

GUARANTY FEDERAL BANCSHARES INC  
Form 10-Q  
August 10, 2017  
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

**FORM 10-Q**

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-23325

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**Guaranty Federal Bancshares, Inc.**  
(Exact name of registrant as specified in its charter)

**Delaware** **43-1792717**  
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

**1341 West Battlefield**  
**Springfield, Missouri** **65807**  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (417) 520-4333

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definitions of "large accelerated filer", "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company  Emerging growth company

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

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

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

<u>Class</u>	<u>Outstanding as of August 8, 2017</u>
Common Stock, Par Value \$0.10 per share	4,421,775 Shares

**GUARANTY FEDERAL BANCSHARES, INC.**

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**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****GUARANTY FEDERAL BANCSHARES, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****JUNE 30, 2017 (UNAUDITED) AND DECEMBER 31, 2016**

	<b>6/30/17</b>	<b>12/31/16</b>
<b>ASSETS</b>		
Cash and due from banks	\$3,531,188	\$3,769,478
Interest-bearing deposits in other financial institutions	7,216,159	5,318,963
Cash and cash equivalents	10,747,347	9,088,441
Available-for-sale securities	85,006,043	92,399,235
Held-to-maturity securities	20,954	27,528
Stock in Federal Home Loan Bank, at cost	4,577,500	4,611,000
Mortgage loans held for sale	1,903,062	2,183,633
Loans receivable, net of allowance for loan losses of June 30, 2017 - \$6,640,164 - December 31, 2016 - \$5,742,449	608,159,460	538,273,640
Accrued interest receivable	2,060,646	1,947,063
Prepaid expenses and other assets	3,487,669	2,961,336
Foreclosed assets held for sale	1,302,012	2,682,353
Premises and equipment, net	11,717,390	10,871,039
Bank owned life insurance	19,505,622	19,272,893
Deferred and income taxes receivable	3,231,501	3,661,658
	<b>\$751,719,206</b>	<b>\$687,979,819</b>

**LIABILITIES AND STOCKHOLDERS' EQUITY****LIABILITIES**

Deposits	\$567,013,636	\$505,362,750
Federal Home Loan Bank advances	93,800,000	95,700,000
Subordinated debentures	15,465,000	15,465,000
Advances from borrowers for taxes and insurance	374,878	192,460
Accrued expenses and other liabilities	1,528,647	1,077,396
Accrued interest payable	213,907	207,833
	<b>678,396,068</b>	<b>618,005,439</b>

**COMMITMENTS AND CONTINGENCIES**

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**STOCKHOLDERS' EQUITY**

Capital Stock:

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Common stock, \$0.10 par value; authorized 10,000,000 shares; issued June 30, 2017 and December 31, 2016 - 6,875,503 shares	687,550	687,550
Additional paid-in capital	50,569,054	50,552,077
Retained earnings, substantially restricted	59,484,791	57,347,282
Accumulated other comprehensive loss	(292,716 )	(1,309,241 )
	110,448,679	107,277,668
Treasury stock, at cost; June 30, 2017 and December 31, 2016 - 2,453,728 and 2,465,476 shares, respectively	(37,125,541 )	(37,303,288 )
	73,323,138	69,974,380
	\$751,719,206	\$687,979,819

See Notes to Condensed Consolidated Financial Statements.

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**GUARANTY FEDERAL BANCSHARES, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****THREE MONTHS AND SIX MONTHS ENDED JUNE 30, 2017 AND 2016 (UNAUDITED)**

	Three months ended		Six months ended	
	6/30/2017	6/30/2016	6/30/2017	6/30/2016
<b>Interest Income</b>				
Loans	\$6,743,613	\$5,628,133	\$12,990,123	\$11,330,025
Investment securities	454,040	525,713	929,509	983,564
Other	43,855	50,468	93,278	95,770
	7,241,508	6,204,314	14,012,910	12,409,359
<b>Interest Expense</b>				
Deposits	746,701	570,194	1,368,555	1,155,011
FHLB and Federal Reserve advances	449,698	313,108	849,625	614,272
Subordinated debentures	155,910	143,480	307,590	282,910
	1,352,309	1,026,782	2,525,770	2,052,193
<b>Net Interest Income</b>	5,889,199	5,177,532	11,487,140	10,357,166
<b>Provision for Loan Losses</b>	575,000	375,000	1,050,000	750,000
<b>Net Interest Income After Provision for Loan Losses</b>	5,314,199	4,802,532	10,437,140	9,607,166
<b>Noninterest Income</b>				
Service charges	290,926	279,099	558,032	545,068
Gain on sale of investment securities	62,274	60,375	62,274	111,405
Gain on sale of mortgage loans held for sale	523,534	382,583	932,148	732,457
Gain on sale of Small Business Administration loans	124,857	82,686	255,345	152,238
Net gain (loss) on foreclosed assets	(29,809 )	(8,797 )	8,264	(19,505 )
Other income	395,278	383,467	780,362	766,572
	1,367,060	1,179,413	2,596,425	2,288,235
<b>Noninterest Expense</b>				
Salaries and employee benefits	2,934,648	2,705,866	5,792,419	5,256,798
Occupancy	485,154	433,124	971,383	877,825
FDIC deposit insurance premiums	59,377	127,864	112,489	244,714
Data processing	232,436	211,535	461,752	426,665
Advertising	131,250	131,250	262,500	262,500
Other expense	725,051	699,755	1,386,993	1,350,368
	4,567,916	4,309,394	8,987,536	8,418,870
<b>Income Before Income Taxes</b>	2,113,343	1,672,551	4,046,029	3,476,531
<b>Provision for Income Taxes</b>	520,770	416,399	1,024,215	943,774
<b>Net Income Available to Common Shareholders</b>	\$1,592,573	\$1,256,152	\$3,021,814	\$2,532,757
<b>Basic Income Per Common Share</b>	\$0.36	\$0.29	\$0.69	\$0.58
<b>Diluted Income Per Common Share</b>	\$0.36	\$0.28	\$0.68	\$0.57

See Notes to Condensed Consolidated Financial Statements.



**GUARANTY FEDERAL BANCSHARES, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****THREE MONTHS AND SIX MONTHS ENDED JUNE 30, 2017 AND 2016 (UNAUDITED)**

	Three months ended		Six months ended	
	6/30/2017	6/30/2016	6/30/2017	6/30/2016
<b>NET INCOME</b>	\$1,592,573	\$1,256,152	\$3,021,814	\$2,532,757
<b>OTHER ITEMS OF COMPREHENSIVE INCOME:</b>				
Change in unrealized gain on investment securities available-for-sale, before income taxes	812,311	1,588,158	1,448,165	2,447,064
Change in unrealized gain on interest rate swaps, before income taxes	227,642	-	227,642	-
Less: Reclassification adjustment for realized gains on investment securities included in net income, before income taxes	(62,274 )	(60,375 )	(62,274 )	(111,405 )
Total other items of comprehensive income	977,679	1,527,783	1,613,533	2,335,659
Income tax expense related to other items of comprehensive income	361,742	565,280	597,008	864,193
Other comprehensive income	615,937	962,503	1,016,525	1,471,466
<b>TOTAL COMPREHENSIVE INCOME</b>	<b>\$2,208,510</b>	<b>\$2,218,655</b>	<b>\$4,038,339</b>	<b>\$4,004,223</b>

See Notes to Condensed Consolidated Financial Statements.

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**GUARANTY FEDERAL BANCSHARES, INC.****CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY****SIX MONTHS ENDED JUNE 30, 2017 (UNAUDITED)**

	Common Stock	Additional Paid- In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
<b>Balance, January 1, 2017</b>	\$687,550	\$50,552,077	\$(37,303,288)	\$57,347,282	\$(1,309,241 )	\$69,974,380
Net income	-	-	-	3,021,814	-	3,021,814
Change in unrealized gain on available-for-sale securities and effect of interest rate swaps, net of income taxes					1,016,525	1,016,525
Dividends on common stock (\$0.20 per share)	-	-	-	(884,305 )	-	(884,305 )
Stock award plans	-	16,977	177,747	-	-	194,724
<b>Balance, June 30, 2017</b>	\$687,550	\$50,569,054	\$(37,125,541)	\$59,484,791	\$(292,716 )	\$73,323,138

See Notes to Condensed Consolidated Financial Statements.

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**GUARANTY FEDERAL BANCSHARES, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****SIX MONTHS ENDED JUNE 30, 2017 AND 2016 (UNAUDITED)**

	<b>6/30/2017</b>	<b>6/30/2016</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$3,021,814	\$2,532,757
Items not requiring (providing) cash:		
Deferred income taxes	(786,131 )	(124,379 )
Depreciation	465,587	401,932
Provision for loan losses	1,050,000	750,000
Gain on sale of mortgage loans held for sale and investment securities	(994,422 )	(843,862 )
Gain on sale of foreclosed assets	(60,132 )	-
Gain on sale of Small Business Administration Loans	(255,345 )	(152,238 )
Amortization of deferred income, premiums and discounts	398,523	281,861
Stock award plan expense	194,724	213,260
Origination of loans held for sale	(30,824,846 )	(28,598,708 )
Proceeds from sale of loans held for sale	32,037,565	29,256,415
Increase in cash surrender value of bank owned life insurance	(232,729 )	(245,382 )
Changes in:		
Accrued interest receivable	(113,583 )	106,091
Prepaid expenses and other assets	(302,583 )	(51,540 )
Accounts payable and accrued expenses	456,151	(54,158 )
Income taxes receivable	619,280	459,404
Net cash provided by operating activities	4,673,873	3,931,453
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of loans receivable	-	(11,132,508 )
Proceeds on sale of loans	19,683,510	-
Net change in loans	(90,700,542 )	(17,629,540 )
Principal payments on available-for-sale securities	3,655,127	3,909,170
Principal payments on held-to-maturity securities	6,573	9,241
Proceeds from calls/maturities of available-for-sale securities	-	535,000
Purchase of premises and equipment	(1,311,938 )	(679,031 )
Purchase of available-for-sale securities	(5,568,959 )	(64,776,154 )
Proceeds from sale of available-for-sale securities	10,717,148	54,920,025
Redemption (purchase) of Federal Home Loan Bank stock	33,500	(1,081,500 )
Purchase of tax credit investments	(223,750 )	-
Proceeds from sale of foreclosed assets held for sale	1,644,191	108,592
Net cash used in investing activities	(62,065,140 )	(35,816,705 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Cash dividends paid on common stock	(883,131 )	(705,921 )
Net increase in demand deposits, NOW accounts and savings accounts	38,682,025	781,901
Net increase (decrease) in certificates of deposit	22,968,861	(3,753,036 )
Proceeds from Federal Home Loan Bank advances	149,500,000	116,350,000

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Repayments of Federal Home Loan Bank and Federal Reserve advances	(151,400,000)	(90,050,000 )
Advances from borrowers for taxes and insurance	182,418	200,869
Stock options exercised	-	85,800
Net cash provided by financing activities	59,050,173	22,909,613
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>1,658,906</b>	<b>(8,975,639 )</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<b>9,088,441</b>	<b>18,774,419</b>
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<b>\$10,747,347</b>	<b>\$9,798,780</b>

See Notes to Condensed Consolidated Financial Statements.

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## **NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

### **Note 1: Basis of Presentation**

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included.

These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Guaranty Federal Bancshares, Inc.'s (the "Company") Annual Report on Form 10-K for the year ended December 31, 2016 ("2016 Annual Report") filed with the Securities and Exchange Commission (the "SEC"). The results of operations for the periods are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet of the Company as of December 31, 2016, has been derived from the audited consolidated balance sheet of the Company as of that date. Certain information and note disclosures normally included in the Company's annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted.

### **Note 2: Principles of Consolidation**

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Guaranty Bank (the "Bank"). All significant intercompany transactions and balances have been eliminated in consolidation.

### **Note 3: Securities**

The amortized cost and approximate fair values of securities classified as available-for-sale were as follows:

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	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
<b>As of June 30, 2017</b>				
Debt Securities:				
Municipals	35,989,090	235,378	(368,313 )	35,856,155
Corporates	3,000,000	55,000	-	3,055,000
Government sponsored mortgage-backed securities and SBA loan pools	46,709,113	22,669	(636,894 )	46,094,888
	\$85,698,203	\$ 313,047	\$(1,005,207)	\$85,006,043

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
<b>As of December 31, 2016</b>				
Debt Securities:				
Municipals	\$ 39,357,506	\$ 65,673	\$ (1,085,654)	\$ 38,337,525
Corporates	7,003,986	54,050	(4,514 )	7,053,522
Government sponsored mortgage-backed securities and SBA loan pools	48,115,793	19,432	(1,127,037)	47,008,188
	\$ 94,477,285	\$ 139,155	\$ (2,217,205)	\$ 92,399,235

Maturities of available-for-sale debt securities as of June 30, 2017:

	Amortized Cost	Approximate Fair Value
1-5 years	2,846,819	2,890,286
6-10 years	15,422,023	15,486,199
After 10 years	20,720,248	20,534,670
Government sponsored mortgage-backed securities and SBA loan pools not due on a single maturity date	46,709,113	46,094,888
	\$ 85,698,203	\$ 85,006,043

The amortized cost and approximate fair values of securities classified as held to maturity are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
<b>As of June 30, 2017</b>				
Debt Securities:				
Government sponsored mortgage-backed securities	\$ 20,954	\$ 568	\$ (17 )	\$ 21,505

Amortized	Gross	Gross	Approximate
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	Cost	Unrealized Gains	Unrealized (Losses)	Fair Value
<b>As of December 31, 2016</b>				
Debt Securities:				
Government sponsored mortgage-backed securities	\$ 27,528	\$ 625	\$ -	\$ 28,153

Maturities of held-to-maturity securities as of June 30, 2017:

	Amortized	Approximate
	Cost	Fair Value
Government sponsored mortgage-backed securities not due on a single maturity date	\$ 20,954	\$ 21,505

The book value of securities pledged as collateral, to secure public deposits and for other purposes, amounted to \$62,989,893 and \$48,723,259 as of June 30, 2017 and December 31, 2016, respectively. The approximate fair value of pledged securities amounted to \$62,398,478 and \$47,617,900 as of June 30, 2017 and December 31, 2016, respectively.

Realized gains and losses are recorded as net securities gains. Gains on sales of securities are determined on the specific identification method. Gross gains of \$62,274 and \$111,405 as of June 30, 2017 and June 30, 2016, respectively, were realized from the sale of available-for-sale securities. The tax effect of these net gains was \$23,041 and \$41,220 as of June 30, 2017 and June 30, 2016, respectively.

The Company evaluates all securities quarterly to determine if any unrealized losses are deemed to be other than temporary. Certain investment securities are valued at less than their historical cost. These declines are primarily the result of the rate for these investments yielding less than current market rates, or declines in stock prices of equity securities. Based on evaluation of available evidence, management believes the declines in fair value for these securities are temporary. It is management's intent to hold the debt securities to maturity or until recovery of the unrealized loss. Should the impairment of any of these debt securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified, to the extent the loss is related to credit issues, and to other comprehensive income to the extent the decline on debt securities is related to other factors and the Company does not intend to sell the security prior to recovery of the unrealized loss.

Certain other investments in debt and equity securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at June 30, 2017 and December 31, 2016, was \$62,887,238 and \$79,361,229, respectively, which is approximately 74% and 86% of the Company's investment portfolio.

The following table shows gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at June 30, 2017 and December 31, 2016.



June 30, 2017

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	Municipals	19,268,849	(306,515 )	1,572,882	(61,798 )	20,841,731
Government sponsored mortgage-backed securities and SBA loan pools	36,305,898	(512,187 )	5,739,609	(124,724 )	42,045,507	(636,911 )
	\$55,574,747	\$(818,702 )	\$7,312,491	\$(186,522 )	\$62,887,238	\$(1,005,224)

December 31, 2016

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	Municipals	\$33,084,816	\$(1,082,021)	\$179,402	\$(3,633)	\$33,264,218
Corporates	1,996,172	(3,828)	881,100	(686)	2,877,272	(4,514)
Government sponsored mortgage-backed securities and SBA loan pools	39,570,463	(1,022,511)	3,649,276	(104,526)	43,219,739	(1,127,037)
	\$74,651,451	\$(2,108,360)	\$4,709,778	\$(108,845)	\$79,361,229	\$(2,217,205)

**Note 4: Loans and Allowance for Loan Losses**

Categories of loans at June 30, 2017 and December 31, 2016 include:

	June 30, 2017	December 31, 2016
Real estate - residential mortgage:		
One to four family units	\$106,372,711	\$106,410,559
Multi-family	76,025,304	48,483,523
Real estate - construction	56,812,066	40,912,307
Real estate - commercial	263,215,296	249,580,873
Commercial loans	87,030,844	75,404,732
Consumer and other loans	25,858,453	23,606,306
Total loans	615,314,674	544,398,300
Less:		
Allowance for loan losses	(6,640,164)	(5,742,449)
Deferred loan fees/costs, net	(515,050)	(382,211)
Net loans	\$608,159,460	\$538,273,640

Classes of loans by aging at June 30, 2017 and December 31, 2016 were as follows:

**As of June 30, 2017**

30-59 Days	60-89 Days	90 Days	Total Past	Current	Total Loans	Total Loans
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	Past Due	Past Due	and more	Due		Receivable	> 90 Days
			Past Due				and Accruing
<i>(In Thousands)</i>							
Real estate - residential mortgage:							
One to four family units	\$1,153	\$422	\$193	\$1,768	\$104,605	\$106,373	\$ -
Multi-family	351	-	-	351	75,674	76,025	-
Real estate - construction	\$7,440	-	-	7,440	49,372	56,812	-
Real estate - commercial	161	-	666	827	262,388	263,215	-
Commercial loans	601	-	1,278	1,879	85,152	87,031	-
Consumer and other loans	-	-	7	7	25,852	25,859	-
Total	\$9,706	\$422	\$2,144	\$12,272	\$603,043	\$615,315	\$ -

**As of December 31, 2016**

	30-59 Days	60-89 Days	90 Days and more Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 Days and Accruing
<i>(In Thousands)</i>							
Real estate - residential mortgage:							
One to four family units	\$367	\$495	\$103	\$965	\$105,446	\$106,411	\$-
Multi-family	-	-	-	-	48,483	48,483	-
Real estate - construction	-	-	-	-	40,912	40,912	-
Real estate - commercial	-	-	-	-	249,581	249,581	-
Commercial loans	-	-	593	593	74,812	75,405	-
Consumer and other loans	-	-	38	38	23,568	23,606	-
<b>Total</b>	<b>\$367</b>	<b>\$495</b>	<b>\$734</b>	<b>\$1,596</b>	<b>\$542,802</b>	<b>\$544,398</b>	<b>\$-</b>

Nonaccruing loans are summarized as follows:

	June 30, 2017	December 31, 2016
Real estate - residential mortgage:		
One to four family units	\$1,847,293	\$2,060,180
Multi-family	-	-
Real estate - construction	5,364,771	5,446,896
Real estate - commercial	827,272	161,491
Commercial loans	1,670,686	925,281
Consumer and other loans	6,400	37,791
<b>Total</b>	<b>\$9,716,422</b>	<b>\$8,631,639</b>

The following tables present the activity in the allowance for loan losses based on portfolio segment for the three and six months ended June 30, 2017 and 2016:

<b>Three months ended</b>	Construction	Commercial Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
<b>June 30, 2017</b>								
<i>(In Thousands)</i>								
<b>Allowance for loan losses:</b>								
Balance, beginning of period	\$1,299	\$1,742	\$818	\$273	\$883	\$282	\$875	\$6,172

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Provision charged to expense	142	119	51	50	99	88	26	\$575
Losses charged off	-	-	-	-	(85 )	(53 )	-	\$(138 )
Recoveries	21	-	2	-	2	6	-	\$31
Balance, end of period	\$1,462	\$ 1,861	\$ 871	\$ 323	\$ 899	\$ 323	\$ 901	\$6,640

Six months ended June 30, 2017	Commercial Construction Real Estate		One to four family	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	<i>(In Thousands)</i>							
Balance, beginning of period	\$1,377	\$ 1,687	\$ 856	\$ 206	\$ 1,168	\$ 337	\$ 111	\$5,742
Provision charged to expense	46	174	18	117	(188 )	93	790	\$1,050
Losses charged off	-	-	(11 )	-	(85 )	(123 )	-	\$(219 )
Recoveries	39	-	8	-	4	16	-	\$67
Balance, end of period	\$1,462	\$ 1,861	\$ 871	\$ 323	\$ 899	\$ 323	\$ 901	\$6,640

<b>Three months ended</b>	Commercial		One			Consumer		
<b>June 30, 2016</b>	Construction	Real Estate	to four family	Multi-family	Commercial	and Other	Unallocated	Total
<b>Allowance for loan losses:</b>								
<i>(In Thousands)</i>								
Balance, beginning of period	\$ 1,868	\$ 1,486	\$ 826	\$ 159	\$ 1,503	\$ 270	\$ 73	\$ 6,185
Provision charged to expense	19	101	77	(2 )	21	5	154	\$ 375
Losses charged off	(252 )	-	(47 )	-	(159 )	(45 )	-	\$(503 )
Recoveries	33	26	6	-	1	58	-	\$ 124
Balance, end of period	\$ 1,668	\$ 1,613	\$ 862	\$ 157	\$ 1,366	\$ 288	\$ 227	\$ 6,181

<b>Six months ended</b>	Commercial		One			Consumer		
<b>June 30, 2016</b>	Construction	Real Estate	to four family	Multi-family	Commercial	and Other	Unallocated	Total
<b>Allowance for loan losses:</b>								
<i>(In Thousands)</i>								
Balance, beginning of period	\$ 1,246	\$ 1,526	\$ 821	\$ 177	\$ 1,382	\$ 223	\$ 437	\$ 5,812
Provision charged to expense	640	55	74	(20 )	142	69	(210 )	\$ 750
Losses charged off	(252 )	-	(47 )	-	(159 )	(74 )	-	\$(532 )
Recoveries	34	32	14	-	1	70	-	\$ 151
Balance, end of period	\$ 1,668	\$ 1,613	\$ 862	\$ 157	\$ 1,366	\$ 288	\$ 227	\$ 6,181

The following tables present the recorded investment in loans based on portfolio segment and impairment method as of June 30, 2017 and December 31, 2016:

<b>As of June 30, 2016</b>	Commercial		One			Consumer		
	Construction	Real Estate	to four family	Multi-family	Commercial	and Other	Unallocated	Total
<b>Allowance for loan losses:</b>								
<i>(In Thousands)</i>								
Ending balance: individually evaluated for impairment	\$ 277	\$ 93	\$ 65	\$ -	\$ 327	\$ 12	\$ -	\$ 774

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Ending balance: collectively evaluated for impairment	\$ 1,185	\$ 1,768	\$ 806	\$ 323	\$ 572	\$ 311	\$ 901	\$ 5,866
<b>Loans:</b>								
Ending balance: individually evaluated for impairment	\$ 5,364	\$ 328	\$ 1,848	\$ -	\$ 975	\$ 64	\$ -	\$ 8,579
Ending balance: collectively evaluated for impairment	\$ 51,448	\$ 262,887	\$ 104,525	\$ 76,025	\$ 86,056	\$ 25,795	\$ -	\$ 606,736
<b>December 31, 2016</b>	Construction	Commercial	One to four	Multi-family	Commercial	Consumer and Other	Unallocated	Total
	Real Estate	Real Estate	family					
<b>Allowance for loan losses:</b>	<i>(In Thousands)</i>							
Ending balance: individually evaluated for impairment	\$ 302	\$ -	\$ 14	\$ -	\$ 241	\$ 45	\$ -	\$ 602
Ending balance: collectively evaluated for impairment	\$ 1,075	\$ 1,687	\$ 842	\$ 206	\$ 927	\$ 292	\$ 111	\$ 5,140
<b>Loans:</b>								
Ending balance: individually evaluated for impairment	\$ 5,447	\$ 161	\$ 2,060	\$ -	\$ 925	\$ 106	\$ -	\$ 8,699
Ending balance: collectively evaluated for impairment	\$ 35,465	\$ 249,420	\$ 104,351	\$ 48,483	\$ 74,480	\$ 23,500	\$ -	\$ 535,699

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to income. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. The general component covers nonclassified loans and is based on historical charge-off experience and expected loss given default derived from the Bank's internal risk rating process. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, 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. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans.



The following table summarizes the recorded investment in impaired loans at June 30, 2017 and December 31, 2016:

	June 30, 2017			December 31, 2016		
	Recorded Unpaid Principal Balance	Specific Allowance		Recorded Unpaid Principal Balance	Specific Allowance	
	<i>(In Thousands)</i>					
<b>Loans without a specific valuation allowance</b>						
Real estate - residential mortgage:						
One to four family units	\$1,802	\$1,802	\$ -	\$2,006	\$2,006	\$ -
Multi-family	-	-	-	-	-	-
Real estate - construction	2,967	2,967	-	3,017	3,017	-
Real estate - commercial	328	328	-	161	161	-
Commercial loans	540	540	-	622	622	-
Consumer and other loans	6	6	-	3	3	-
<b>Loans with a specific valuation allowance</b>						
Real estate - residential mortgage:						
One to four family units	\$46	\$46	\$ 65	\$54	\$54	\$ 14
Multi-family	-	-	-	-	-	-
Real estate - construction	2,397	3,630	277	2,430	3,663	302
Real estate - commercial	-	-	93	-	-	-
Commercial loans	435	936	327	303	755	241
Consumer and other loans	58	58	12	103	103	45
<b>Total</b>						
Real estate - residential mortgage:						
One to four family units	\$1,848	\$1,848	65	\$2,060	\$2,060	\$ 14
Multi-family	-	-	-	-	-	-
Real estate - construction	5,364	6,597	277	5,447	6,680	302
Real estate - commercial	328	328	93	161	161	-
Commercial loans	975	1,476	327	925	1,377	241
Consumer and other loans	64	64	12	106	106	45
<b>Total</b>	<b>\$8,579</b>	<b>\$10,313</b>	<b>\$ 774</b>	<b>\$8,699</b>	<b>\$10,384</b>	<b>\$ 602</b>

The following table summarizes average impaired loans and related interest recognized on impaired loans for the three and six months ended June 30, 2017 and 2016:

	For the Three Months Ended June 30, 2017 Average		For the Three Months Ended June 30, 2016 Average	
	Investment in Impaired Loans ( <i>In Thousands</i> )	Interest Income Recognized	Investment in Impaired Loans	Interest Income Recognized
<b>Loans without a specific valuation allowance</b>				
Real estate - residential mortgage:				
One to four family units	\$1,823	\$ -	\$2,207	\$ -
Multi-family	-	-	-	-
Real estate - construction	2,966	-	5,662	-
Real estate - commercial	398	-	525	-
Commercial loans	564	-	872	-
Consumer and other loans	13	-	128	1
<b>Loans with a specific valuation allowance</b>				
Real estate - residential mortgage:				
One to four family units	\$46	\$ -	\$9	\$ -
Multi-family	-	-	-	-
Real estate - construction	2,397	-	2,266	-
Real estate - commercial	-	-	-	-
Commercial loans	463	-	392	-
Consumer and other loans	71	-	120	-
<b>Total</b>				
Real estate - residential mortgage:				
One to four family units	\$1,869	\$ -	\$2,216	\$ -
Multi-family	-	-	-	-
Real estate - construction	5,363	-	7,928	-
Real estate - commercial	398	-	525	-
Commercial loans	1,027	-	1,264	-
Consumer and other loans	84	-	248	1
<b>Total</b>	<b>\$8,741</b>	<b>\$ -</b>	<b>\$12,181</b>	<b>\$ 1</b>

	For the Six Months Ended June 30, 2017 Average		For the Six Months Ended June 30, 2016 Average	
	Investment in Impaired Loans (In Thousands)	Interest Income Recognized	Investment in Impaired Loans	Interest Income Recognized
<b>Loans without a specific valuation allowance</b>				
Real estate - residential mortgage:				
One to four family units	\$1,856	\$ -	\$2,223	\$ -
Multi-family	-	-	-	-
Real estate - construction	2,978	-	5,693	-
Real estate - commercial	460	-	863	-
Commercial loans	583	-	1,112	-
Consumer and other loans	11	-	78	1
<b>Loans with a specific valuation allowance</b>				
Real estate - residential mortgage:				
One to four family units	\$43	\$ -	\$21	\$ -
Multi-family	-	-	-	-
Real estate - construction	2,406	-	2,308	-
Real estate - commercial	-	-	-	-
Commercial loans	507	-	545	-
Consumer and other loans	79	-	102	-
<b>Total</b>				
Real estate - residential mortgage:				
One to four family units	\$1,899	\$ -	\$2,244	\$ -
Multi-family	-	-	-	-
Real estate - construction	5,384	-	8,001	-
Real estate - commercial	460	-	863	-
Commercial loans	1,090	-	1,657	-
Consumer and other loans	90	-	180	1
<b>Total</b>	<b>\$8,923</b>	<b>\$ -</b>	<b>\$12,945</b>	<b>\$ 1</b>

At June 30, 2017, the Bank's impaired loans shown in the table above included loans that were classified as troubled debt restructurings ("TDR"). The restructuring of a loan is considered a TDR if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession.

In assessing whether or not a borrower is experiencing financial difficulties, the Bank considers information currently available regarding the financial condition of the borrower. This information includes, but is not limited to, whether (i) the debtor is currently in payment default on any of its debt; (ii) a payment default is probable in the foreseeable future without the modification; (iii) the debtor has declared or is in the process of declaring bankruptcy and (iv) the debtor's projected cash flow is sufficient to satisfy the contractual payments due under the original terms of the loan without a modification.

The Bank considers all aspects of the modification to loan terms to determine whether or not a concession has been granted to the borrower. Key factors considered by the Bank include the debtor's ability to access funds at a market rate for debt with similar risk characteristics, the significance of the modification relative to unpaid principal balance or collateral value of the debt, and the significance of a delay in the timing of payments relative to the original contractual terms of the loan. The most common concessions granted by the Bank generally include one or more modifications to the terms of the debt, such as (i) a reduction in the interest rate for the remaining life of the debt, (ii) an extension of the maturity date at an interest rate lower than the current market rate for new debt with similar risk, (iii) a reduction on the face amount or maturity amount of the debt as stated in the original loan, (iv) a temporary period of interest-only payments, (v) a reduction in accrued interest, and (vi) an extension of amortization.

The following table presents the carrying balance of TDRs as of June 30, 2017 and December 31, 2016:

	June 30, 2017	December 31, 2016
Real estate - residential mortgage:		
One to four family units	\$ 1,345,609	\$ 1,564,468
Multi-family	-	-
Real estate - construction	5,364,770	5,446,895
Real estate - commercial	5,736,849	5,736,849
Commercial loans	282,352	401,403
Consumer and other loans	-	-
Total	\$ 12,729,580	\$ 13,149,615

The bank did not have any new TDRs for the six months ending June 30, 2017. The Bank has allocated \$357,585 and \$329,734 of specific reserves to customers whose loan terms have been modified in TDR as of June 30, 2017 and December 31, 2016, respectively.

There were no TDRs for which there was a payment default within twelve months following the modification during the three and six months ending June 30, 2017 and 2016. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

As part of the on-going monitoring of the credit quality of the Bank's loan portfolio, management tracks loans by an internal rating system. All loans are assigned an internal credit quality rating based on an analysis of the borrower's financial condition. The criteria used to assign quality ratings to extensions of credit that exhibit potential problems or well-defined weaknesses are primarily based upon the degree of risk and the likelihood of orderly repayment, and their effect on the Bank's safety and soundness. The following are the internally assigned ratings:

Pass: This rating represents loans that have strong asset quality and liquidity along with a multi-year track record of profitability.

Special mention: This rating represents loans that are currently protected but are potentially weak. The credit risk may be relatively minor, yet constitute an increased risk in light of the circumstances surrounding a specific loan.

Substandard: This rating represents loans that show signs of continuing negative financial trends and unprofitability and therefore, is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any.

Doubtful: This rating represents loans that have all the weaknesses of substandard classified loans with the additional characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Risk characteristics applicable to each segment of the loan portfolio are described as follows.

Real estate-Residential 1-4 family: The residential 1-4 family real estate loans are generally secured by owner-occupied 1-4 family residences. Repayment of these loans is primarily dependent on the personal income and credit rating of the borrowers. Credit risk in these loans can be impacted by economic conditions within the Bank's market areas that might impact either property values or a borrower's personal income. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Real estate-Construction: Construction and land development real estate loans are usually based upon estimates of costs and estimated value of the completed project and include independent appraisal reviews and a financial analysis of the developers and property owners. Sources of repayment of these loans may include permanent loans, sales of developed property or an interim loan commitment from the Bank until permanent financing is obtained. These loans are considered to be higher risk than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, general economic conditions and the availability of long-term financing. Credit risk in these loans may be impacted by the creditworthiness of a borrower, property values and the local economies in the Bank's market areas.

Real estate-Commercial: Commercial real estate loans typically involve larger principal amounts, and repayment of these loans is generally dependent on the successful operations of the property securing the loan or the business conducted on the property securing the loan. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Credit risk in these loans may be impacted by the creditworthiness of a borrower, property values and the local economies in the Bank's market areas.

Commercial: The commercial portfolio includes loans to commercial customers for use in financing working capital needs, equipment purchases and expansions. The loans in this category are repaid primarily from the cash flow of a borrower's principal business operation. Credit risk in these loans is driven by creditworthiness of a borrower and the economic conditions that impact the cash flow stability from business operations.

Consumer: The consumer loan portfolio consists of various term and line of credit loans such as automobile loans and loans for other personal purposes. Repayment for these types of loans will come from a borrower's income sources that are typically independent of the loan purpose. Credit risk is driven by consumer economic factors (such as unemployment and general economic conditions in the Bank's market area) and the creditworthiness of a borrower.

The following tables provide information about the credit quality of the loan portfolio using the Bank's internal rating system as of June 30, 2017 and December 31, 2016:

<b>June 30, 2017</b>	Commercial Construction Real Estate	One to four family	Multi-family	Commercial	Consumer and Other	Total	
<i>(In Thousands)</i>							
Rating:							
Pass	\$51,447	\$ 255,457	\$ 100,349	\$ 76,025	\$ 83,654	\$ 25,675	\$592,607
Special Mention	-	5,916	2,803	-	1,715	-	10,434

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Substandard	5,365	1,676	3,221	-	954	184	11,400
Doubtful	-	166	-	-	708	-	874
Total	\$56,812	\$ 263,215	\$106,373	\$ 76,025	\$ 87,031	\$ 25,859	\$615,315

December 31, 2016	Commercial	One to	Multi-family	Commercial	Consumer	Total
	Construction	four		Real Estate	and Other	
		family				

*(In Thousands)*

Rating:							
Pass	\$35,465	\$ 242,200	\$100,367	\$ 48,483	\$ 69,093	\$ 23,380	\$518,988
Special Mention	-	5,922	2,591	-	4,503	-	13,016
Substandard	5,447	1,459	3,453	-	1,225	226	11,810
Doubtful	-	-	-	-	584	-	584
Total	\$40,912	\$ 249,581	\$106,411	\$ 48,483	\$ 75,405	\$ 23,606	\$544,398



For loans amortized at cost, interest income is accrued based on the unpaid principal balance. Loan origination fees net of certain direct origination costs, are deferred and amortized as a level yield adjustment over the respective term of the loan.

The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the loan is well-secured and in process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

#### Note 5: Benefit Plans

The Company has stock-based employee compensation plans, which are described in the Company's 2016 Annual Report.

The following tables below summarize transactions under the Company's equity plans for the six months ended June 30, 2017:

<b>Stock Options</b>	Number of shares		Weighted Average Exercise Price
	Incentive Stock Option	Non- Incentive Stock Option	
Balance outstanding as of January 1, 2017	60,000	52,500	\$ 20.15
Granted	-	-	-
Exercised	-	-	-
Forfeited	(10,000)	(25,000 )	29.49
Balance outstanding as of June 30, 2017	50,000	27,500	\$ 15.93
Options exercisable as of June 30, 2017	50,000	27,500	\$ 15.93

The total intrinsic value of stock options exercised for the six months ended June 30, 2017 and 2016 was \$0 and \$169,103, respectively. The total intrinsic value of outstanding stock options (including exercisable) was \$618,320 and \$430,880 at June 30, 2017 and 2016, respectively.

### Restricted Stock

	Number of Shares	Weighted Average Grant- Date Fair Value
Balance of shares non-vested as of January 1, 2017	60,955	\$ 13.62
Granted	13,386	20.33
Vested	(27,291)	12.25
Forfeited	-	-
Balance of shares non-vested as of June 30, 2017	47,050	\$ 16.33

In February 2017, the Company granted 6,960 shares of restricted stock to directors pursuant to the 2015 Equity Plan of which 6,195 have a cliff vesting at the end of one year and thus, expensed over that same period and 765 shares have a cliff vesting at the end of three years, and thus, expensed over that same period. These shares had a grant date market price of \$20.35 per share. The total amount of expense for restricted stock grants to directors (including all previous years grants) during the six months ended June 30, 2017 and 2016 was \$66,924 and \$62,240, respectively.

For the six months ended June 30, 2017 and 2016, the Company granted 6,426 and 15,343 shares, respectively, of restricted stock to officers that have a cliff vesting at the end of three years. The expense is being recognized over the applicable vesting period. The total amount of expense for restricted stock grants to officers (including all previous years grants) during the six months ended June 30, 2017 and 2016 was \$108,039 and \$151,020, respectively.

### Performance Stock Units

	Performance	Weighted Average Grant- Date Fair Value
Balance of shares non-vested as of January 1, 2017	-	\$ -
Granted	55,823	20.48
Vested	-	-
Forfeited	-	-
Balance of shares non-vested as of June 30, 2017	55,823	\$ 20.48

On March 29, 2017, the Company granted restricted stock units representing 55,823 hypothetical shares of common stock to officers. There are three possible levels of incentive awards: threshold (25%); target (50%); and maximum (100%). The restricted stock units vest based on two financial performance factors over the period from March 29, 2017 to December 31, 2019 (the "Performance Period"). The two performance measurements of the Company (and the weight given to each measurement) applicable to each award level are as follows: (i) Total Assets (50%) and (ii) Return on Average Assets (50%). In determining compensation expense, the fair value of the restricted stock unit awards was determined based on the closing price of the Company's common stock on the date of grant, which was \$20.48 per share. The expense is being recognized over the applicable vesting period. Due to the fact that the measurements cannot be determined at the time of the grant, the Company estimated that the most likely outcome is the achievement of the target level. If during the Performance Period, additional information becomes available to lead the Company to believe a different level will be achieved for the Performance Period, the Company will reassess the number of units that will vest for the grant and adjust its compensation expense accordingly on a prospective basis. The total amount of expense for restricted stock units during the six months ended June 31, 2017 was \$51,816.



Total stock-based compensation expense recognized for the three months ended June 30, 2017 and 2016 was \$134,318 and \$126,403, respectively. Total stock-based compensation expense recognized for the six months ended June 30, 2017 and 2016 was \$226,779 and \$213,260, respectively. As of June 30, 2017, there was \$940,486 of unrecognized compensation expense related to nonvested restricted stock awards, which will be recognized over the remaining vesting period.

#### Note 6: Income Per Common Share

	For three months ended June 30, 2017			For six months ended June 30, 2017		
	Income Available	Average Common Shares Outstanding	Per Common Share	Income Available	Average Common Shares Outstanding	Per Common Share
Basic Income Per Common Share	\$1,592,573	4,374,725	\$ 0.36	\$3,021,814	4,368,921	\$ 0.69
Effect of Dilutive Securities		51,686			54,439	
Diluted Income Per Common Share	\$1,592,573	4,426,411	\$ 0.36	\$3,021,814	4,423,360	\$ 0.68

  

	For three months ended June 30, 2016			For six months ended June 30, 2016		
	Income Available	Average Common Shares Outstanding	Per Common Share	Income Available	Average Common Shares Outstanding	Per Common Share
Basic Income Per Common Share	\$1,256,152	4,366,507	\$ 0.29	\$2,532,757	4,363,375	\$ 0.58
Effect of Dilutive Securities		53,977			52,028	
Diluted Income Per Common Share	\$1,256,152	4,420,484	\$ 0.28	\$2,532,757	4,415,403	\$ 0.57

Stock options to purchase 58,500 and 33,500 shares of common stock were outstanding during the three and six months ended June 30, 2017 and stock options to purchase 83,500 shares of common stock were outstanding during the three and six months ended June 30, 2016 but were not included in the computation of diluted income per common share because their exercise price was greater than the average market price of the common shares.

**Note 7: New Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, (Topic 606): *Revenue from Contracts with Customers* (“ASU 2014-09”). The scope of the guidance applies to revenue arising from contracts with customers, except for the following: lease contracts, insurance contracts, contractual rights and obligations within the scope of other guidance and nonmonetary exchanges between entities in the same line of business to facilitate sales to customers. The core principle of the new guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration that the entity receives or expects to receive. ASU 2014-09 is not expected to significantly impact the timing or approach to revenue recognition for financial institutions. Initially, the amendments were effective for public entities for annual reporting periods beginning after December 15, 2016, however, the FASB issued ASU 2015-14 *Revenue from Contracts with Customers (Topic 606) – Deferral of the Effective Date*” which deferred the effective date of ASU 2014-09 by one year to annual and interim periods beginning after December 15, 2017. The guidance does not apply to revenue associated with financial instruments, including loans and securities that are accounted for under GAAP, which comprises a significant portion of our revenue stream. As the Company plans to adopt the new guidance in the first quarter of 2018, it is currently evaluating the impact of adopting ASU 2014-09 on its consolidated financial statements, but at this time do not believe the standard will have a significant impact on the financial statements, other than the required new disclosures.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments- Overall (Subtopic 825-10): *Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”). ASU 2016-01 simplifies the impairment assessment of equity investments, clarifies reporting disclosure requirements for financial instruments measured at amortized cost, and requires the exit price notion be disclosed when measuring fair value of financial instruments. ASU 2016-01 details the required separate presentation in other comprehensive income for the change in fair value of a liability related to change in instrument specific credit risk and details the required separate presentation of financial assets and liabilities by measurement category, and clarifies the guidance for a valuation allowance on deferred tax assets related to available-for-sale securities. ASU 2016-01 is effective for annual and interim reporting periods beginning after December 15, 2017. Adoption of ASU 2016-01 is not expected to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases* (“ASU 2016-02”). ASU 2016-02 establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the impact of our pending adoption of the new standard on our consolidated financial statements, but at this time do not believe the standard will have a significant impact on the financial statements.

In March 2016, the FASB issued ASU 2016-09, Compensation-Stock Compensation (Topic 718): *Improvements to Employee Share-Based Payment Accounting*. The purpose of the update was to simplify the accounting for share-based payment transactions, including the income tax consequences of such transactions. Under the provisions of the update the income tax consequences of excess tax benefits and deficiencies are to be recognized in income tax expense in the reporting period in which the awards vest. Previously, excess tax benefits or deficiencies impact stockholders’ equity directly to the extent there was a cumulative excess tax benefit. In the event that a tax deficiency had occurred during the reporting period and a cumulative excess tax benefit did not exist, the tax deficiency was recognized in income tax expense under previous GAAP. The update also provided that entities may continue to estimate forfeitures in accounting for stock based compensation or recognize them as they occur. The provisions of this update became effective for interim and annual periods beginning after December 15, 2016. The adoption of this amendment did not have a material impact on the Company’s financial position, results of operations or cash flows.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): *Measurement of Credit Losses on Financial Instruments*. Among other things, the amendments in this ASU require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with later

effective dates for non-SEC registrant public companies and other organizations. Early adoption will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Company is currently evaluating the provisions of ASU No. 2016-13 to determine the potential impact the new standard will have on the Company's consolidated financial statements, and it is too early at this time to determine the impact on the financial statements.



In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): *Classification of Certain Cash Receipts and Cash Payments*. The update is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows with respect to eight types of cash flows. This new accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2017. Adoption of ASU 2016-15 is not expected to have a material impact on our consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20): *Premium Amortization of Purchased Callable Debt Securities*. The amendments in this ASU shorten the amortization period for certain callable debt securities held at a premium. The amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The amendment will be effective for interim and annual reporting periods beginning after December 15, 2018. The Company elected to early adopt ASU 2017-08 during 2017 and it did not have a significant effect on our consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Compensation-Stock Compensation (Subtopic 718): *Scope of Modification Accounting*. ASU 2017-09 clarifies when changes to terms or conditions of a share-based payment award must be accounted for as a modification. Under the new guidance, an entity will not apply modification accounting to a share-based payment award if all of the following are the same immediately before and after the change: (i) the fair value of the award, (ii) the vesting conditions of the award, and (iii) the classification of the award as either an equity or liability instrument. ASU 2017-09 is effective for the fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The guidance requires companies to apply the requirements prospectively to awards modified on or after the adoption date. ASU 2017-09 is not expected to have a significant impact on our consolidated financial statements.

## **Note 8: Derivative Financial Instruments**

The Company records all derivative financial instruments at fair value in the financial statements. Derivatives are used as a risk management tool to hedge the exposure to changes in interest rates or other identified market risks.

When a derivative is intended to be a qualifying hedged instrument, the Company prepares written hedge documentation that designates the derivative as 1) a hedge of fair value of a recognized asset or liability (fair value hedge) or 2) a hedge of a forecasted transaction, such as, the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). The written documentation includes identification of, among other items, the risk management objective, hedging instrument, hedged item, and methodologies for assessing and measuring hedge effectiveness and ineffectiveness, along with support for management's assertion that the hedge will be highly effective.

In June 2017, the Company entered into a forward start interest rate swap agreement totaling \$50 million notional amount to hedge against interest rate risk on FHLB advances. As a cash flow hedge, the portion of the change in the fair value of the derivative that has been deemed highly effective is recognized in other comprehensive income until the related cash flows from the hedged item are recognized in earnings. At June 30, 2017, the Company reported a \$143,415 unrealized gain, net of an \$84,228 tax effect, in other comprehensive income related to this cash flow hedge. The Company documents, both at inception and periodically over the life of the hedge, its analysis of actual and expected hedge effectiveness. To the extent that the hedge of future cash flows is deemed ineffective, changes in the fair value of the derivative are recognized in earnings as a component of other noninterest expense. For the quarter ended June 30, 2017, there was no ineffectiveness attributable to the cash flow hedge.

A summary of the Company's derivative financial instruments at June 30, 2017 is shown in the following table:

Forward Start	Termination	Derivative	Notional	Rate	Rate	Estimated
Inception Date	Date	Type	Amount	Paid	Hedged	Value at June 30, 2017
					3 month	
2/28/2018	2/28/2025	Interest rate swap	\$50,000,000	2.12%	LIBOR	\$227,643
					Floating	

#### Note 9: Disclosures about Fair Value of Assets and Liabilities

ASC Topic 820, *Fair Value Measurements*, defines fair value as 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. Topic 820 also specifies a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

**Level 1:** Quoted prices in active markets for identical assets or liabilities

**Level 2:** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

**Level 3:** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

The following is a description of the inputs and valuation methodologies used for assets measured at fair value on a recurring basis and recognized in the accompanying condensed consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

*Available-for-sale securities:* Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include equity securities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. For these investments, the inputs used by the pricing service to determine fair value may include one or a combination of observable inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bid offers and reference data market research publications and are classified within Level 2 of the valuation hierarchy. Level 2 securities include U.S. government agencies, municipal securities and government sponsored mortgage-backed securities. The Company has no Level 3 securities.

*Derivative Financial Instruments:* Derivatives are recorded at fair value on a recurring basis utilizing Level 2 inputs. The Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, live trading levels, among other things.

The following table presents the fair value measurements of assets recognized in the accompanying condensed consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2017 and December 31, 2016 (dollar amounts in thousands):

**6/30/2017****Financial assets:**

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
Debt securities:				
Municipals	\$ -	\$35,856	\$ -	\$35,856
Corporates	-	3,055	-	3,055
Government sponsored mortgage-backed securities and SBA loan pools	-	46,095	-	46,095
Available-for-sale securities	\$ -	\$85,006	\$ -	\$85,006

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
Interest rate swaps	\$ -	\$ 228	\$ -	\$ 228

**12/31/2016****Financial assets:**

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
Debt securities:				
Municipals	\$ -	\$38,338	\$ -	\$38,338
Corporates	-	7,053	-	7,053
Government sponsored mortgage-backed securities and SBA loan pools	-	47,008	-	47,008
Available-for-sale securities	\$ -	\$92,399	\$ -	\$92,399

The following is a description of the valuation methodologies used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying statements of financial condition, as well as the general classification of such assets pursuant to the valuation hierarchy.

*Foreclosed Assets Held for Sale:* Fair value is estimated using recent appraisals, comparable sales and other estimates of value obtained principally from independent sources, adjusted for selling costs and discounts based on management's assessment of the condition and marketability of the collateral. Foreclosed assets held for sale are classified within Level 3 of the valuation hierarchy.

*Impaired loans (Collateral Dependent):* Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral for collateral dependent loans.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value. Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2017 and December 31, 2016 (dollar amounts in thousands):

Impaired loans:

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
June 30, 2017	\$ -	\$ -	\$ 1,053	\$ 1,053
December 31, 2016	\$ -	\$ -	\$ 1,006	\$ 1,006

Foreclosed assets held for sale:

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total fair value
June 30, 2017	\$ -	\$ -	\$ -	\$ -
December 31, 2016	\$ -	\$ -	\$ 149	\$ 149

There were no transfers between valuation levels for any asset during the six months ended June 30, 2017 or 2016. If valuation techniques are deemed necessary, the Company considers those transfers to occur at the end of the period when the assets are valued.

The following table presents quantitative information about unobservable inputs used in nonrecurring Level 3 fair value measurement (dollar amounts in thousands):

	Fair Value	Valuation	Unobservable	Range
	June 30, 2017	Technique	Input	(Weighted Average)
Impaired loans (collateral dependent)	\$ 1,053	Market Comparable	Discount to reflect realizable value	0% - 71% (10%)
Foreclosed assets held for sale	\$ -	Market Comparable	Discount to reflect realizable value	0%

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying condensed consolidated balance sheets at amounts other than fair value.

Cash and cash equivalents, interest-bearing deposits and Federal Home Loan Bank stock

The carrying amounts reported in the condensed consolidated balance sheets approximate those assets' fair value.

Held-to-maturity securities

Fair value is based on quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans

The fair value of loans is estimated by discounting the future cash flows using the market rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Loans with similar characteristics were aggregated for purposes of the calculations. The carrying amount of accrued interest approximates its fair value.



Deposits

Deposits include demand deposits, savings accounts, NOW accounts and certain money market deposits. The carrying amount approximates fair value. The fair value of fixed-maturity certificates of deposit is estimated by discounting the future cash flows using rates currently offered for deposits of similar remaining maturities.

Federal Home Loan Bank advances

The fair value of advances is estimated by using rates on debt with similar terms and remaining maturities.

Subordinated debentures

For these variable rate instruments, the carrying amount is a reasonable estimate of fair value. There is currently a limited market for similar debt instruments and the Company has the option to call the subordinated debentures at an amount close to its par value.

Interest payable

The carrying amount approximates fair value.

Commitments to originate loans, letters of credit and lines of credit

The fair value of commitments to originate loans is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit worthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

The following tables present estimated fair values of the Company's financial instruments at June 30, 2017 and December 31, 2016.

June 30, 2017		
Carrying	Fair Value	Hierarchy
Amount		Level

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Financial assets:			
Cash and cash equivalents	\$10,747,347	\$10,747,347	1
Held-to-maturity securities	20,954	21,506	2
Federal Home Loan Bank stock	4,577,500	4,577,500	2
Mortgage loans held for sale	1,903,062	1,903,062	2
Loans, net	608,159,460	611,060,521	3
Interest receivable	2,060,646	2,060,646	2
Financial liabilities:			
Deposits	567,013,636	566,365,967	2
Federal Home Loan Bank advances	93,800,000	94,109,786	2
Subordinated debentures	15,465,000	15,465,000	3
Interest payable	213,907	213,907	2
Unrecognized financial instruments (net of contractual value):			
Commitments to extend credit	-	-	-
Unused lines of credit	-	-	-

	December 31, 2016		Hierarchy Level
	Carrying Amount	Fair Value	
Financial assets:			
Cash and cash equivalents	\$9,088,441	\$9,088,441	1
Held-to-maturity securities	27,528	28,153	2
Federal Home Loan Bank stock	4,611,000	4,611,000	2
Mortgage loans held for sale	2,183,633	2,183,633	2
Loans, net	538,273,640	537,645,692	3
Interest receivable	1,947,063	1,947,063	2
Financial liabilities:			
Deposits	505,362,750	504,829,161	2
Federal Home Loan Bank advances	95,700,000	95,764,840	2
Subordinated debentures	15,465,000	15,465,000	3
Interest payable	207,833	207,833	2
Unrecognized financial instruments (net of contractual value):			
Commitments to extend credit	-	-	-
Unused lines of credit	-	-	-

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

### General

The primary function of the Company is to monitor and oversee its investment in the Bank. The Company engages in few other activities, and the Company has no significant assets other than its investment in the Bank. As a result, the results of operations of the Company are derived primarily from operations of the Bank. The Bank's results of operations are primarily dependent on net interest margin, which is the difference between interest income on interest-earning assets and interest expense on interest-bearing liabilities. The Bank's income is also affected by the level of its noninterest expenses, such as employee salaries and benefits, occupancy expenses and other expenses. The following discussion reviews material changes in the Company's financial condition as of June 30, 2017, and the results of operations for the three and six months ended June 30, 2017 and 2016.

The discussion set forth below, as well as other portions of this Form 10-Q, may contain forward-looking comments. Such comments are based upon the information currently available to management of the Company and management's perception thereof as of the date of this Form 10-Q. When used in this Form 10-Q, words such as "anticipates," "estimates," "believes," "expects," and similar expressions are intended to identify forward-looking statements but are not

the exclusive means of identifying such statements. Such statements are subject to risks and uncertainties. Actual results of the Company's operations could materially differ from those forward-looking comments. The differences could be caused by a number of factors or combination of factors including, but not limited to: changes in demand for banking services; changes in portfolio composition; changes in management strategy; increased competition from both bank and non-bank companies; changes in the general level of interest rates; changes in general or local economic conditions; changes in federal or state regulations and legislation governing the operations of the Company or the Bank; and other factors set forth in reports and other documents filed by the Company with the SEC from time to time, including the risk factors described under Item 1A. of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

## Financial Condition

The Company's total assets increased \$63,739,387 (9%) from \$687,979,819 as of December 31, 2016, to \$751,719,206 as of June 30, 2017.

Available-for-sale securities decreased \$7,393,192 (8%) from \$92,399,235 as of December 31, 2016, to \$85,006,043 as of June 30, 2017. The Company had sales and principal payments of \$14,596,025 offset by purchases of \$5,568,959. The Company had unrealized losses of \$692,160 at June 30, 2017 which was an improvement from unrealized losses of \$2,078,050 at December 31, 2016.

Net loans receivable increased by \$69,885,820 (13%) from \$538,273,640 as of December 31, 2016 to \$608,159,460 as of June 30, 2017. New production included a mix of multi-family, agriculture, hospitality and Small Business Administration ("SBA") lending. During the six month period, permanent multi-family loans increased \$27,541,781 (57%), construction loans increased \$15,899,759 (39%), commercial loans increased \$11,626,112 (15%) and commercial real estate loans increased \$13,634,423 (5%). The Company continues to focus its lending efforts in the commercial, owner occupied real estate and small business lending categories.

Allowance for loan losses increased \$897,715 (16%) from \$5,742,449 as of December 31, 2016 to \$6,640,164 as of June 30, 2017. In addition to the provision for loan loss of \$1,050,000 recorded by the Company for the six months ended June 30, 2017, charge-offs of specific loans (classified as nonperforming at December 31, 2016) exceeded loan recoveries by \$152,285. The increase in the allowance is primarily due to the increased loan balances and reserves on a few specific problem credits. The allowance for loan losses, as a percentage of gross loans outstanding (excluding mortgage loans held for sale), as of June 30, 2017 and December 31, 2016 was 1.08% and 1.05%, respectively. The allowance for loan losses, as a percentage of nonperforming loans outstanding, as of June 30, 2017 and December 31, 2016 was 68.3% and 66.5%, respectively. Management believes the allowance for loan losses is at a level to be sufficient in providing for potential loan losses in the Bank's existing loan portfolio.

Deposits increased \$61,650,886 (12%) from \$505,362,750 as of December 31, 2016, to \$567,013,636 as of June 30, 2017. For the six months ended June 30, 2017, checking and savings accounts increased by \$38,682,025 and certificates of deposit increased by \$22,968,861. The increase in checking and savings accounts was due to the Bank's continued focus to increase core transaction deposits, including retail, commercial and public funds. The increase in certificates of deposit was primarily due to the Bank supplementing deposit sources with \$20,000,000 of brokered certificate of deposits. The Bank utilizes brokered certificate of deposits as a tool to manage cost of funds and to efficiently match changes in liquidity needs based on loan growth. See also the discussion under Item 3—"Quantitative and Qualitative Disclosure about Market Risk – Asset/Liability Management."

Federal Home Loan Bank advances decreased \$1,900,000 (2%) from \$95,700,000 as of December 31, 2016 to \$93,800,000 as of June 30, 2017 due to principal reductions.

Stockholders' equity (including unrealized loss on available-for-sale securities, net of tax) increased \$3,348,758 (5%) from \$69,974,380 as of December 31, 2016, to \$73,323,138 as of June 30, 2017. The Company's net income during this period exceeded dividends paid or declared by \$2,137,509. The equity portion of the Company's unrealized losses on available-for-sale securities and effects of interest rate swaps improved by \$1,016,525 during the six month period. On a per common share basis, stockholders' equity increased from \$16.09 as of December 31, 2016 to \$16.76 as of June 30, 2017.

### **Average Balances, Interest and Average Yields**

The Company's profitability is primarily dependent upon net interest income, which represents the difference between interest and fees earned on loans and debt and equity securities, and the cost of deposits and borrowings. Net interest income is dependent on the difference between the average balances and rates earned on interest-earning assets and the average balances and rates paid on interest-bearing liabilities. Non-interest income, non-interest expense, and income taxes also impact net income.

The following table sets forth certain information relating to the Company's average consolidated balance sheets and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense annualized by the average balance of assets or liabilities, respectively, for the periods shown. Average balances were derived from average daily balances. The average balance of loans includes loans on which the Company has discontinued accruing interest. The yields and costs include fees which are considered adjustments to yields. All dollar amounts are in thousands.

	Three months ended 6/30/2017			Three months ended 6/30/2016		
	Average Balance	Interest	Yield / Cost	Average Balance	Interest	Yield / Cost
<b>ASSETS</b>						
Interest-earning:						
Loans	\$608,269	\$6,743	4.45 %	\$496,966	\$5,628	4.55 %
Investment securities	88,267	454	2.06 %	110,662	526	1.91 %
Other assets	10,289	44	1.72 %	17,583	50	1.14 %
Total interest-earning	706,825	7,241	4.11 %	625,211	6,204	3.99 %
Noninterest-earning	39,043			41,906		
	\$745,868			\$667,117		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>						
Interest-bearing:						
Savings accounts	\$29,509	14	0.19 %	\$27,518	14	0.20 %
Transaction accounts	340,975	459	0.54 %	321,262	305	0.38 %
Certificates of deposit	114,227	273	0.96 %	112,879	251	0.89 %
FHLB advances	104,255	450	1.73 %	65,265	313	1.93 %
Subordinated debentures	15,465	156	4.05 %	15,465	143	3.72 %
Total interest-bearing	604,431	1,352	0.90 %	542,389	1,026	0.76 %
Noninterest-bearing	68,342			55,536		
Total liabilities	672,773			597,925		
Stockholders' equity	73,095			69,192		
	\$745,868			\$667,117		
Net earning balance	\$102,394			\$82,822		
Earning yield less costing rate			3.21 %			3.23 %
Net interest income, and net yield spread on interest earning assets		\$5,889	3.34 %		\$5,178	3.33 %
Ratio of interest-earning assets to interest-bearing liabilities		117 %			115 %	

	Six months ended 6/30/2017			Six months ended 6/30/2016		
	Average Balance	Interest	Yield / Cost	Average Balance	Interest	Yield / Cost
<b>ASSETS</b>						
Interest-earning:						
Loans	\$588,792	\$12,990	4.45 %	\$497,218	\$11,330	4.58 %
Investment securities	90,919	930	2.06 %	104,345	983	1.89 %
Other assets	13,743	93	1.36 %	21,203	96	0.91 %
Total interest-earning	693,454	14,013	4.08 %	622,766	12,409	4.01 %
Noninterest-earning	40,685			40,929		
	\$734,139			\$663,695		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>						
Interest-bearing:						
Savings accounts	\$29,021	28	0.19 %	\$26,954	27	0.20 %
Transaction accounts	338,155	821	0.49 %	325,002	625	0.39 %
Certificates of deposit	111,800	519	0.94 %	112,794	503	0.90 %
FHLB advances	102,911	850	1.67 %	61,184	614	2.02 %
Subordinated debentures	15,465	308	4.02 %	15,465	283	3.68 %
Total interest-bearing	597,352	2,526	0.85 %	541,399	2,052	0.76 %
Noninterest-bearing	64,624			53,706		
Total liabilities	661,976			595,105		
Stockholders' equity	72,163			68,590		
	\$734,139			\$663,695		
Net earning balance	\$96,102			\$81,367		
Earning yield less costing rate			3.22 %			3.24 %
Net interest income, and net yield spread on interest earning assets		\$11,487	3.34 %		\$10,357	3.34 %
Ratio of interest-earning assets to interest-bearing liabilities		116 %			115 %	

### Results of Operations - Comparison of Three and Six Month Periods Ended June 30, 2017 and 2016

Net income for the three and six months ended June 30, 2017 was \$1,592,573 and \$3,021,814, respectively, compared to \$1,256,152 and \$2,532,757 for the three and six months ended June 30, 2016, respectively, which represents an increase in earnings of \$336,421 (27%) for the three month period, and an increase in earnings of \$489,057 (19%) for the six month period.

### Interest Income



Total interest income for the three and six months ended June 30, 2017 increased \$1,037,194 (17%) and \$1,603,551 (13%), respectively, as compared to the three and six months ended June 30, 2016. For the three and six month period ended June 30, 2017 compared to the same periods in 2016, the average yield on interest earning assets increased 12 basis points to 4.11% and increased 7 basis points to 4.08%, while the average balance of interest earning assets increased approximately \$81,614,000 for the three month period and increased approximately \$70,688,000 for the six month period. These increases were primarily due to the Company's strong loan activity during the first half of 2017, in which loan balances increased \$69.9 million compared to December 31, 2016. However, pricing on loans remains very competitive on new and renewing credits. This pricing pressure has impacted the ability to maintain loan yield compared to 2016. For the three and six month period ended June 30, 2017 compared to the same periods in 2016, the yield on loans decreased 10 basis points to 4.45% and decreased 13 basis points to 4.45%.

### **Interest Expense**

Total interest expense for the three and six months ended June 30, 2017 increased \$325,527 (32%) and \$473,577 (23%), respectively, when compared to the three and six months ended June 30, 2016. For the three and six months period ended June 30, 2017 compared to the same periods in 2016, the average cost of interest bearing liabilities increased 14 basis points to 0.90% and increased 9 basis points to 0.85%, while the average balance of interest bearing liabilities increased approximately \$62,042,000 for the three month period and increased approximately \$55,953,000 for the six month period. To fund its asset growth going forward, the Company will continue to utilize a cost effective mix of retail and commercial deposits along with non-core, wholesale funding.

### **Net Interest Income**

Net interest income for the three and six months ended June 30, 2017 increased \$711,667 (14%) and increased \$1,129,974 (11%), respectively, when compared to the same periods in 2016. For the three and six month periods ended June 30, 2017, the average balance of net interest earning assets over liabilities increased by approximately \$19,572,000 and \$14,735,000, respectively, when compared to the same periods in 2016. For the three and six month periods ended June 30, 2017, the net interest margin increased 1 basis points to 3.34% and remained unchanged at 3.34%, respectively, when compared to the same periods in 2016.

### **Provision for Loan Losses**

Provisions for loan losses are charged or credited to earnings to bring the total allowance for loan losses to a level considered adequate by the Company to provide for potential loan losses in the existing loan portfolio. When making its assessment, the Company considers prior loss experience, volume and type of lending, local banking trends and impaired and past due loans in the Company's loan portfolio. In addition, the Company considers general economic conditions and other factors related to collectability of the Company's loan portfolio.

Based on its internal analysis and methodology, management recorded a provision for loan losses of \$575,000 and \$1,050,000 for the three months and six months ended June 30, 2017, respectively, compared to \$375,000 and \$750,000 for the same periods in 2016.

The Company's increase in provision was primarily due to the increased loan balances and increased reserves on a few small problem credits. The Bank will continue to monitor its allowance for loan losses and make future additions based on economic and regulatory conditions. Management may need to increase the allowance for loan losses

through charges to the provision for loan losses if anticipated growth in the Bank's loan portfolio increases or other circumstances warrant.

Although the Bank maintains its allowance for loan losses at a level which it considers to be sufficient to provide for potential loan losses in its existing loan portfolio, there can be no assurance that future loan losses will not exceed internal estimates. In addition, the amount of the allowance for loan losses is subject to review by regulatory agencies which can order the establishment of additional loan loss provisions.

### **Noninterest Income**

Noninterest income increased \$187,647 (16%) and \$308,190 (13%) for the three months and six months ended June 30, 2017, respectively, when compared to the three months and six months ended June 30, 2016. This is primarily due to the Company's increase in fixed-rate mortgage loan income of approximately \$141,000 and \$200,000 and increase in gains on sale of SBA loans of approximately \$42,000 and \$103,000 for the three and six months ended June 30, 2017, respectively, when compared to the same periods in 2016.

### **Noninterest Expense**

Noninterest expense increased \$258,522 (6%) and \$568,666 (7%) for the three and six months ended June 30, 2017 when compared to the same periods in 2016, primarily due to the Company's continued investment in personnel for new markets and to support overall growth of the Company.

Salaries and employee benefits increased \$228,782 (8%) and \$535,621 (10%) for the three and six months ended June 30, 2017 when compared to the same periods in 2016. The Company's recent expansion in the Joplin, Missouri market has created the need for additions of commercial and mortgage staff. The Company has also experienced compensation increases in other key areas of operations, technology and health/retirement benefits.

### **Provision for Income Taxes**

The provision for income taxes increased by \$104,371 (25%) and \$80,441 (9%) for the three and six months ended June 30, 2017 when compared to the same periods of 2016. The increase in the provision for income taxes is a direct result of the Company's taxable income.

### **Nonperforming Assets**

The allowance for loan losses is calculated based upon an evaluation of pertinent factors underlying the various types and quality of the Bank's existing loan portfolio. When making such evaluation, management considers such factors as the repayment status of its loans, the estimated net realizable value of the underlying collateral, borrowers' intent (to the extent known by the Bank) and ability to repay the loan, local economic conditions and the Bank's historical loss ratios. The allowance for loan losses, as a percentage of nonperforming loans outstanding, as of June 30, 2017 and December 31, 2016 was 68.3% and 66.5%, respectively. Total loans classified as substandard, doubtful or loss as of June 30, 2017, were \$12,273,479 or 1.63% of total assets as compared to \$12,393,688 or 1.80% of total assets at December 31, 2016. Management considered nonperforming and total classified loans in evaluating the adequacy of the Bank's allowance for loan losses.

The ratio of nonperforming assets to total assets is another useful tool in evaluating exposure to credit risk. Nonperforming assets of the Bank are comprised of nonperforming loans (including troubled debt restructurings) and assets which have been acquired as a result of foreclosure or deed-in-lieu of foreclosure. All dollar amounts are in thousands.

	6/30/2017	12/31/2016	12/31/2015		
Nonperforming loans	\$ 9,716	\$ 8,632	\$ 13,755		
Real estate acquired in settlement of loans	1,302	2,682	2,392		
Total nonperforming assets	\$ 11,018	\$ 11,314	\$ 16,147		
Total nonperforming assets as a percentage of total assets	1.47	% 1.64	% 2.47	%	
Allowance for loan losses	\$ 6,640	\$ 5,742	\$ 5,812		
Allowance for loan losses as a percentage of gross loans	1.08	% 1.05	% 1.17	%	

### Liquidity and Capital Resources

Liquidity refers to the ability to manage future cash flows to meet the needs of depositors and borrowers and fund operations. Maintaining appropriate levels of liquidity allows the Company to have sufficient funds available for customer demand for loans, withdrawal of deposit balances and maturities of deposits and other liabilities. The Company's primary sources of liquidity include cash and cash equivalents, customer deposits, brokered and internet deposits and Federal Home Loan Bank of Des Moines borrowings. The Company also has established borrowing lines available from the Federal Reserve Bank and other correspondent banks, which are considered a secondary source of funds.

The Company's most liquid assets are cash and cash equivalents, which are cash on hand, amounts due from financial institutions, and certificates of deposit with other financial institutions that have an original maturity of three months or less. The levels of such assets are dependent on the Bank's operating, financing, and investment activities at any given time. The Company's cash and cash equivalents totaled \$10,747,347 as of June 30, 2017 and \$9,088,441 as of December 31, 2016, representing an increase of \$1,658,906. The variations in levels of cash and cash equivalents are influenced by many factors but primarily loan originations and payments, deposit flows and anticipated future deposit flows, which are subject to, and influenced by, many factors.

In July 2013, the Board of Governors of the Federal Reserve Board and the FDIC approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks (commonly known as Basel III). Under the final rules, which began for the Company and the Bank on January 1, 2015 and are subject to a phase-in period through January 1, 2019, minimum requirements will increase for both the quantity and quality of capital held by the Company and the Bank. The rules include a new common equity Tier 1 capital to risk-weighted assets ratio (CET1 ratio) of 4.5% and a capital conservation buffer of 2.5% of risk-weighted assets, which when fully phased-in, effectively results in a minimum CET1 ratio of 7.0%. Basel III raises the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0% (which, with the capital conservation buffer, effectively results in a minimum Tier 1 capital ratio of 8.5% when fully phased-in), effectively resulting in a minimum total capital to risk-weighted assets ratio of 10.5% (with the capital conservation buffer fully phased-in), and requires a minimum leverage ratio of 4.0%. Basel III also makes changes to risk weights for certain assets and off-balance-sheet exposures. We expect that the capital ratios for the Company and the Bank under Basel III will continue to exceed the well capitalized minimum capital requirements, when fully phased in.

The Bank's capital ratios are above the levels required to be considered a well-capitalized financial institution. As of June 30, 2017, the Bank's common equity Tier 1 ratio was 13.20%, the Bank's Tier 1 leverage ratio was 11.77%, its Tier 1 risk-based capital ratio was 13.20% and the Bank's total risk-based capital ratio was 14.20% - all exceeding the minimums of 6.5%, 5.0%, 8.0% and 10.0%, respectively, as well as exceeding the minimums plus the 1.25% of capital conservation buffer required as of June 30, 2017.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

#### **Asset/Liability Management**

The goal of the Bank's asset/liability policy is to manage interest rate risk so as to maximize net interest income over time in changing interest rate environments. Management monitors the Bank's net interest spreads (the difference between yields received on assets and paid on liabilities) and, although constrained by market conditions, economic conditions, and prudent underwriting standards, the Bank offers deposit rates and loan rates designed to maximize net interest income. Management also attempts to fund the Bank's assets with liabilities of a comparable duration to minimize the impact of changing interest rates on the Bank's net interest income. Since the relative spread between financial assets and liabilities is constantly changing, the Bank's current net interest income may not be an indication of future net interest income.

As a part of its asset and liability management strategy and throughout the past several years, the Bank has continued to emphasize the origination of short-term commercial real estate, commercial business and consumer loans, while originating fixed-rate, one- to four-family residential loans primarily for immediate resale in the secondary market.

The Bank constantly monitors its deposits in an effort to decrease their interest rate sensitivity. Rates of interest paid on deposits at the Bank are priced competitively in order to meet the Bank's asset/liability management objectives and spread requirements. The Bank believes, based on historical experience, that a substantial portion of such accounts represents non-interest rate sensitive core deposits.

**Interest Rate Sensitivity Analysis**

The following table sets forth as of June 30, 2017 management's estimates of the projected changes in net portfolio value ("NPV") in the event of 100 and 200 basis point ("BP") instantaneous and permanent increases and decreases in market interest rates. Dollar amounts are expressed in thousands.

BP Change in Rates	Estimated Net Portfolio Value			NPV as % of PV of Assets	
	\$ Amount	\$ Change	% Change	NPV Ratio	Change
+200	\$ 101,559	\$(6,047 )	-6	% 13.93 %	-0.32 %
+100	105,094	(2,512 )	-2	% 14.16 %	-0.09 %
NC	107,606	-	0	% 14.25 %	0.00 %
-100	103,544	(4,062 )	-4	% 13.58 %	-0.67 %
-200	89,849	(17,757)	-17	% 11.68 %	-2.57 %

Computations of prospective effects of hypothetical interest rate changes are based on an internally generated model using actual maturity and repricing schedules for the Bank's loans and deposits, and are based on numerous assumptions, including relative levels of market interest rates, loan repayments and deposit run-offs, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions the Bank may undertake in response to changes in interest rates. For further discussion of the Company's market risk, see the Interest Rate Sensitivity Analysis Section of Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

Management cannot predict future interest rates or their effect on the Bank's NPV in the future. Certain shortcomings are inherent in the method of analysis presented in the computation of NPV. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in differing degrees to changes in market interest rates. Additionally, certain assets, such as adjustable-rate loans, have an initial fixed rate period typically from one to five years, and over the remaining life of the asset changes in the interest rate are restricted. In addition, the proportion of adjustable-rate loans in the Bank's portfolio could decrease in future periods due to refinancing activity if market interest rates remain steady in the future. Further, in the event of a change in interest rates, prepayment and early withdrawal levels could deviate significantly from those assumed in the table. Finally, the ability of many borrowers to service their adjustable-rate debt may decrease in the event of an interest rate increase.

The Bank's Board of Directors (the "Board") is responsible for reviewing the Bank's asset and liability management policies. The Board meets quarterly to review interest rate risk and trends, as well as liquidity and capital ratios and requirements. The Bank's management is responsible for administering the policies and determinations of the Board



with respect to the Bank's asset and liability goals and strategies.

#### **Item 4. Controls and Procedures**

(a) The Company maintains disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

During the quarter ended June 30, 2017, the Company conducted an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of June 30, 2017.

(b) There have been no changes in the Company's internal control over financial reporting during the quarter ended June 30, 2017 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II**

### **Item 1. Legal Proceedings**

None.

### **Item 1A. Risk Factors**

Not applicable.

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

#### **ISSUER PURCHASES OF EQUITY SECURITIES**

The Company has a repurchase plan which was announced on August 20, 2007. This plan authorizes the purchase by the Company of up to 350,000 shares of the Company's common stock. There is no expiration date for this plan. There are no other repurchase plans in effect at this time. The Company had no repurchase activity of the Company's common stock during the quarter ended June 30, 2017.

### **Item 3. Defaults Upon Senior Securities**

Not applicable.

### **Item 4. Mine Safety Disclosures**

Not applicable.

### **Item 5. Other Information**

None

**Item 6. Exhibits**

11. Statement re: computation of per share earnings (set forth in “Note 6: Income Per Common Share” of the Notes to Condensed Consolidated Financial Statement (unaudited))

31(i).1 Certification of the Principal Executive Officer pursuant to Rule 13a -14(a) of the Exchange Act

31(i).2 Certification of the Principal Financial Officer pursuant to Rule 13a - 14(a) of the Exchange Act

32 Officer certifications pursuant to 18 U.S.C. Section 1350

101 The following materials from Guaranty Federal Bancshares, Inc.’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2017 formatted in Extensible Business Reporting Language (XBRL): (i) Condensed Consolidated Balance Sheets (unaudited), (ii) Condensed Consolidated Statements of Income (unaudited), (iii) Condensed Consolidated Statements of Comprehensive Income (unaudited), (iv) Condensed Consolidated Statement of Stockholders’ Equity (unaudited), (v) the Condensed Consolidated Statements of Cash Flows (unaudited), and (vi) related notes.\*

\*Pursuant to Regulation S-T, the interactive data files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

## 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.

Guaranty Federal Bancshares, Inc.

### Signature and Title

### Date

/s/ Shaun A. Burke  
Shaun A. Burke

August 10, 2017

President and Chief Executive Officer

(Principal Executive Officer and Duly Authorized Officer)

/s/ Carter Peters  
Carter Peters

August 10, 2017

Executive Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)