance	9,836	9,660
Accrued interest receivable	1,867	1,921
Premises and equipment, net	20,187	20,574
Other real estate owned ("OREO")	14,701	16,595
Other assets	6,552	6,388
Total assets	\$520,305	\$524,037
Liabilities and Stockholders' Equity		
Liabilities		
Deposits	\$422,523	\$424,943
Escrowed funds	1,063	1,043
Federal Home Loan Bank of New York advances	32,688	34,916
Securities sold under agreements to repurchase	15,000	15,000
Accrued interest payable	280	300
Accounts payable and other liabilities	4,091	3,326

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Total liabilities	475,645	479,528
Stockholders' equity		
Preferred stock: \$.01 Par Value, 1,000,000 shares authorized; none issued	—	—
Common stock: \$.01 Par Value, 8,000,000 shares authorized; 5,923,742 issued; 5,806,624 and 5,801,631 shares outstanding at March 31, 2012 and September 30, 2011, respectively, at cost	59	59
Additional paid-in capital	26,406	26,496
Treasury stock: 117,118 and 122,111 shares at March 31, 2012 and September 30, 2011, respectively, at cost	(1,333 )	(1,480 )
Unearned Employee Stock Ownership Plan shares	(1,172 )	(1,228 )
Retained earnings	21,159	21,069
Accumulated other comprehensive loss	(459 )	(407 )
Total stockholders' equity	44,660	44,509
Total liabilities and stockholders' equity	\$520,305	\$ 524,037

The accompanying notes are an integral part of these statements.

Table of Contents**MAGYAR BANCORP, INC. AND SUBSIDIARY**

## Consolidated Statements of Operations

(In Thousands, Except Per Share Data)

	For the Three Months Ended March 31,		For the Six Months Ended March 31,	
	2012	2011	2012	2011
	(Unaudited)			
Interest and dividend income				
Loans, including fees	\$4,692	\$5,005	\$9,398	\$10,152
Investment securities				
Taxable	521	533	1,061	1,035
Tax-exempt	1	1	2	3
Federal Home Loan Bank of New York stock	29	40	53	87
Total interest and dividend income	5,243	5,579	10,514	11,277
Interest expense				
Deposits	1,016	1,278	2,118	2,694
Borrowings	497	597	1,001	1,207
Total interest expense	1,513	1,875	3,119	3,901
Net interest and dividend income	3,730	3,704	7,395	7,376
Provision for loan losses	323	478	693	836
Net interest and dividend income after provision for loan losses	3,407	3,226	6,702	6,540
Other income				
Service charges	235	235	502	576
Other operating income	105	104	216	216
Gains on sales of loans	143	10	260	459
Gains on sales of investment securities	64	35	148	35
Losses on OREO	(87 )	(157 )	(119 )	(292 )
Total other income	460	227	1,007	994
Other expenses				
Compensation and employee benefits	1,871	1,987	3,726	3,857
Occupancy expenses	726	709	1,455	1,376
Advertising	38	49	82	102
Professional fees	332	303	565	550

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Service fees	135	145	257	289
OREO expenses	173	113	399	236
FDIC deposit insurance premiums	181	357	357	706
Other expenses	443	391	863	856
Total other expenses	3,899	4,054	7,704	7,972
Income before income tax expense	(32 )	(601 )	5	(438 )
Income tax benefit	(42 )	(244 )	(35 )	(208 )
Net income	\$10	\$(357 )	\$40	\$(230 )
Net income (loss) per share-basic and diluted	\$0.00	\$(0.06 )	\$0.01	\$(0.04 )

The accompanying notes are an integral part of these statements.

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## Consolidated Statements of Comprehensive Loss

(In Thousands)

	For the Three Months Ended March 31, 2012 2011 (Unaudited)		For the Six Months Ended March 31, 2012 2011	
Net income (loss)	\$ 10	\$(357)	\$ 40	\$(230)
Other comprehensive income (loss):				
Net unrealized gain (loss) on securities available for sale	42	100	116	(321)
Realized gains on sales of securities available for sale	(64)	(35 )	(148)	(35 )
Unrealized loss on derivatives	(22)	(28 )	(45 )	(101)
	(44)	37	(77 )	(457)
Deferred income tax effect	15	(21 )	25	161
Total other comprehensive (loss) income	(29)	16	(52 )	(296)
Total comprehensive loss	\$(19)	\$(341)	\$(12 )	\$(526)

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## Consolidated Statement of Changes in Stockholders' Equity

For the Six Months Ended March 31, 2012

(In Thousands, Except for Share Amounts)

(Unaudited)

	Common Stock Shares Outstanding	Par Value	Additional Paid-In Capital	Treasury Stock	Unearned ESOP Shares	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance, September 30, 2011	5,801,631	\$ 59	\$ 26,496	\$(1,480 )	\$(1,228 )	\$ 21,069	\$ (407 )	\$ 44,509
Comprehensive Loss:								
Net income	—	—	—	—	—	40	—	40
Other comprehensive loss							(52 )	(52 )
Purchase of treasury stock	(10,700 )	—	—	(32 )	—	—	—	(32 )
Treasury stock used for restricted stock plan	15,693	—	(229 )	179	—	50	—	—
ESOP shares allocated	—	—	(33 )	—	56	—	—	23
Stock-based compensation expense	—	—	172	—	—	—	—	172
Balance, March 31, 2012	5,806,624	\$ 59	\$ 26,406	\$(1,333 )	\$(1,172 )	\$ 21,159	\$ (459 )	\$ 44,660

The accompanying notes are an integral part of this statement.

Table of Contents**MAGYAR BANCORP, INC. AND SUBSIDIARY**

## Consolidated Statements of Cash Flows

(In Thousands)

	For the Six Months Ended March 31, 2012      2011 (Unaudited)	
Operating activities		
Net income (loss)	\$40	\$(230 )
Adjustment to reconcile net income (loss) to net cash provided by operating activities		
Depreciation expense	490	485
Premium amortization on investment securities, net	129	155
Provision for loan losses	693	836
Provision for loss on other real estate owned	77	449
Proceeds from the sales of loans	4,930	7,613
Gains on sale of loans	(260 )	(459 )
Gains on sales of investment securities	(148 )	(35 )
Losses (gains) on the sales of other real estate owned	42	(157 )
ESOP compensation expense	23	27
Stock-based compensation expense	172	201
Decrease (increase) in accrued interest receivable	54	(25 )
Increase in surrender value bank owned life insurance	(176 )	(178 )
(Increase) decrease in other assets	(184 )	320
Decrease in accrued interest payable	(20 )	(48 )
Increase (decrease) in accounts payable and other liabilities	765	(222 )
Net cash provided by operating activities	6,627	8,732
Investing activities		
Net increase in loans receivable	(6,341 )	(2,124 )
Purchases of investment securities held to maturity	(8,057 )	(7,747 )
Purchases of investment securities available for sale	(10,156)	(18,091)
Sales of investment securities available for sale	5,584	2,016
Principal repayments on investment securities held to maturity	7,499	9,752
Principal repayments on investment securities available for sale	2,967	1,854
Purchases of premises and equipment	(103 )	(307 )
Investment in other real estate owned	(269 )	(968 )
Proceeds from the sale of other real estate owned	3,417	541
Redemption of Federal Home Loan Bank stock	100	85
Net cash used by investing activities	(5,359 )	(14,989)
Financing activities		

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Net (decrease) increase in deposits	(2,420 )	2,598
Net increase (decrease) in escrowed funds	20	(298 )
Repayments of long-term advances	(2,228 )	(1,878 )
Purchase of treasury stock	(32 )	—
Net cash (used) provided by financing activities	(4,660 )	422
Net decrease in cash and cash equivalents	(3,392 )	(5,835 )
Cash and cash equivalents, beginning of period	15,034	21,086
Cash and cash equivalents, end of period	\$11,642	\$15,251
Supplemental disclosures of cash flow information		
Cash paid for		
Interest	\$3,139	\$3,949
Income taxes	\$6	\$6
Non-cash investing activities		
Real estate acquired in full satisfaction of loans in foreclosure	\$1,373	\$3,581

The accompanying notes are an integral part of these statements.

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**MAGYAR BANCORP, INC. AND SUBSIDIARY**

Notes to Consolidated Financial Statements

(Unaudited)

**NOTE A – BASIS OF PRESENTATION**

The consolidated financial statements include the accounts of Magyar Bancorp, Inc. (the “Company”), its wholly owned subsidiary, Magyar Bank (the “Bank”), and the Bank’s wholly owned subsidiaries Magyar Service Corporation, Hungaria Urban Renewal, LLC, and MagBank Investment Company. All material intercompany transactions and balances have been eliminated. The Company prepares its financial statements on the accrual basis and in conformity with accounting principles generally accepted in the United States of America (“US GAAP”). The unaudited information furnished herein reflects all adjustments (consisting of normal recurring accruals) that are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented.

Operating results for the three and six months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the year ending September 30, 2012. The September 30, 2011 information has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by US GAAP for complete financial statements.

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of other real estate owned, and the assessment of realizability of deferred income tax assets.

The Company has evaluated events and transactions occurring subsequent to the balance sheet date of March 31, 2012 for items that should potentially be recognized or disclosed in these financial statements. The evaluation was conducted through the date these financial statements were issued.

**NOTE B- RECENT ACCOUNTING PRONOUNCEMENTS**

In connection with the preparation of quarterly and annual reports in accordance with the Securities and Exchange Commission's (SEC) Securities Exchange Act of 1934, SEC Staff Accounting Bulletin Topic 11.M requires the disclosure of the impact that recently issued accounting standards will have on financial statements when they are adopted in the future.

The FASB has issued ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Specifically, ASU 2010-06 amends Codification Subtopic 820-10 to now require: (1) a reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers; and (2) in the reconciliation for fair value measurements using significant unobservable inputs, a reporting entity should present separately information about purchases, sales, issuances, and settlements. In addition, ASU 2010-06 clarifies the requirements of the following existing disclosures: (1) for purposes of reporting fair value measurement for each class of assets and liabilities, a reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities; and (2) a reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Early adoption is permitted. The ASU did not have a material impact on the Company's financial statements.

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The FASB issued ASU 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*, to amend FASB ASC Topic 820, Fair Value Measurements, to bring U.S. GAAP for fair value measurements in line with International Accounting Standards. The ASU clarifies existing guidance for items such as: the application of the highest and best use concept to non-financial assets and liabilities; the application of fair value measurement to financial instruments classified in a reporting entity's stockholder's equity; and disclosure requirements regarding quantitative information about unobservable inputs used in the fair value measurements of level 3 assets. The ASU also creates an exception to Topic 820 for entities which carry financial instruments within a portfolio or group, under which the entity is now permitted to base the price used for fair valuation upon a price that would be received to sell the net asset position or transfer a net liability position in an orderly transaction. The ASU also allows for the application of premiums and discounts in a fair value measurement if the financial instrument is categorized in level 2 or 3 of the fair value hierarchy. Lastly, the ASU contains new disclosure requirements regarding fair value amounts categorized as level 3 in the fair value hierarchy such as: disclosure of the valuation process used; effects of and relationships between unobservable inputs; usage of nonfinancial assets for purposes other than their highest and best use when that is the basis of the disclosed fair value; and categorization by level of items disclosed at fair value, but not measured at fair value for financial statement purposes. This ASU was effective for interim and annual periods beginning after December 15, 2011 and did not have a material impact on the Company's financial statements.

The FASB issued ASU 2011-05, *Presentation of Comprehensive Income* to amend FASB ASC Topic 220, *Comprehensive Income*, to facilitate the continued alignment of U.S. GAAP with International Accounting Standards. The ASU prohibits the presentation of the components of comprehensive income in the statement of stockholder's equity. Reporting entities are allowed to present either: a statement of comprehensive income, which reports both net income and other comprehensive income; or separate, but consecutive, statements of net income and other comprehensive income. Under previous GAAP, all 3 presentations were acceptable. Regardless of the presentation selected, the Reporting Entity is required to present all reclassifications between other comprehensive and net income on the face of the new statement or statements. The provisions of this ASU are effective for fiscal years and interim periods beginning after December 31, 2011. The Company is evaluating the updates to Topic 820 and does not expect their implementation to have a material impact on its consolidated financial statements.

The FASB issued ASU 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. The amendments to the Codification in ASU No. 2011-12 are effective at the same time as the amendments in ASU No. 2011-05, so that entities will not be required to comply with the presentation requirements in ASU No. 2011-05 that ASU No. 2011-12 is deferring. The amendments are being made to allow the FASB time to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. All other requirements in ASU No. 2011-05 are not affected by ASU No. 2011-12, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company is evaluating the updates to Topic 220 and does not expect their implementation to have a material impact on its consolidated financial statements.

NOTE C - CONTINGENCIES

The Company, from time to time, is a party to routine litigation that arises in the normal course of business. In the opinion of management, the resolution of this litigation, if any, would not have a material adverse effect on the Company's consolidated financial position or results of operations.

NOTE D - EARNINGS (LOSS) PER SHARE

Basic and diluted earnings (loss) per share for the three and six months ended March 31, 2012 and 2011 were calculated by dividing net income (loss) by the weighted-average number of shares outstanding for the period. All stock options and restricted stock awards were anti-dilutive for the three and six months ended March 31, 2012 and the three and six months ended March 31, 2011. The following table shows the Company's earnings (loss) per share for the periods presented:

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	For the Three Months Ended March 31, 2012		For the Six Months Ended March 31, 2011	
	2012	2011	2012	2011
	(In thousands except for per share data)			
Income (loss) applicable to common shares	\$10	\$(357 )	\$40	\$(230 )
Weighted average number of common shares outstanding - basic	5,810	5,800	5,802	5,798
Stock options and restricted stock	—	—	—	—
Weighted average number of common shares and common share equivalents - diluted	5,810	5,800	5,802	5,798
Basic earnings (loss) per share	\$0.00	\$(0.06 )	\$0.01	\$(0.04 )
Diluted earnings (loss) per share	\$0.00	(0.06 )	\$0.01	(0.04 )

Options to purchase 188,276 shares of common stock at a weighted average price of \$14.61 and 13,402 shares of restricted shares at a weighted average price of \$4.43 were outstanding and not included in the computation of diluted earnings per share for the three and six months ended March 31, 2012 because the grant (or option strike) price was greater than the average market price of the common shares during the periods. Options to purchase 188,276 shares of common stock at an average price of \$14.61 and 25,588 restricted shares at a weighted average price of \$10.15 were outstanding and not included in the computation of diluted earnings per share for the three and six months ended March 31, 2011 because the grant (or option strike) price was greater than the average market price of the common shares during the periods.

## NOTE E – STOCK-BASED COMPENSATION AND STOCK REPURCHASE PROGRAM

The Company follows FASB Accounting Standards Codification (“ASC”) Section 718, Compensation-Stock Compensation, which covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. ASC 718 requires that compensation cost relating to share-based payment transactions be recognized in financial statements. The cost is measured based on the fair value of the equity or liability instruments issued.

ASC 718 also requires the Company to realize as a financing cash flow rather than an operating cash flow, as previously required, the benefits of realized tax deductions in excess of previously recognized tax benefits on compensation expense. In accordance with SEC Staff Accounting Bulletin (“SAB”) No. 107, the Company classified share-based compensation for employees and outside directors within “compensation and employee benefits” in the consolidated statement of operations to correspond with the same line item as the cash compensation paid.



Stock options generally vest over a five-year service period and expire ten years from issuance. Management recognizes compensation expense for all option grants over the awards' respective requisite service periods. The fair values of all option grants were estimated using the Black-Scholes option-pricing model. Since there was limited historical information on the volatility of the Company's stock, management also considered the average volatilities of similar entities for an appropriate period in determining the assumed volatility rate used in the estimation of fair value. Management estimated the expected life of the options using the simplified method allowed under SAB No. 107. The 7-year Treasury yield in effect at the time of the grant provided the risk-free rate for periods within the contractual life of the option. Management recognizes compensation expense for the fair values of these awards, which have graded vesting, on a straight-line basis over the requisite service period of the awards. Once vested, these awards are irrevocable. Shares will be obtained from either the open market or treasury stock upon share option exercise.

Restricted shares generally vest over a five-year service period on the anniversary of the grant date. Once vested, these awards are irrevocable. The product of the number of shares granted and the grant date market price of the Company's common stock determine the fair value of restricted shares under the Company's restricted stock plans. Management recognizes compensation expense for the fair value of restricted shares on a straight-line basis over the requisite service period.

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The following is a summary of the status of the Company's stock option activity and related information for its option plan for the six months ended March 31, 2012:

	Number of Stock Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Balance at September 30, 2011	188,276	\$ 14.61		
Granted	—	—		
Exercised	—	—		
Forfeited	—	—		
Balance at March 31, 2012	188,276	\$ 14.61	4.9 years	\$ —
Exercisable at March 31, 2012	188,276	\$ 14.61	4.9 years	\$ —

The following is a summary of the Company's non-vested stock awards as of March 31, 2012 and changes during the six months ended March 31, 2012:

	Number of Stock Awards	Weighted Average Grant Date Fair Value
Balance at September 30, 2011	33,145	\$ 9.22
Granted	—	—
Vested	(15,693)	14.55
Forfeited	—	—
Balance at March 31, 2012	17,452	\$ 4.43

Stock option and stock award expenses included with compensation expense were \$68,000 and \$104,000, respectively, for the six months ended March 31, 2012.

The Company announced in November 2007 its second stock repurchase program of up to 5% of its publicly-held outstanding shares of common stock, or 129,924 shares. Through March 31, 2012, the Company had repurchased a total of 77,670 shares of its common stock at an average cost of \$8.51 per share under this program. 10,700 shares

were repurchased during the six months ended March 31, 2012 at an average price of \$2.94. Under the stock repurchase program, 52,254 shares of the 129,924 shares authorized remained available for repurchase as of March 31, 2012. The Company's intended use of the repurchased shares is for general corporate purposes, including the funding of awards granted under the 2006 Equity Incentive Plan.

The Company has an Employee Stock Ownership Plan ("ESOP") for the benefit of employees of the Company and the Bank who meets the eligibility requirements as defined in the plan. The ESOP trust purchased 217,863 shares of common stock in the open market using proceeds of a loan from the Company. The total cost of shares purchased by the ESOP trust was \$2.3 million, reflecting an average cost per share of \$10.58. The Bank will make cash contributions to the ESOP on an annual basis sufficient to enable the ESOP to make the required loan payments to the Company. The loan bears a variable interest rate that adjusts annually every January 1<sup>st</sup> to the then published Prime Rate (3.25% at January 1, 2012) with principal and interest payable annually in equal installments over thirty years. The loan is secured by shares of the Company's stock.

As the debt is repaid, shares are released as collateral and allocated to qualified employees. Accordingly, the shares pledged as collateral are reported as unearned ESOP shares in the Consolidated Balance Sheet. As shares are released from collateral, the Company reports compensation expense equal to the then current market price of the shares, and the shares become outstanding for earnings per share computations.

At March 31, 2012, shares allocated to participants totaled 103,545. Unallocated ESOP shares held in suspense totaled 114,318 at March 31, 2012 and had a fair market value of \$588,738. The Company's contribution expense for the ESOP was \$23,000 and \$27,000 for the six months ended March 31, 2012 and 2011, respectively.



We use fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Our securities available-for-sale are recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record at fair value other assets or liabilities on a non-recurring basis, such as held-to-maturity securities, mortgage servicing rights, loans receivable and other real estate owned, or OREO. These non-recurring fair value adjustments involve the application of lower-of-cost-or-market accounting or write-downs of individual assets.

In accordance with ASC 820, we group our assets and liabilities 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 our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques. The results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability.

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We base our 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. ASC 820 requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

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

Securities available-for-sale

Our available-for-sale portfolio is carried at estimated fair value on a recurring basis, with any unrealized gains and losses, net of taxes, reported as accumulated other comprehensive income/loss in stockholders' equity. Our securities available-for-sale portfolio consists of U.S government and government-sponsored enterprise obligations, municipal bonds, and mortgage-backed securities. The fair values of these securities are obtained from an independent nationally recognized pricing service. Our independent pricing service provides us with prices which are categorized as Level 2, as quoted prices in active markets for identical assets are generally not available for the securities in our portfolio. Various modeling techniques are used to determine pricing for our mortgage-backed securities, including option pricing and discounted cash flow models. The inputs to these models include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data.

Derivative financial instruments

The Company uses interest rate floors to manage its interest rate risk. The interest rate floors have been designated as cash flow hedging instruments. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities.

The following table provides the level of valuation assumptions used to determine the carrying value of our assets measured at fair value on a recurring basis.

	Fair Value at March 31, 2012			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Securities available for sale:				
Obligations of U.S. government agencies:				
Mortgage backed securities - residential	\$5,081	\$ —	\$5,081	\$ —
Obligations of U.S. government-sponsored enterprises:				
Mortgage-backed securities-residential	15,323	—	15,323	—

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Mortgage backed securities-commercial	4,310	—	4,310	—
Debt securities	1,040	—	1,040	—
Private label mortgage-backed securities-residential	1,209	—	1,209	—
Total securities available for sale	\$26,963	\$ —	\$26,963	\$ —

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	Fair Value at September 30, 2011			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Securities available for sale:				
Obligations of U.S. government agencies:				
Mortgage backed securities - residential	\$3,394	\$ —	\$3,394	\$ —
Obligations of U.S. government-sponsored enterprises:				
Mortgage-backed securities-residential	14,088	—	14,088	—
Mortgage backed securities-commercial	4,402	—	4,402	—
Debt securities	2,029	—	2,029	—
Private label mortgage-backed securities-residential	1,399	—	1,399	—
Total securities available for sale	\$25,312	\$ —	\$25,312	\$ —

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

Mortgage Servicing Rights, net

Mortgage Servicing Rights (MSRs) are carried at the lower of cost or estimated fair value. The estimated fair value of MSR is determined through a calculation of future cash flows, incorporating estimates of assumptions market participants would use in determining fair value including market discount rates, prepayment speeds, servicing income, servicing costs, default rates and other market driven data, including the market's perception of future interest rate movements and, as such, are classified as Level 3.

Impaired Loans

Loans which meet certain criteria are evaluated individually for impairment. A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. All amounts due according to the contractual terms means that both the contractual interest and principal payments of a loan will be collected as scheduled in the loan agreement. Three impairment measurement methods are used, depending upon the collateral securing the asset: 1) the present value of expected future cash flows discounted at the loan's effective interest rate (the rate of return implicit in the loan); 2) the asset's observable market price; or 3) the fair value of the collateral if the asset is collateral dependent. The regulatory agencies require this method for loans from which repayment is expected to be provided solely by the underlying collateral. Our impaired loans are generally collateral dependent and, as such, are carried at the estimated fair value of the collateral less estimated selling costs. Fair value is estimated through current appraisals, and adjusted as necessary, by management, to reflect current market conditions and, as such, are generally classified as Level 3.



Appraisals of collateral securing impaired loans are conducted by approved, qualified, and independent third-party appraisers. Such appraisals are ordered via the Bank's credit administration department, independent from the lender who originated the loan, once the loan is deemed impaired, as described in the previous paragraph. Impaired loans are generally re-evaluated with an updated appraisal within one year of the last appraisal. However, the Company also obtains updated appraisals on performing construction loans that are approaching their maturity date to determine whether or not the fair value of the collateral securing the loan remains sufficient to cover the loan amount prior to considering an extension. The Company discounts the appraised "as is" value of the collateral for estimated selling and disposition costs and compares the resulting fair value of collateral to the outstanding loan amount. If the outstanding loan amount is greater than the discounted fair value, the Company requires a reduction in the outstanding loan balance or additional collateral before considering an extension to the loan. If the borrower is unwilling or unable to reduce the loan balance or increase the collateral securing the loan, it is deemed impaired and the difference between the loan amount and the fair value of collateral, net of estimated selling and disposition costs, is charged off through a reduction of the allowance for loan loss.

#### Other Real Estate Owned

The fair value of other real estate owned is determined through current appraisals, and adjusted as necessary, by management, to reflect current market conditions. As such, other real estate owned is generally classified as Level 3.

The following table provides the level of valuation assumptions used to determine the carrying value of our assets measured at fair value on a non-recurring basis at March 31, 2012 and September 30, 2011.

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## Fair Value at March 31, 2012

Total	Level 1	Level 2	Level 3
-------	---------	---------	---------

(Dollars in thousands)

Impaired loans	\$4,117	\$ —	—\$4,117
Other real estate owned	253	—	— 253
	\$4,370	\$ —	—\$4,370

## Fair Value at September 30, 2011

Total	Level 1	Level 2	Level 3
-------	---------	---------	---------

(Dollars in thousands)

Impaired loans	\$16,745	\$ —	—\$16,745
Other real estate owned	2,625	—	— 2,625
	\$19,370	\$ —	—\$19,370

The following methods and assumptions were used to estimate the fair value of each class of financial instruments not already disclosed above for which it is practicable to estimate fair value:

Cash and interest earning deposits with banks: The carrying amounts are a reasonable estimate of fair value.

Held to maturity securities: The fair values of our held to maturity securities are obtained from an independent nationally recognized pricing service. Our independent pricing service provides us with prices which are categorized as Level 2, as quoted prices in active markets for identical assets are generally not available for the securities in our portfolio.

Loans: Fair value for the loan portfolio, excluding impaired loans with specific loss allowances, is estimated based on discounted cash flow analysis using interest rates currently offered for loans with similar terms to borrowers of similar credit quality.

Federal Home Loan Bank of New York (“FHLB”) stock: The carrying amount of FHLB stock approximates fair value and considers the limited marketability of the investment.

Bank-owned life insurance: The carrying amounts are based on the cash surrender values of the individual policies, which is a reasonable estimate of fair value.

The fair value of commitments to extend credit is estimated based on the amount of unamortized deferred loan commitment fees. The fair value of letters of credit is based on the amount of unearned fees plus the estimated costs to terminate the letters of credit. Fair values of unrecognized financial instruments including commitments to extend credit and the fair value of letter of credit are considered immaterial.

Deposits: The fair value of deposits with no stated maturity, such as money market deposit accounts, interest-bearing checking accounts and savings accounts, is equal to the amount payable on demand. The fair value of certificates of deposit is based on the discounted value of contractual cash flows. The discount rate is equivalent to current market rates for deposits of similar size, type and maturity.

Accrued interest receivable and payable: For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

Federal Home Loan Bank of New York advances and securities sold under reverse repurchase agreements: The fair value of borrowings is based on the discounted value of contractual cash flows. The discount rate is equivalent to the rate currently offered by the Federal Home Loan Bank of New York for borrowings of similar maturity and terms.

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The carrying amounts and estimated fair values of the Company's financial instruments at March 31, 2012 and September 30, 2011 were as follows:

	March 31, 2012		September 30, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
(Dollars in thousands)				
Financial assets				
Investment securities	\$72,462	\$73,225	\$70,312	\$71,025
Loans, net of allowance for loan losses	380,859	391,099	381,254	390,025
Bank owned life insurance	9,836	9,836	9,660	9,660
Financial liabilities				
Deposits				
Demand, NOW and money market savings	254,769	254,769	249,383	249,383
Certificates of deposit	167,754	170,845	175,560	178,818
Total deposits	\$422,523	\$425,614	\$424,943	\$428,201
Borrowings	\$47,688	\$50,823	\$49,916	\$53,175

The fair value of commitments to extend credit is estimated based on the amount of unamortized deferred loan commitment fees. The fair value of letters of credit is based on the amount of unearned fees plus the estimated cost to terminate the letters of credit. Fair values of unrecognized financial instruments including commitments to extend credit and the fair value of letters of credit are considered immaterial.

Cash and cash equivalents, accrued interest receivable and accrued interest payable are not presented in the above table as the carrying amounts shown in the consolidated balance sheet equal fair value.

The following presents the carrying amount, fair value, and placement in the fair value hierarchy of the Company's financial instruments carried at cost or amortized cost as of March 31, 2012 and September 30, 2011. This table excludes financial instruments for which the carrying amount approximates fair value. For short-term financial assets such as cash and cash equivalents, the carrying amount is a reasonable estimate of fair value due to the relatively short time between the origination of the instrument and its expected realization. For financial liabilities such as interest-bearing demand, NOW, and money market savings deposits, the carrying amount is a reasonable estimate of fair value due to these products having no stated maturity.

Carrying Fair

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Fair Value Measurement  
Placement

(Level 1) (Level 2) (Level 3)

Value Value  
(Dollars in thousands)

March 31, 2012

Financial instruments - assets

Investment securities held-to-maturity	\$ 45,499	\$46,262	\$2,953	\$43,309	\$ —
Loans	380,859	391,099			391,099

Financial instruments - liabilities

Certificate of deposit	167,754	170,845	—	170,845	—
Borrowings	47,688	50,823	—	50,823	—

September 30, 2011

Financial instruments - assets

Investment securities held-to-maturity	\$ 45,000	\$45,713	\$2,914	\$42,799	\$ —
Loans	381,254	390,025			390,025

Financial instruments - liabilities

Certificate of deposit	175,560	178,818	—	178,818	—
Borrowings	49,916	53,175	—	53,175	—

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## NOTE H - INVESTMENT SECURITIES

The following tables summarize the amortized cost and fair values of securities available for sale at March 31, 2012 and September 30, 2011:

	At March 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Securities available for sale:				
Obligations of U.S. government agencies:				
Mortgage backed securities - residential	\$4,993	\$ 89	\$ (1 )	\$5,081
Obligations of U.S. government-sponsored enterprises:				
Mortgage-backed securities-residential	15,195	141	(13 )	15,323
Mortgage backed securities-commercial	4,095	215	—	4,310
Debt securities	1,000	40	—	1,040
Private label mortgage-backed securities-residential	1,219	—	(10 )	1,209
Total securities available for sale	\$26,502	\$ 485	\$ (24 )	\$26,963

	At September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Securities available for sale:				
Obligations of U.S. government agencies:				
Mortgage backed securities - residential	\$3,310	\$ 84	\$ —	\$3,394
Obligations of U.S. government-sponsored enterprises:				
Mortgage-backed securities-residential	13,915	215	(42 )	14,088
Mortgage backed securities-commercial	4,137	265	—	4,402
Debt securities	2,000	29	—	2,029
Private label mortgage-backed securities-residential	1,456	—	(57 )	1,399
Total securities available for sale	\$24,818	\$ 593	\$ (99 )	\$25,312

The maturities of the debt securities and mortgage-backed securities available-for-sale at December 31, 2011 are summarized in the following table:

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	At March 31, 2012	
	Amortized Cost	Fair Value
	(Dollars in thousands)	
Due within 1 year	\$—	\$—
Due after 1 but within 5 years	—	—
Due after 5 but within 10 years	1,000	1,040
Due after 10 years	—	—
Total debt securities	1,000	1,040
Mortgage-backed securities:		
Residential	21,407	21,613
Commercial	4,095	4,310
Total	\$26,502	\$26,963

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The following tables summarize the amortized cost and fair values of securities held to maturity at March 31, 2012 and September 30, 2011:

	At March 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(Dollars in thousands)				
Securities held to maturity:				
Obligations of U.S. government agencies:				
Mortgage-backed securities-residential	\$13,428	\$ 465	\$ (25)	) \$13,868
Mortgage-backed securities-commercial	1,604	17	—	1,621
Obligations of U.S. government-sponsored enterprises:				
Mortgage backed securities-residential	17,492	467	(9)	) 17,950
Debt securities	8,496	3	(74)	) 8,425
Private label mortgage-backed securities-residential	1,438	47	(83)	) 1,402
Obligations of state and political subdivisions	41	2	—	43
Corporate securities	3,000	—	(47)	) 2,953
Total securities held to maturity	\$45,499	\$ 1,001	\$ (238)	) \$46,262

	At September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(Dollars in thousands)				
Securities held to maturity:				
Obligations of U.S. government agencies:				
Mortgage-backed securities-residential	\$14,875	\$ 483	\$ (11)	) \$15,347
Mortgage-backed securities-commercial	1,646	18	—	1,664
Obligations of U.S. government-sponsored enterprises:				
Mortgage backed securities-residential	17,315	441	—	17,756
Debt securities	6,500	12	—	6,512
Private label mortgage-backed securities-residential	1,592	14	(160)	) 1,446
Obligations of state and political subdivisions	72	2	—	74
Corporate securities	3,000	—	(86)	) 2,914
Total securities held to maturity	\$45,000	\$ 970	\$ (257)	) \$45,713

The maturities of the debt securities and the mortgage backed securities held to maturity at March 31, 2012 are summarized in the following table:



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At March 31,  
2012

Amortized Cost      Fair Value  
(Dollars in  
thousands)

Due within 1 year	\$—	\$—
Due after 1 but within 5 years	3,041	2,996
Due after 5 but within 10 years	—	—
Due after 10 years	8,496	8,425
Total debt securities	11,537	11,421

Mortgage-backed securities:

Residential	32,358	33,220
Commercial	1,604	1,621
Total	\$45,499	\$46,262

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## NOTE I – IMPAIRMENT OF INVESTMENT SECURITIES

The Company recognizes credit-related other-than-temporary impairment on debt securities in earnings while noncredit-related other-than-temporary impairment on debt securities not expected to be sold are recognized in other comprehensive income (“OCI”).

We review our investment portfolio on a quarterly basis for indications of impairment. This review includes analyzing the length of time and the extent to which the fair value has been lower than the cost, the financial condition and near-term prospects of the issuer, including any specific events which may influence the operations of the issuer and the intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in the market. We evaluate our intent and ability to hold debt securities based upon our investment strategy for the particular type of security and our cash flow needs, liquidity position, capital adequacy and interest rate risk position. In addition, the risk of future other-than-temporary impairment may be influenced by prolonged recession in the U.S. economy, changes in real estate values and interest deferrals.

Investment securities with fair values less than their amortized cost contain unrealized losses. The following tables present the gross unrealized losses and fair value at March 31, 2012 and September 30, 2011 for both available for sale and held to maturity securities by investment category and time frame for which the loss has been outstanding:

	Number of Securities	March 31, 2012		12 Months Or Greater		Total	
		Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
(Dollars in thousands)							
Obligations of U.S. government agencies:							
Mortgage-backed securities - residential	2	\$1,950	\$ (1 )	\$2,031	\$ (25 )	\$3,981	\$ (26 )
Mortgage-backed securities - commercial	1	—	—	20	—	20	—
Obligations of U.S. government-sponsored enterprises:							
Mortgage backed securities - residential	3	4,080	(22 )	—	—	4,080	(22 )
Debt securities	4	5,923	(74 )	—	—	5,923	(74 )
Private label mortgage-backed securities-residential	3	—	—	1,996	(93 )	1,996	(93 )
Corporate securities	1	2,953	(47 )	—	—	2,953	(47 )
Total	14	\$14,906	\$ (144 )	\$4,047	\$ (118 )	\$18,953	\$ (262 )

September 30, 2011

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	Number of Securities	Less Than 12 Months		12 Months Or Greater		Total	
		Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
(Dollars in thousands)							
Obligations of U.S. government agencies:							
Mortgage-backed securities - residential	1	\$2,339	\$ (11 )	\$—	\$ —	\$2,339	\$ (11 )
Mortgage-backed securities - commercial	1	—	—	21	—	21	—
Obligations of U.S. government-sponsored enterprises:							
Mortgage backed securities - residential	4	6,925	(42 )	—	—	6,925	(42 )
Private label mortgage-backed securities residential	3	—	—	2,132	(217 )	2,132	(217 )
Corporate securities	1	2,914	(86 )	—	—	2,914	(86 )
Total	10	\$12,178	\$ (139 )	\$2,153	\$ (217 )	\$14,331	\$ (356 )

At March 31, 2012, there were fourteen investment securities with unrealized losses. The Company anticipates full recovery of amortized costs with respect to these securities. The Company does not intend to sell these securities and has determined that it is not more likely than not that the Company would be required to sell these securities prior to maturity or market price recovery. Management has considered factors regarding other than temporarily impaired securities and determined that there are no securities with impairment that is other than temporary as of March 31, 2012.

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## NOTE J – LOANS RECEIVABLE, NET AND RELATED ALLOWANCE FOR LOAN LOSSES

Loans receivable, net were comprised of the following:

	March 31, 2012	September 30, 2011
	(Dollars in thousands)	
One-to four-family residential	\$ 161,997	\$ 159,228
Commercial real estate	137,614	120,994
Construction	24,519	34,144
Home equity lines of credit	21,525	22,352
Commercial business	27,305	36,195
Other	11,762	11,945
Total loans receivable	384,722	384,858
Net deferred loan costs	145	208
Allowance for loan losses	(4,008 )	(3,812 )
Total loans receivable, net	\$380,859	\$381,254

The segments of the Bank's loan portfolio are disaggregated to a level that allows management to monitor risk and performance. The residential mortgage loan segment is further disaggregated into two classes: amortizing term loans, which are primarily first liens, and home equity lines of credit, which are generally second liens. The commercial real estate loan segment is further disaggregated into three classes. Commercial real estate loans include loans secured by multifamily structures, owner-occupied commercial structures, and non-owner occupied nonresidential properties. The construction loan segment consists primarily of loans to developers or investors for the purpose of acquiring, developing and constructing residential or commercial structures and to a lesser extent one-to-four family residential construction loans made to individuals for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built. Construction loans to developers and investors have a higher risk profile because the ultimate buyer, once development is completed, is generally not known at the time of the loan. The commercial business loan segment consists of loans made for the purpose of financing the activities of commercial customers and consists primarily of revolving lines of credit. The consumer loan segment consists primarily of stock-secured installment loans, but also includes unsecured personal loans and overdraft lines of credit connected with customer deposit accounts.

Management evaluates individual loans in all segments for possible impairment if the loan either is in nonaccrual status, or is risk rated Substandard and is greater than 90 days past due. Loans are considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors

considered by management in evaluating impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Once the determination has been made that a loan is impaired, the recorded investment in the loan is compared to the fair value of the loan using one of three methods: (a) the present value of expected future cash flows discounted at the loan's effective interest rate; (b) the loan's observable market price; or (c) the fair value of the collateral securing the loan, less anticipated selling and disposition costs. The method is selected on a loan-by loan basis, with management primarily utilizing the fair value of collateral method. If there is a shortfall between the fair value of the loan and the recorded investment in the loan, the Company charges the difference to the allowance for loan loss as a charge-off and carries the impaired loan on its books at fair value. It is the Company's policy to evaluate impaired loans on an annual basis to ensure the recorded investment in a loan does not exceed its fair value.

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The following table presents impaired loans by class, segregated by those for which a specific allowance was required and charged-off and those for which a specific allowance was not necessary at the dates presented:

	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
At March 31, 2012	(Dollars in thousands)				
One-to four-family residential	\$—	\$ —	\$ 5,354	\$5,354	\$ 5,428
Commercial real estate	1,679	492	5,892	7,571	8,575
Construction	—	—	11,360	11,360	14,200
Home equity lines of credit	1,340	127	707	2,047	2,128
Commercial business	—	—	225	225	313
Total impaired loans	\$3,019	\$ 619	\$ 23,538	\$26,557	\$ 30,644

	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
At September 30, 2011	(Dollars in thousands)				
One-to four-family residential	\$—	\$ —	\$ 3,523	\$3,523	\$ 3,532
Commercial real estate	1,679	239	5,477	7,156	8,160
Construction	3,263	77	12,294	15,557	18,831
Home equity lines of credit	—	—	788	788	833
Commercial business	—	—	255	255	342
Total impaired loans	\$4,942	\$ 316	\$ 22,337	\$27,279	\$ 31,698

The following table presents the average recorded investment in impaired loans for the periods indicated. There was no interest income recognized on impaired loans during the periods presented.

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During the Three Months Ended March 31, 2012  
 During the Six Months Ended March 31, 2012  
 (Dollars in thousands)

One-to four-family residential	\$4,601	\$4,242
Commercial real estate	7,064	7,094
Construction	11,432	12,807
Home equity lines of credit	1,377	1,181
Commercial business	231	239
Other	—	—
Average investment in impaired loans	\$24,704	\$25,562
Interest income recognized on an accrual basis on impaired loans	\$—	\$—
Interest income recognized on a cash basis on impaired loans	\$—	\$—

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Management uses a ten point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized, and are aggregated as “Pass” rated. The criticized rating categories utilized by management generally follow bank regulatory definitions. The Special Mention category includes assets that are currently protected but are potentially weak, resulting in an undue and unwarranted credit risk, but not to the point of justifying a Substandard classification. Loans in the Substandard category have well-defined weaknesses that jeopardize the liquidation of the debt, and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. All loans greater than three months past due are considered Substandard. Any portion of a loan that has been charged off is placed in the Loss category.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Bank has a structured loan rating process with several layers of internal and external oversight. Generally, consumer and residential mortgage loans are included in the Pass categories unless a specific action, such as severe delinquency, bankruptcy, repossession, or death occurs to raise awareness of a possible credit event. The Bank’s Commercial Loan Officers are responsible for the timely and accurate risk rating of the loans in their portfolios at origination and on an ongoing basis. The Asset Review Committee performs monthly reviews of all commercial relationships internally rated 6 (“Watch”) or worse. Confirmation of the appropriate risk grade is performed by an external Loan Review Company that semi-annually reviews and assesses loans within the portfolio. Generally, the external consultant reviews commercial relationships greater than \$500,000 and/or criticized relationships greater than \$250,000. Detailed reviews, including plans for resolution, are performed on loans classified as Substandard on a monthly basis.

The following table presents the classes of the loan portfolio summarized by the aggregate Pass and the criticized categories of Special Mention, Substandard and Doubtful within the Bank’s internal risk rating system at the dates presented:

	Pass	Special Mention	Substandard	Doubtful	Total
	(Dollars in thousands)				
March 31, 2012					
One-to four-family residential	\$ 150,488	\$ 6,155	\$ 5,354	\$ —	\$ 161,997
Commercial real estate	123,117	5,751	7,067	1,679	137,614
Construction	8,678	4,481	11,360	—	24,519
Home equity lines of credit	18,645	833	707	1,340	21,525
Commercial business	24,846	1,551	908	—	27,305
Other	11,762	—	—	—	11,762
Total	\$ 337,536	\$ 18,771	\$ 25,396	\$ 3,019	\$ 384,722

	Pass	Special Mention	Substandard	Doubtful	Total
	(Dollars in thousands)				
September 30, 2011					



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One-to four-family residential	\$ 150,306	\$ 4,720	\$ 4,202	\$	—	\$ 159,228
Commercial real estate	104,993	5,868	10,133		—	120,994
Construction	12,378	6,209	15,557		—	34,144
Home equity lines of credit	20,092	833	1,427		—	22,352
Commercial business	29,927	5,039	1,229		—	36,195
Other	11,945	—	—		—	11,945
Total	\$ 329,641	\$ 22,669	\$ 32,548	\$	—	\$ 384,858

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Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following table presents the classes of the loan portfolio summarized by the aging categories of performing loans and nonaccrual loans at the dates presented:

		30-59	60-89	90			
	Current	Days	Days	Days	Total	Non-	Total
		Past	Past	+	Past	Accrual	Loans
		Due	Due	Past	Due		
		Due	Due	Due	Due		
(Dollars in thousands)							
March 31, 2012							
One-to four-family residential	\$ 155,177	\$ 530	\$ 188	\$ 6,102	\$ 6,820	\$ 5,354	\$ 161,997
Commercial real estate	128,777	494	—	8,343	8,837	8,343	137,614
Construction	13,159	—	—	11,360	11,360	11,360	24,519
Home equity lines of credit	20,719	127	150	529	806	529	21,525
Commercial business	27,021	12	—	272	284	272	27,305
Other	11,762	—	—	—	—	—	11,762
Total	\$ 356,615	\$ 1,163	\$ 338	\$ 26,606	\$ 28,107	\$ 25,858	\$ 384,722

		30-59	60-89	90			
	Current	Days	Days	Days	Total	Non-	Total
		Past	Past	+	Past	Accrual	Loans
		Due	Due	Past	Due		
		Due	Due	Due	Due		
(Dollars in thousands)							
September 30, 2011							
One-to four-family residential	\$ 154,164	\$ 523	\$ 485	\$ 4,056	\$ 5,064	\$ 3,523	\$ 159,228
Commercial real estate	112,546	—	851	7,597	8,448	7,156	120,994
Construction	18,588	—	92	15,464	15,556	15,464	34,144
Home equity lines of credit	21,384	180	—	788	968	788	22,352
Commercial business	35,940	—	—	255	255	255	36,195
Other	11,945	—	—	—	—	—	11,945
Total	\$ 354,567	\$ 703	\$ 1,428	\$ 28,160	\$ 30,291	\$ 27,186	\$ 384,858

At March 31, 2012, nonaccrual loans totaled \$25,853,000 and loans ninety days or more delinquent and accruing interest totaled \$748,000. At September 30, 2011, nonaccrual loans totaled \$27,186,000 and loans ninety days or more delinquent and accruing interest totaled \$974,000.

An allowance for loan losses (“ALL”) is maintained to absorb losses from the loan portfolio. The ALL is based on management’s continuing evaluation of the risk characteristics and credit quality of the loan portfolio, assessment of current economic conditions, diversification and size of the portfolio, adequacy of collateral, past and anticipated loss

experience, and the amount of NPLs.

The Bank's methodology for determining the ALL is based on the requirements of ASC Section 310-10-35 for loans individually evaluated for impairment (discussed above) and ASC Subtopic 450-20 for loans collectively evaluated for impairment, as well as the Interagency Policy Statements on the Allowance for Loan and Lease Losses and other bank regulatory guidance.

Loans that are collectively evaluated for impairment are analyzed with general allowances being made as appropriate. For general allowances, historical loss trends are used in the estimation of losses in the current portfolio. These historical loss amounts are modified by other qualitative and economic factors.

The loans are segmented into classes based on their inherent varying degrees of risk, as described above. Management tracks the historical net charge-off activity by segment and utilizes this figure, as a percentage of the segment, as the general reserve percentage for pooled, homogenous loans that have not been deemed impaired. Typically, an average of losses incurred over a defined number of consecutive historical years is used. A 5 year history is currently utilized for all loan segments except for construction loans, where the highest single year loss percentage of the most recent five years is used in place of a 5 year average.

Non-impaired credits are segregated for the application of qualitative factors. Management has identified a number of additional qualitative factors which it uses to supplement the historical charge-off factor because these factors are likely to cause estimated credit losses associated with the existing loan pools to differ from historical loss experience. The additional factors that are evaluated quarterly and updated using information obtained from internal, regulatory, and governmental sources are: national and local economic trends and conditions; levels of and trends in delinquency rates and non-accrual loans; trends in volumes and terms of loans; effects of changes in lending policies; experience, ability, and depth of lending staff; value of underlying collateral; and concentrations of credit from a loan type, industry and/or geographic standpoint.

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Management reviews the loan portfolio on a quarterly basis using a defined, consistently applied process in order to make appropriate and timely adjustments to the ALL. When information confirms all or part of specific loans to be uncollectible, these amounts are promptly charged off against the ALL. Since loans individually evaluated for impairment are promptly written down to their fair value, typically there is no portion of the ALL for loans individually evaluated for impairment.

The following table summarizes the ALL by loan category at both September 30, 2011 and March 31, 2012 and the related activity for the six months ended March 31, 2012:

	One-to Four- Family Residential	Commercial Real Estate	Construction	Home Equity Lines of Credit	Commercial Business	Other	Unallocated	Total
	(Dollars in thousands)							
Balance- September 30, 2011	\$734	\$ 1,266	\$ 1,043	\$ 101	\$ 551	\$ 13	\$ 104	\$3,812
Charge-offs	—	—	(184 )	(81 )	(69 )	—	—	(334 )
Recoveries	—	—	—	—	—	—	—	—
Provision	(148)	245	90	58	135	(7 )	(3 )	370
Balance- December 31, 2011	\$586	\$ 1,511	\$ 949	\$ 78	\$ 617	\$ 6	\$ 101	\$3,848
Charge-offs	(20 )	—	(143 )	—	—	—	—	(163 )
Recoveries	—	—	—	—	—	—	—	—
Provision	245	192	(60 )	150	(212 )	4	4	323
Balance-March 31, 2012	\$811	\$ 1,703	\$ 746	\$ 228	\$ 405	\$ 10	\$ 105	\$4,008

The following table summarizes the ALL by loan category at March 31, 2011 and related activity for the three months ended March 31, 2011:

	One-to Four- Family Residential	Commercial Real Estate	Construction	Home Equity Lines of Credit	Commercial Business	Other	Unallocated	Total
	(Dollars in thousands)							
Balance- December 31, 2010	\$474	\$ 927	\$ 1,695	\$ 65	\$ 605	\$ 12	\$ 509	\$ 4,287
Charge-offs	(32 )	(585 )	(224 )	—	(155 )	—	—	(996 )

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Recoveries	—	—	—	—	—	—	—	—
Provision	22	808	(133 )	(4 )	192	2	(409 )	478
Balance-March 31, 2011	\$464	\$ 1,150	\$ 1,338	\$ 61	\$ 642	\$ 14	\$ 100	\$ 3,769

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The following table summarize the ALL by loan category, segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of March 31, 2012 and September 30, 2011:

	One-to Four- Family Residential	Commercial Real Estate	Construction	Home Equity Lines of Credit	Commercial Business	Other	Unallocated	Total
(Dollars in thousands)								
<u>Allowance for Loan</u>								
<u>Losses:</u>								
Balance- March 31, 2012	\$ 811	\$ 1,703	\$ 746	\$ 228	\$ 405	\$ 10	\$ 105	\$ 4,008
Individually evaluated for impairment	—	492	—	127	—	—	—	619
Collectively evaluated for impairment	811	1,211	746	101	405	10	105	3,389
Loans receivable:								
Balance- March 31, 2012	\$ 161,997	\$ 137,614	\$ 24,519	\$ 21,525	\$ 27,305	\$ 11,762		\$ 384,722
Individually evaluated for impairment	5,354	7,571	11,360	2,047	225	—		26,557
Collectively evaluated for impairment	156,643	130,043	13,159	19,478	27,080	11,762		358,165
	One-to Four- Family Residential	Commercial Real Estate	Construction	Home Equity Lines of Credit	Commercial Business	Other	Unallocated	Total
(Dollars in thousands)								
<u>Allowance for Loan</u>								
<u>Losses:</u>								
Balance- September 30, 2011	\$ 734	\$ 1,266	\$ 1,043	\$ 101	\$ 551	\$ 13	\$ 104	\$ 3,812
Individually evaluated for impairment	—	239	77	—	—	—	—	316
Collectively evaluated for impairment	734	1,027	966	101	551	13	104	3,496
Loans receivable:								
Balance- September 30, 2011	\$ 159,228	\$ 120,994	\$ 34,144	\$ 22,352	\$ 36,195	\$ 11,945		\$ 384,858
Individually evaluated for impairment	3,523	7,156	15,557	788	255	—		27,279
Collectively evaluated for impairment	155,705	113,838	18,587	21,564	35,940	11,945		357,579

The allowance for loan losses is based on estimates, and actual losses will vary from current estimates. Management believes that the segmentation of the loan portfolio into homogeneous pools and the related historical loss ratios and other qualitative factors, as well as the consistency in the application of assumptions, result in an ALL that is representative of the risk found in the components of the portfolio at any given date.

The Bank has adopted FASB issue ASU No. 2011-02 on the determination of whether a loan restructuring is considered to be a Troubled Debt Restructuring (“TDR”). A TDR is a loan that has been modified whereby the Bank has agreed to make certain concessions to a borrower to meet the needs of both the borrower and the Bank to maximize the ultimate recovery of a loan. TDR occurs when a borrower is experiencing, or is expected to experience, financial difficulties and the loan is modified using a modification that would otherwise not be granted to the borrower. The types of concessions granted are generally included, but not limited to interest rate reductions, limitations on the accrued interest charged, term extensions, and deferment of principal.

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There were no TDRs during the three months ended March 31, 2012 and two TDRs during the six months ended March 31, 2012. These were classified as TDRs due to financial difficulty of the borrowers and lower than market interest rates. The following table summarizes the TDRs during the six month period ended March 31, 2012:

	Six Months Ended March 31, 2012		
	Number of Loans	Investment Before TDR Modification	Investment After TDR Modification
		(Dollars in thousands)	
One-to four-family residential	1	\$ 1,749	\$ 1,749
Commercial real estate	1	249	249
Total	2	\$ 1,998	\$ 1,998

A default on a troubled debt restructured loan for purposes of this disclosure occurs when a borrower is 90 days past due or a foreclosure or repossession of the applicable collateral has occurred. During the three and six months ended March 31, 2012, no defaults occurred on troubled debt restructured loans that were modified as a TDR within the previous 12 months.

## NOTE K - DEPOSITS

A summary of deposits by type of account are summarized as follows:

	2012 March 31	2011 September 30
	(Dollars in thousands)	
Demand accounts	\$52,685	\$51,220
Savings accounts	57,618	60,533
NOW accounts	38,100	30,941
Money market accounts	106,366	106,689
Certificates of deposit	138,706	144,739
Retirement certificates	29,048	30,821
	\$422,523	\$424,943



NOTE L – INCOME TAXES

The Company records income taxes using the asset and liability method. Accordingly, deferred tax assets and liabilities: (i) are recognized for the expected future tax consequences of events that have been recognized in the financial statements or tax returns; (ii) are attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases; and (iii) are measured using enacted tax rates expected to apply in the years when those temporary differences are expected to be recovered or settled.

Where applicable, deferred tax assets are reduced by a valuation allowance for any portions determined not likely to be realized. The valuation allowance is assessed by management on a quarterly basis and adjusted, by a charge or credit to income tax expense, as changes in facts and circumstances warrant. In assessing whether it is more likely than not that some portion or all of the deferred tax assets will not be realized, management considers projections of future taxable income, the projected periods in which current temporary differences will be deductible, the availability of carry forwards, feasible and permissible tax planning strategies and existing tax laws and regulations. Due to the uncertainty of the Company's ability to realize the benefit of certain deferred tax assets within statutory time limits, the net deferred tax assets are partially offset by a valuation allowance at March 31, 2012, the amount of which has not materially changed from that in place at September 30, 2011.

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A reconciliation of income tax between the amounts calculated based upon pre-tax income (loss) at the Company's federal statutory rate and the amounts reflected in the consolidated statements of operations are as follows:

	For the Three Months Ended March 31,		For the Six Months Ended March 31,	
	2012	2011	2012	2011
	(in thousands)			
Income tax (benefit) expense at 34% statutory federal tax rate	\$ (11 )	\$ (204 )	\$ 2	\$ (149 )
Change in valuation allowance related to deferred income tax assets	(7 )	—	9	—
State tax benefit	3	(18 )	11	(13 )
Other	(27 )	(22 )	(57 )	(46 )
Income tax benefit	\$ (42 )	\$ (244 )	\$ (35 )	\$ (208 )

## NOTE M - FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Company uses derivative financial instruments, such as interest rate floors and collars, as part of its interest rate risk management. Interest rate caps and floors are agreements whereby one party agrees to pay or receive a floating rate of interest on a notional principal amount for a predetermined period of time if certain market interest rate thresholds are met. The Company considers the credit risk inherent in these contracts to be negligible.

As of March 31, 2012 and September 30, 2011, the Company did not hold any interest rate floors or collars.

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments are commitments to extend credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the balance

sheets.

	2012	2011
	March	September
	31	30
	(Dollars in thousands)	
Financial instruments whose contract amounts represent credit risk		
Letters of credit	\$1,518	\$ 1,508
Unused lines of credit	36,121	37,502
Fixed rate loan commitments	3,228	2,368
Variable rate loan commitments	7,271	5,569
	\$48,138	\$ 46,947

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

Forward-Looking Statements

When used in this filing and in future filings by the Company with the Securities and Exchange Commission, in the Company's press releases or other public or shareholder communications, or in oral statements made with the approval of an authorized executive officer, the words or phrases, "anticipate," "would be," "will allow," "intends to," "will likely result," "are expected to," "will continue," "is anticipated," "estimated," "projected," "believes", or similar expressions are intended to identify "forward looking statements." Forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, those risks previously disclosed in the Company's filings with the SEC, general economic conditions, changes in interest rates, regulatory considerations, competition, technological developments, retention and recruitment of qualified personnel, and market acceptance of the Company's pricing, products and services, and with respect to the loans extended by the Bank and real estate owned, the following: risks related to the economic environment in the market areas in which the Bank operates, particularly with respect to the real estate market in New Jersey; the risk that the value of the real estate securing these loans may decline in value; and the risk that significant expense may be incurred by the Company in connection with the resolution of these loans.

The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made, and advises readers that various factors, including regional and national economic conditions, substantial changes in levels of market interest rates, credit and other risks of lending and investing activities, and competitive and regulatory factors, could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from those anticipated or projected.

The Company does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

**Critical Accounting Policies**

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. Critical accounting policies may involve complex subjective decisions or assessments. We consider the following to be our critical accounting policies.

***Allowance for Loan Losses.*** The allowance for loan losses is the amount estimated by management as necessary to cover credit losses in the loan portfolio both probable and reasonably estimable at the balance sheet date. The allowance is established through the provision for loan losses which is charged against income. In determining the allowance for loan losses, management makes significant estimates and has identified this policy as one of our most critical. Due to the high degree of judgment involved, the subjectivity of the assumptions utilized and the potential for changes in the economic environment that could result in changes to the amount of the recorded allowance for loan losses, the methodology for determining the allowance for loan losses is considered a critical accounting policy by management.

As a substantial amount of our loan portfolio is collateralized by real estate, appraisals of the underlying value of property securing loans and discounted cash flow valuations of properties are critical in determining the amount of the allowance required for specific loans. Assumptions for appraisals and discounted cash flow valuations are instrumental in determining the value of properties. Overly optimistic assumptions or negative changes to assumptions could significantly affect the valuation of a property securing a loan and the related allowance determined. The assumptions supporting such appraisals and discounted cash flow valuations are carefully reviewed by management to determine that the resulting values reasonably reflect amounts realizable on the related loans.

Management performs a quarterly evaluation of the adequacy of the allowance for loan losses. We consider a variety of factors in establishing this estimate including, but not limited to, current economic conditions, delinquency statistics, geographic and industry concentrations, the adequacy of the underlying collateral, the financial strength of the borrower, results of internal loan reviews and other relevant factors. This evaluation is inherently subjective as it requires material estimates by management that may be susceptible to significant change based on changes in economic and real estate market conditions.

The evaluation has a specific and general component. The specific component relates to loans that are delinquent or otherwise identified as impaired through the application of our loan review process and our loan grading system. All such loans are evaluated individually, with principal consideration given to the value of the collateral securing the loan and discounted cash flows. Specific impairment allowances are established as required by this analysis. The general component is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. We also analyze historical loss experience, delinquency trends, general economic conditions and geographic and industry concentrations. This analysis establishes factors that are applied to the loan groups to determine the amount of the general component of the allowance for loan losses.

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Actual loan losses may be significantly greater than the allowances we have established, which could have a material negative effect on our financial results.

**Other Real Estate Owned.** Real estate acquired through foreclosure, or a deed-in-lieu of foreclosure, is recorded at fair value less estimated selling costs at the date of acquisition or transfer, and subsequently at the lower of its new cost or fair value less estimated selling costs. Adjustments to the carrying value at the date of acquisition or transfer are charged to the allowance for loan losses. The carrying value of the individual properties is subsequently adjusted to the extent it exceeds estimated fair value less estimated selling costs, at which time a provision for losses on such real estate is charged to operations.

Appraisals are critical in determining the fair value of the other real estate owned amount. Assumptions for appraisals are instrumental in determining the value of properties. Overly optimistic assumptions or negative changes to assumptions could significantly affect the valuation of a property. The assumptions supporting such appraisals are carefully reviewed by management to determine that the resulting values reasonably reflect amounts realizable.

**Deferred Income Taxes.** The Company records income taxes using the asset and liability method. Accordingly, deferred tax assets and liabilities: (i) are recognized for the expected future tax consequences of events that have been recognized in the financial statements or tax returns; (ii) are attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases; and (iii) are measured using enacted tax rates expected to apply in the years when those temporary differences are expected to be recovered or settled.

Where applicable, deferred tax assets are reduced by a valuation allowance for any portions determined not likely to be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income tax expense in the period of enactment. The valuation allowance is adjusted, by a charge or credit to income tax expense, as changes in facts and circumstances warrant.

**Comparison of Financial Condition at March 31, 2012 and September 30, 2011**

Total assets decreased \$3.7 million, or 0.7%, to \$520.3 million at March 31, 2012 from \$524.0 million at September 30, 2011. The decrease was attributable to lower cash balances, which decreased \$3.4 million, or 22.6%, to \$11.6 million at March 31, 2012 from \$15.0 million at September 30, 2011 and lower other real estate owned balances, which decreased \$1.9 million, or 11.4%, to \$14.7 million at March 31, 2012 from \$16.6 million at September 30, 2011. The decrease was partially offset by higher balances of investment securities.

Cash and interest bearing deposits with banks decreased \$3.4 million, or 22.6%, to \$11.6 million at March 31, 2012 from \$15.0 million at September 30, 2011. Investment security purchases and net deposit outflows accounted for the year-to-date decline.

Total loans receivable decreased \$136,000 during the six months ended March 31, 2012 to \$384.7 million and were comprised of \$162.0 million (42.1%) one-to-four family residential mortgage loans, \$137.6 million (35.8%) commercial real estate loans, \$27.3 million (7.1%) commercial business loans, \$24.5 million (6.4%) construction loans, \$21.5 million (5.6%) home equity lines of credit and \$11.8 million (3.0%) other loans. Contraction of the portfolio during the six months ended March 31, 2012 occurred primarily in construction loans, which decreased \$9.6 million, followed by a decrease of \$8.9 million in commercial business loans. Commercial real estate loans increased \$16.6 million and residential mortgage loans increased \$2.8 million.

Total non-performing loans ("NPLs") decreased by \$1.6 million to \$26.6 million at March 31, 2012 from \$28.2 million at September 30, 2011. The ratio of NPLs to total loans decreased to 6.9% at March 31, 2012 from 7.3% at September 30, 2011.

Included in the NPLs total at March 31, 2012 were eleven construction loans totaling \$11.4 million, eleven commercial loans totaling \$8.6 million, sixteen residential mortgage loans totaling \$6.1 million, and three home equity lines of credit totaling \$529,000.

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Adverse economic conditions have led to high levels of NPLs, particularly in the Company's construction loan portfolio. The repayment of construction loans is typically dependent upon the sale of the collateral securing the loan, which has been negatively impacted by rapid deterioration in the housing market and decreased buyer demand. As a result, construction projects have slowed and reached their maturity dates. In order for the Company to extend the loans beyond the original maturity date, the value of the collateral securing the loan must be assessed, which is typically done by obtaining an updated third-party appraisal. Given the deterioration in the economy and, specifically, the housing market, updated valuations of the collateral reflect depreciation from earlier assessments. To the extent that an updated valuation of the collateral is insufficient to cover a collateral-dependent loan, the Company reduces the balance of the loan via a charge to the allowance for loan loss.

At March 31, 2012, non-performing construction loans consisted of five loans totaling \$7.2 million for the development of single family homes with collateral ranging from partially completed land to completed leased homes, five loans totaling \$3.8 million secured by land and other real estate, and one loan totaling \$313,000 secured by two complete condominium units. These loans were used for land acquisition and construction in various locations in the States of New Jersey and Pennsylvania. Magyar Bank is determining the proper course of action to collect the principal outstanding on these loans. Year-to-date, the Bank has charged off \$327,000 in construction loan balances through a reduction of its allowance for loan loss.

Construction loans may contain interest reserves on which the interest is capitalized to the loan. At March 31, 2012, there was one performing construction loan with an interest reserve representing an outstanding balance of \$294,000, original interest reserves of \$95,000, advanced interest reserves of \$5,000, and a remaining interest reserve balance of \$90,000. At September 30, 2011, there was one performing construction loan with an interest reserve representing an outstanding balance of \$290,000, an original interest reserve of \$95,000, an advanced interest reserve of \$1,000, and remaining interest reserve balance of \$94,000.

Underwriting for construction loans with and without interest reserves has followed a uniform process. Construction loan progress is monitored on a monthly basis by management as well as by the Board of Directors. Each time an advance is requested, an inspection is made of the project by an outside engineer or appraiser, depending on the size and complexity of the project, to determine the amount of work completed and if the costs to date are supported adequately. The Bank's construction loan operations personnel compare the advance request with the original budget and remaining loan funds available to ensure the project is in balance and that at all times the amount remaining on the loan is sufficient to complete the project.

A number of the Bank's construction loans have been extended due to slower sales as a result of economic conditions. In cases where updated appraisals reflect collateral values insufficient to cover the loan, additional collateral and/or a principal reduction is required to extend the loan. Some of the Bank's loans that originally had interest reserves are non-performing. The Bank does not have any currently NPLs with active interest reserves. Once a loan is deemed impaired, any interest reserve is frozen and the loan is placed on non-accrual so that no future interest income is recorded on these loans. The Bank ceased originating new non-owner occupied construction loans in October 2008.



NPLs secured by one-to four-family residential properties including home equity lines of credit increased \$1.8 million to \$6.6 million at March 31, 2012 from \$4.8 million at September 30, 2011. The loans consisted of two commercial-purpose loans totaling \$2.1 million and fourteen consumer loans totaling \$4.5 million. Included in the totals were three loans totaling \$748,000 that were ninety days delinquent and still accruing interest at March 31, 2012. The Company has not and does not intend to originate or purchase sub-prime loans or option-ARM loans. Fiscal year-to-date, the Bank has charged off \$101,000 in residential loans through a reduction of its allowance for loan loss.

Non-performing commercial real estate loans increased \$746,000 to \$8.3 million at March 31, 2012 from \$7.6 million at September 30, 2011. The ten non-accrual loans were in various stages of foreclosure and collection at March 31, 2012. Fiscal year-to-date, there have been no charge-offs to commercial real estate loans.

Non-performing commercial business loans increased \$17,000 to \$272,000 at March 31, 2012 from \$255,000 at September 30, 2011. The Bank is in the process of collecting the principal outstanding on the two non-accrual loans which will include foreclosure proceedings for those loans secured by real estate. Fiscal year-to-date, the Bank has charged off \$69,000 in non-performing commercial business loans through a reduction of its allowance for loan loss.

The allowance for loan loss increased by \$196,000 during the six months ended March 31, 2012 to \$4.0 million from \$3.8 million at September 30, 2011. The increase in the allowance for loan loss was primarily the result of higher specific reserves, which increased to \$619,000 at March 31, 2012 from \$316,000 at September 30, 2011, offset by a lower general allowance for construction loans. Performing construction loan balances decreased \$5.4 million, or 29.2%, to \$13.2 million during the six months ended March 31, 2012.

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The allowance for loan loss does not typically include a specific reserve for NPLs as all such loans are reported at the lower of amortized cost or fair value, based upon updated independent appraisals of collateral or the discounted value of expected loan repayments. Valuations of such loans are performed at least annually with charge-offs recorded when appraised values, net of estimated selling and disposition costs, are less than the loan balances. Specific reserves may be used on occasions where an updated valuation is unavailable. At March 31, 2012, the Bank held specific reserves totaling \$619,000 for a \$1.7 million non-performing commercial real estate participation loan, for which the Bank was not the lead lender, and two home equity lines of credit to a real estate developer totaling \$1.3 million.

The allowance for loan losses as a percentage of NPLs increased to 15.1% at March 31, 2012 from 13.5% at September 30, 2011. Our allowance for loan losses as a percentage of total loans increased to 1.04% at March 31, 2012 from 0.99% at September 30, 2011. Future increases in the allowance for loan losses may be necessary based on possible future increases in NPLs and charge-offs, possible additional deterioration of collateral values, and the possible continuation or deterioration of the current economic environment.

At March 31, 2012, investment securities totaled \$72.5 million, reflecting an increase of \$2.2 million, or 3.1%, from September 30, 2011. The increase was funded by cash and cash equivalents as well as sales of other real estate owned. Investment securities at March 31, 2012 consisted of \$57.2 million in mortgage-backed securities issued by U.S. government agencies and U.S. government-sponsored enterprises, \$9.5 million in U.S. government-sponsored enterprise debt securities, \$3.0 million in corporate notes, \$2.6 million in "private-label" mortgage-backed securities, and \$41,000 in state municipal bonds. There were no other-than-temporary-impairment charges for the Company's investment securities for the six months ended March 31, 2012.

Other real estate owned decreased \$1.9 million to \$14.7 million at March 31, 2012 from \$16.6 million at September 30, 2011. During the six months ended March 31, 2012, the Bank sold three properties totaling \$3.4 million for a loss of \$42,000 and added five properties totaling \$1.4 million resulting from foreclosure of collateral securing NPLs. The Bank is determining the proper course of action for its other real estate owned, which may include holding the properties until the real estate market improves, selling the properties to a developer and completing partially completed homes for either rental or sale. In addition, the Company has entered into contracts to sell \$4.0 million of the properties held as other real estate owned. No additional losses are expected.

Total deposits decreased \$2.4 million, or 0.6%, to \$422.5 million during the six months ended March 31, 2012. The decrease in deposits occurred in certificates of deposit (including individual retirement accounts), which decreased \$7.8 million, or 4.4%, to \$167.8 million and savings accounts, which decreased \$2.9 million, or 4.8% to \$57.6 million. Offsetting the decrease were increases in interest-bearing checking accounts, which increased \$7.2 million, or 23.1%, to \$38.1 million and in non-interest checking accounts, which increased \$1.5 million, or 2.9%, to \$52.7 million.

Included in total deposits at March 31, 2012 were \$483,000 in Certificate of Deposit Account Registry Service (CDARS) Reciprocal certificates of deposit and \$8.1 million in brokered certificates of deposit. At September 30,

2011, the Company held \$1.8 million in CDARS Reciprocal certificates of deposit and \$10.0 million in brokered certificates of deposit.

Federal Home Loan Bank of New York advances decreased \$2.2 million, or 6.4%, to \$32.7 million while securities sold under agreements to repurchase were unchanged at \$15.0 million at March 31, 2012.

Stockholders' equity increased \$151,000, or 0.3%, to \$44.7 million at March 31, 2012 from \$44.5 million at September 30, 2011. The increase was due to the Company's results from operations, partially offset by changes in the Company's accumulated other comprehensive loss during the six month period.

The Company repurchased 10,700 shares of its common stock at an average price of \$2.94 during the six months ended March 31, 2012,. Through March 31, 2012, the Company had repurchased 77,670 shares at an average price of \$8.51 pursuant to the second stock repurchase plan, which has reduced outstanding shares to 5,806,624.

The Company's book value per share increased to \$7.69 at March 31, 2012 from \$7.67 at September 30, 2011. The increase was the result of the Company's results from operations.

Table of Contents**Average Balance Sheets for the Three and Six Months Ended March 31, 2012 and 2011**

The table on the following page presents certain information regarding the Company's financial condition and net interest income for the three months ended March 31, 2012 and 2011. The table presents the annualized average yield on interest-earning assets and the annualized average cost of interest-bearing liabilities. We derived the yields and costs by dividing annualized income or expense by the average balance of interest-earning assets and interest-bearing liabilities, respectively, for the periods shown. We derived average balances from daily balances over the periods indicated. Interest income includes fees that we consider adjustments to yields.

	For the Three Months Ended March 31, 2012			2011				
	Average Balance	Interest Income/ Expense	Yield/Cost (Annualized)	Average Balance	Interest Income/ Expense	Yield/Cost (Annualized)		
(Dollars In Thousands)								
Interest-earning assets:								
Interest-earning deposits	\$9,814	\$ 7	0.28	% \$9,344	\$ 4	0.18	%	
Loans receivable, net	384,489	4,692	4.89	% 393,798	5,005	5.15	%	
Securities								
Taxable	72,307	514	2.85	% 72,344	529	2.97	%	
Tax-exempt <sup>(1)</sup>	47	1	7.91	% 77	2	8.44	%	
FHLB of NY stock	2,301	29	5.05	% 2,760	40	5.91	%	
Total interest-earning assets	468,958	5,243	4.48	% 478,323	5,580	4.73	%	
Noninterest-earning assets	54,474			53,639				
Total assets	\$523,432			\$531,962				
Interest-bearing liabilities:								
Savings accounts <sup>(2)</sup>	\$58,201	57	0.39	% \$61,667	89	0.58	%	
NOW accounts <sup>(3)</sup>	145,052	162	0.45	% 134,935	256	0.77	%	
Time deposits <sup>(4)</sup>	168,425	797	1.90	% 182,936	933	2.07	%	
Total interest-bearing deposits	371,678	1,016	1.10	% 379,538	1,278	1.37	%	
Borrowings	49,972	497	3.99	% 60,727	597	3.99	%	
Total interest-bearing liabilities	421,650	1,513	1.44	% 440,265	1,875	1.73	%	
Noninterest-bearing liabilities	57,105			48,026				
Total liabilities	478,755			488,291				
Retained earnings	44,677			43,671				
Total liabilities and retained earnings	\$523,432			\$531,962				
Tax-equivalent basis adjustment		—			(1 )			
Net interest income		\$ 3,730			\$ 3,704			
Interest rate spread			3.04	%		3.00	%	
Net interest-earning assets	\$47,308			\$38,058				
Net interest margin <sup>(5)</sup>			3.19	%		3.14	%	
	111.22	%			108.64	%		

Average interest-earning assets to average  
interest-bearing liabilities

- (1) Calculated using 34% tax rate.
- (2) Includes passbook savings, money market passbook and club accounts.
- (3) Includes interest-bearing checking and money market accounts.
- (4) Includes certificates of deposits and individual retirement accounts.
- (5) Calculated as annualized net interest income divided by average total interest-earning assets.

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	For the Six Months Ended March 31, 2012			2011				
	<b>Average Balance</b>	<b>Interest Income/ Expense</b>	<b>Yield/Cost (Annualized)</b>		<b>Average Balance</b>	<b>Interest Income/ Expense</b>	<b>Yield/Cost (Annualized)</b>	
	(Dollars In Thousands)							
<b><u>Interest-earning assets:</u></b>								
Interest-earning deposits	\$12,424	\$ 18	0.30	%	\$14,367	\$ 15	0.21	%
Loans receivable, net	383,268	9,398	4.89	%	395,944	10,152	5.14	%
Securities								
Taxable	72,671	1,042	2.86	%	68,061	1,020	3.00	%
Tax-exempt <sup>(1)</sup>	60	3	4.31	%	87	4	4.40	%
FHLB of NY stock	2,300	53	4.58	%	2,756	87	6.34	%
Total interest-earning assets	470,723	10,514	4.45	%	481,215	11,278	4.70	%
Noninterest-earning assets	54,883				53,526			
Total assets	\$525,606				\$534,741			
<b><u>Interest-bearing liabilities:</u></b>								
Savings accounts <sup>(2)</sup>	\$59,046	\$ 131	0.44	%	\$62,280	\$ 198	0.64	%
NOW accounts <sup>(3)</sup>	143,604	323	0.45	%	137,761	596	0.87	%
Time deposits <sup>(4)</sup>	171,076	1,664	1.94	%	184,049	1,900	2.07	%
Total interest-bearing deposits	373,726	2,118	1.13	%	384,090	2,694	1.41	%
Borrowings	49,943	1,001	4.00	%	60,498	1,207	4.00	%
Total interest-bearing liabilities	423,669	3,119	1.47	%	444,588	3,901	1.76	%
Noninterest-bearing liabilities	56,908				46,257			
Total liabilities	480,577				490,845			
Retained earnings	44,589				43,896			
Total liabilities and retained earnings	\$525,166				\$534,741			
Tax-equivalent basis adjustment		(1 )				(1 )		
Net interest income		\$7,395				\$7,376		
Interest rate spread			2.99	%			2.94	%
Net interest-earning assets	\$47,054				\$36,627			
Net interest margin <sup>(5)</sup>			3.13	%			3.07	%
Average interest-earning assets to average interest-bearing liabilities	111.11 %				108.24 %			

(1) Calculated using 34% tax rate.

(2) Includes passbook savings, money market passbook and club accounts.

(3) Includes interest-bearing checking and money market accounts.

(4) Includes certificates of deposits and individual retirement accounts.

(5) Calculated as annualized net interest income divided by average total interest-earning assets.

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**Comparison of Operating Results for the Three Months Ended March 31, 2012 and 2011**

**Net Income.** Net income increased \$367,000 during the three-month period ended March 31, 2012 compared with the three-month period ended March 31, 2011 due to higher levels of non-interest income and lower non-interest expenses between the two periods. Non-interest income increased \$233,000, or 102.6%, to \$460,000 due to higher gains from the sales of assets. In addition, non-interest expenses decreased \$155,000, or 3.8%, to \$3.9 million due to lower FDIC deposit insurance premiums and compensation expenses.

**Net Interest and Dividend Income.** Net interest and dividend income was unchanged at \$3.7 million for the three months ended March 31, 2012 and 2011. Total interest and dividend income decreased \$336,000 to \$5.2 million for the three month period ended March 31, 2012 while total interest expense decreased \$362,000 to \$1.5 million during the same comparison period. Our net interest margin increased by 5 basis points to 3.19% for the quarter ended March 31, 2012 compared to 3.14% for the quarter ended March 31, 2011. The yield on interest-earning assets fell 25 basis points to 4.48% for the three months ended March 31, 2012 from 4.73% for the three months ended March 31, 2011 primarily due to the lower interest rate environment. The cost of interest-bearing liabilities fell 29 basis points to 1.44% for the three months ended March 31, 2012 from 1.73% for the three months ended March 31, 2011. The decrease in the cost of interest-bearing liabilities was attributable to the lower rate environment and a more favorable funding composition comprised of a larger percentage of lower-cost deposit account balances.

**Interest and Dividend Income.** Interest and dividend income decreased \$336,000, or 6.0%, to \$5.2 million for the three months ended March 31, 2012 from \$5.6 million for the three months ended March 31, 2011. The decrease was attributable to a \$9.4 million, or 2.0%, decrease in the average balance of interest-earning assets and a 25 basis point decrease in the yield on such assets to 4.48% for the three months ended March 31, 2012 compared with the prior year period.

Interest earned on loans decreased \$313,000, or 6.3%, to \$4.7 million for the three months ended March 31, 2012 compared with the prior year period due to a \$9.3 million decrease in the average balance of loans between the periods and a 26 basis point decrease in the average yield on such loans to 4.89% from 5.15%. The decrease in yield between the two periods was due primarily to the lower market interest rate environment.

Interest earned on our investment securities, excluding Federal Home Loan Bank of New York stock, decreased \$12,000, or 2.2%, due to a \$67,000, or 0.1%, decrease in the average balance of such securities to \$72.3 million for the three months ended March 31, 2012. The average yield on investment securities decreased 13 basis points to 2.85% for the three months ended March 31, 2012 from 2.98% for the three months ended March 31, 2011. The decrease in yield on investment securities was due to the lower overall interest rate market.



**Interest Expense.** Interest expense decreased \$362,000, or 19.3%, to \$1.5 million for the three months ended March 31, 2012 from \$1.9 million for the three months ended March 31, 2011. The average balance of interest-bearing liabilities decreased \$18.6 million, or 4.2%, between the two periods, while the cost on such liabilities fell 29 basis points to 1.44% for the quarter ended March 31, 2012 compared with the prior year period.

The average balance of interest bearing deposits decreased \$7.8 million to \$371.7 million from \$379.5 million while the average cost of such deposits decreased 27 basis points to 1.10% from 1.37% in the lower market interest rate environment. As a result, interest paid on deposits decreased \$262,000 to \$1.0 million for the three months ended March 31, 2012 from \$1.3 million for the three months ended March 31, 2011.

Interest paid on advances and securities sold under agreements to repurchase decreased \$100,000, or 16.8%, to \$497,000 for the three months ended March 31, 2012 from \$597,000 for the prior year period due to a decrease in the average balance of such borrowings to \$50.0 million from \$60.7 million. The average cost of advances and securities sold under agreements to repurchase was 3.99% for the three months ended March 31, 2012 and 2011.

**Provision for Loan Losses.** We establish provisions for loan losses, which are charged to earnings, at a level necessary to absorb known and inherent losses that are both probable and reasonably estimable at the date of the financial statements. In evaluating the level of the allowance for loan losses, management considers historical loss experience, the types of loans and the amount of loans in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, peer group information and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available or as future events occur. After an evaluation of these factors, management recorded a provision of \$323,000 for the three months ended March 31, 2012 compared to a provision of \$478,000 for the prior year period. The provision for loan losses decreased during the current period compared with the prior year period due to lower levels of loan charge-offs, lower levels of NPLs and lower balances of performing construction loans, which require higher provisions.

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Net charge-offs were \$163,000 for the three months ended March 31, 2012 compared to \$996,000 for the three months ended March 31, 2011. The level of loan charge-offs decreased from the prior year as a result of lower depreciation of real estate collateral securing non-performing residential and construction loans than in the prior year period and fewer new NPLs. The loan charge-offs during the three months ended March 31, 2012 resulted from write-downs of three impaired loans. Two NPLs secured by land were written down by \$143,000 and one non-performing loan secured by a single family house was written down by \$20,000 based on updated appraisals of the real estate collateralizing the loans.

Determining the amount of the allowance for loan losses necessarily involves a high degree of judgment. Management reviews the level of the allowance on a quarterly basis, and establishes the provision for loan losses based on the factors set forth in the preceding paragraph. As management evaluates the allowance for loan losses, the increased risk associated with larger non-homogenous construction, commercial real estate and commercial business loans may result in larger additions to the allowance for loan losses in future periods.

**Other Income.** Non-interest income increased \$233,000, or 102.6%, to \$460,000 during the three months ended March 31, 2012 compared to \$227,000 for the three months ended March 31, 2011. The increase was attributable to higher gains on the sales of assets. The Company recorded gains totaling \$143,000 from the sale of loans during the three months ended March 31, 2012, which increased \$133,000 from the prior year period. Gains on the sale of available-for-sale investment securities increased \$29,000 to \$64,000 for the three months ended March 31, 2012 from the prior year period. Losses on the sale of other real estate owned decreased \$70,000 to a loss of \$87,000 for the three months ended March 31, 2011 from a loss of \$157,000 for the prior year period. The loss of \$87,000 for the current year period resulted from a \$77,000 provision for loss against one property, based on an updated appraisal, and a \$10,000 loss on the sale of a property previously carried in OREO for \$212,000.

**Other Expenses.** During the three months ended March 31, 2012, non-interest expenses decreased \$155,000 to \$3.9 million from \$4.1 million for the three months ended March 31, 2011 primarily due to lower Federal Deposit Insurance Corporation deposit insurance premiums paid, which decreased \$176,000, or 49.3%. Compensation and benefit expenses decreased \$116,000, or 5.8%, due to lower stock-based compensation and employee medical benefit expense. Partially offsetting the decreases were higher other real estate owned expenses, which increased \$60,000, or 53.1%, professional fees, which increased \$29,000, or 9.6%, and other expenses, which increased \$52,000, or 13.3%.

**Income Tax Benefit.** The Company recorded a tax benefit of \$42,000 for the three months ended March 31, 2012, compared to a tax benefit of \$244,000 for the three months ended March 31, 2011.

**Comparison of Operating Results for the Six Months Ended March 31, 2012 and 2011**

**Net Income (Loss).** Net income increased \$270,000, or 117.4%, to \$40,000 during the six-month period ended March 31, 2012 compared a net loss of \$230,000 for the six-month period ended March 31, 2011 due primarily to lower non-interest expenses and provisions for loan loss. Net interest and dividend income was unchanged at \$7.4 million while non-interest income increased \$13,000 between periods.

**Net Interest and Dividend Income.** Net interest and dividend income was unchanged at \$7.4 million for the six months ended March 31, 2012 and 2011. Total interest and dividend income decreased \$763,000, or 6.8%, to \$10.5 million for the six month period ended March 31, 2012 compare \$11.3 million for the six month period ended March 31, 2011. Total interest expense decreased \$782,000, or 20.0%, to \$3.1 million for the six month ended March 31, 2012 from \$3.9 million for the same six month period in 2011.

The net interest margin increased by 6 basis points to 3.13% for the six months ended March 31, 2012 compared to 3.07% for the six months ended March 31, 2011. The yield on interest-earning assets fell 25 basis points to 4.45% for the six months ended March 31, 2012 from 4.70% for the six months ended March 31, 2011 primarily due to the lower market interest rate environment. The cost of interest-bearing liabilities fell 29 basis points to 1.47% for the six months ended March 31, 2012 from 1.76% for the six months ended March 31, 2011. The decrease in the cost of interest-bearing liabilities was attributable to the lower market interest rate environment and a more favorable funding composition comprised of a larger percentage of lower-cost deposit account balances.

**Interest and Dividend Income.** The net interest and dividend income increased \$19,000, or 0.3%, and was \$7.4 million during both the six month periods ended March 31, 2012 and 2011.

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Interest earned on loans decreased \$754,000, or 7.4%, to \$9.4 million for the six months ended March 31, 2012 from \$10.2 million for the prior year period due to a \$12.7 million decrease in the average balance of loans between periods and a 25 basis point decrease in the average yield on such loans to 4.89% from 5.14%. The decrease in yield between the two periods was due primarily to the lower market interest rate environment.

Interest earned on our investment securities, excluding Federal Home Loan Bank of New York stock, increased \$25,000, or 2.4%, due to a \$4.6 million, or 6.7%, increase in the average balance of such securities to \$72.7 million for the six months ended March 31, 2012 from \$68.1 million for the six months ended March 31, 2011. The average yield on investment securities decreased 6 basis of point to 1.44% for the six months ended March 31, 2012 from 1.5% for the six months ended March 31, 2011.

**Interest Expense.** Interest expense decreased \$782,000, or 20.0%, to \$3.1 million for the six months ended March 31, 2012 from \$3.9 million for the six months ended March 31, 2011. The decrease in interest expense was primarily due to the average balance of interest-bearing liabilities decreased \$20.9 million, or 4.7%, to \$423.7 million from \$444.6 million, and a 29 basis points decrease in the average cost of such liabilities to 1.47% from 1.76% for the six month ended March 31, 2012 and 2011, respectively.

The average balance of interest bearing deposits decreased \$10.4 million to \$373.7 million for the six months ended March 31, 2012 from \$384.1 million for the same period last year while the average cost of such deposits decreased 27 basis points to 1.13% from 1.41%. This resulted in a \$577,000 decrease in interest paid on deposits to \$2.1 million for the six months ended March 31, 2012 from \$2.7 million for the six months ended March 31, 2011.

Interest paid on advances and securities sold under agreements to repurchase decreased \$206,000, or 17.1%, to \$1.0 million for the six months ended March 31, 2012 compared to \$1.2 million for the prior year period. The decrease in interest expense was due to a decrease in average balance to \$49.9 million from \$60.5 million. The average cost of advances and securities sold under agreements to repurchase was 4.00% for the six months ended March 31, 2012 and 2011.

**Provision for Loan Losses.** We establish provisions for loan losses, which are charged to earnings, at a level necessary to absorb known and inherent losses that are both probable and reasonably estimable at the date of the financial statements. In evaluating the level of the allowance for loan losses, management considers historical loss experience, the types of loans and the amount of loans in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, peer group information and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available or as future events occur. After an evaluation of these factors, management recorded a provision of \$693,000 for the six months ended March 31, 2012 compared to \$836,000 for the six months ended March 31, 2011. The decrease in the provision for loan loss was due primarily to the stabilization of NPLs, lower levels of loan charge-offs and lower levels of outstanding construction loans, which require higher

provisions.

Net charge-offs were \$497,000 for the six months ended March 31, 2012 compared to \$1.8 million for the six months ended March 31, 2011. The loan charge-offs resulted primarily from additional write-downs of loans previously deemed impaired. The level of loan charge-offs decreased from the prior year as a result of lower depreciation of real estate collateral securing non-performing residential and construction loans than in the prior year period. Five non-performing construction loans totaling \$5.5 million were written down by \$327,000 for the six months based on updated appraisals of the real estate securing the loans, reflecting continued depreciation from one year earlier. Of these five loans, one loan carried for \$3.3 million at September 30, 2011 was paid off and two totaling \$639,900 at September 30, 2011 were transferred to other real estate owned. In addition, the Company wrote down a \$657,000 commercial business loan by \$69,000 and two residential mortgage loans and home equity lines of credit totaling \$538,000 by \$101,000 during the six months ended March 31, 2012.

**Other Income.** Non-interest income increased \$13,000, or 1.3%, to \$1.0 million for the six months ended March 31, 2012 compared to \$994,000 for the six months ended March 31, 2011. The increase was attributable to higher net gains on the sales of assets, offset by lower service charges. Gains on the sale of available-for-sale investment securities increased \$113,000 to \$148,000 for the six months ended March 31, 2012 from \$35,000 for the six months ended March 31, 2011. The Company recorded a loss of \$119,000 for other real estate owned for the six months ended March 31, 2012, which decreased \$173,000 from a loss of \$292,000 for the six months ended March 31, 2011. Partially offsetting the higher net gains were lower gains from the sales of loans, which decreased \$199,000 to \$260,000 for the six months ended March 31, 2012 compared with \$459,000 for the six months ended March 31, 2011. Service charges decreased \$74,000 due to lower loan prepayment penalties received during the six months ended March 31, 2012 compared with the prior year period.

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**Other Expenses.** Non-interest expenses decreased \$268,000 to \$7.7 million during the six months ended March 31, 2012 from \$8.0 million for the six months ended March 31, 2011 primarily due to lower Federal Deposit Insurance Corporation deposit insurance premiums paid, which decreased \$349,000, or 49.4%. Compensation and benefit expenses decreased \$131,000, or 3.4%, due to lower stock-based compensation and employee medical benefit expense.

Partially offsetting the decreases were higher other real estate owned expenses, which increased \$163,000, or 69.1%, and occupancy expenses, which increased \$79,000, or 5.7%. The increase in occupancy expenses was due to the opening of the Bank's Bridgewater branch office in July 2011.

**Income Tax Expense (Benefit).** The Company recorded a tax benefit of \$35,000 for the six months ended March 31, 2012, compared to a benefit of \$208,000 for the six months ended March 31, 2011.

Where applicable, deferred tax assets are reduced by a valuation allowance for any portions determined not likely to be realized. The valuation allowance is assessed by management on a quarterly basis and adjusted, by a charge or credit to income tax expense, as changes in facts and circumstances warrant. In assessing whether it is more likely than not that some portion or all of the deferred tax assets will not be realized, management considers projections of future taxable income, the projected periods in which current temporary differences will be deductible, the availability of carry forwards, and existing tax laws and regulations. The valuation allowance in place on deferred tax assets at March 31, 2012, did not materially change from that in place on September 30, 2011.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Liquidity**

The Company's liquidity is a measure of its ability to fund loans, pay withdrawals of deposits, and other cash outflows in an efficient, cost-effective manner. The Company's short-term sources of liquidity include maturity, repayment and sales of assets, excess cash and cash equivalents, new deposits, other borrowings, and new advances from the Federal Home Loan Bank. There has been no material adverse change during the six months ended March 31, 2012 in the ability of the Company and its subsidiaries to fund their operations.

At March 31, 2012, the Company had commitments outstanding under letters of credit of \$1.5 million, commitments to originate loans of \$19.7 million, and commitments to fund undisbursed balances of closed loans and unused lines of credit of \$37.8 million. There has been no material change during the six months ended March 31, 2012 in any of the

Company's other contractual obligations or commitments to make future payments.

### **Capital Requirements**

On April 22, 2010, Magyar Bank entered into agreements with the Federal Deposit Insurance Corporation ("FDIC"), its principal federal banking regulator, and the New Jersey Department of Banking and Insurance (the "Department"), which require the Bank to take certain measures to improve its safety and soundness. In connection with these agreements, the Bank stipulated to the issuance by the FDIC and the Department of consent orders against the Bank (the "Consent Orders") relating to certain findings from a recent examination of the Bank. The Consent Orders were filed with the Securities and Exchange Commission on Form 8-K as Exhibits 10.1 and 10.2 on April 23, 2010.

Among the corrective actions required were for the Bank to develop, within 30 days of the April 22, 2010 effective date of the Consent Orders, a written capital plan that details the manner in which the Bank will achieve a Tier 1 capital as a percentage of the Bank's total assets of at least 8%, and total qualifying capital as a percentage of risk-weighted assets of at least 12%. The Bank developed and filed a capital plan on a timely basis with the FDIC and the Department and the plan remains under review by those regulatory authorities.

On March 2, 2012 the Bank was informed in writing by the FDIC and the Department that the Consent Order entered into with the FDIC and the Department in April 2010 had been terminated. The FDIC and the Department cited to the substantial compliance with the Order by the Bank as the reason for the termination of the Order. The Order was replaced by a Memorandum of Understanding that requires the Bank to maintain the same minimum capital ratios as previously required by the Order.

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At March 31, 2012, the Bank's Tier 1 capital as a percentage of the Bank's total assets was 8.16%, and total qualifying capital as a percentage of risk-weighted assets was 13.48%.

Item 3 – Quantitative and Qualitative Disclosures about Market Risk

Not applicable to smaller reporting companies.

Item 4 – Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that Magyar Bancorp, Inc. files or submits under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms.

There has been no change in the Company's internal control over financial reporting during its six months ended March 31, 2012 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.



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PART II - OTHER INFORMATION

Item 1. Legal proceedings

On December 14, 2011, Elizabeth E. Hance, the former President and Chief Executive Officer of the Company and the Bank, filed a lawsuit against the Company and its directors in the Superior Court of New Jersey, Middlesex County. The lawsuit alleges, among other things, breach of contract and employment discrimination in connection with Ms. Hance's December 2009 separation from employment and seeks severance that she claims she was entitled to, as well as other compensatory and punitive damages. The Company believes that the failure to pay Ms. Hance severance was the result of applicable regulatory prohibitions, and intends to defend the suit vigorously.

Item 1A. Risk Factors

Not applicable to smaller reporting companies.

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

a.) Not applicable.

b.) Not applicable.

c.) The Company repurchased 10,700 shares at the average price of \$2.94 during the six months ended March 31, 2012. The following table presents a summary of the Company's shares repurchased at the period ended March 31, 2012:

Total Number of Shares	Average	Remaining Number of Shares That
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Period	Purchased	Price Paid Per Share	May be Purchased Under the Plan (1)
January 1 - January 31, 2012	—	\$ —	54,854
February 1 - February 29, 2012	2,600	4.04	52,254
March 1 - March 31, 2012	—	—	52,254
	2,600	\$ 4.04	

(1) The Company completed its first stock repurchase program of 130,927 shares in November 2007. The Company announced a second repurchase program of 129,924 shares in November 2007, under which 77,670 shares had been repurchased as of March 31, 2012 at an average price of \$8.51.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

a.) Not applicable.

b.) None.

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Item 6. Exhibits

Exhibits

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Signatures

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

MAGYAR BANCORP, INC.  
(Registrant)

Date: May 14, 2012 /s/ John S. Fitzgerald  
John S. Fitzgerald  
President and Chief Executive Officer

Date: May 14, 2012 /s/ Jon R. Ansari  
Jon R. Ansari  
Senior Vice President and Chief Financial Officer