

Home Financial Bancorp

Accountants' Report and Consolidated Financial Statements

June 30, 2011 and 2010

Home Financial Bancorp

June 30, 2011 and 2010

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Independent Accountants' Report

Audit Committee, Board of Directors and Stockholders
Home Financial Bancorp
Spencer, Indiana

We have audited the accompanying consolidated balance sheets of Home Financial Bancorp as of June 30, 2011 and 2010, and the related consolidated statements of income, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Home Financial Bancorp as of June 30, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

Indianapolis, Indiana
September 13, 2011

Home Financial Bancorp
Consolidated Balance Sheets
June 30, 2011 and 2010

Assets

	<u>2011</u>	<u>2010</u>
Cash	\$ 909,616	\$ 877,395
Short-term interest-bearing deposits	4,032,407	3,803,899
Total cash and cash equivalents	4,942,023	4,681,294
Interest-bearing deposits	1,208,394	1,063,669
Investment securities - available for sale	6,140,208	3,703,859
Loans, net of allowance for loan losses of \$663,101 and \$676,528	57,378,535	57,106,182
Real estate acquired for development	132,935	287,119
Premises and equipment	1,953,388	1,942,220
Federal Home Loan Bank of Indianapolis stock	1,032,500	1,187,700
Interest receivable	371,430	375,333
Other assets	1,672,497	1,884,509
Total assets	<u>\$ 74,831,910</u>	<u>\$ 72,231,885</u>

Liabilities

Deposits		
Noninterest-bearing deposits	\$ 4,415,825	\$ 4,403,574
Interest-bearing deposits	46,375,198	42,814,901
Total deposits	50,791,023	47,218,475
Borrowings	15,000,000	16,500,000
Other liabilities	699,563	512,634
Total liabilities	<u>66,490,586</u>	<u>64,231,109</u>

Commitments and Contingencies

Stockholders' Equity

Preferred stock, without par value		
Authorized and unissued - 2,000,000 shares	—	—
Common stock, without par value		
Authorized - 5,000,000 shares		
Issued and outstanding - 2011 - 1,345,605 shares and 2010 - 1,350,605 shares	3,052,374	3,064,874
Additional paid-in capital	176,473	142,458
Retained earnings	5,110,570	4,765,485
Accumulated other comprehensive income	1,907	27,959
Total stockholders' equity	<u>8,341,324</u>	<u>8,000,776</u>
Total liabilities and stockholders' equity	<u>\$ 74,831,910</u>	<u>\$ 72,231,885</u>

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Consolidated Statements of Income

Years Ended June 30, 2011 and 2010

	2011	2010
Interest Income		
Loans	\$ 4,231,882	\$ 4,217,685
Deposits with financial institutions	46,387	44,721
Investment securities	157,050	141,429
Federal Home Loan Bank stock	<u>25,269</u>	<u>26,855</u>
Total interest and dividend income	<u>4,460,588</u>	<u>4,430,690</u>
Interest Expense		
Deposits	606,478	727,909
Federal Home Loan Bank advances	<u>594,855</u>	<u>742,017</u>
Total interest expense	<u>1,201,333</u>	<u>1,469,926</u>
Net Interest Income	3,259,255	2,960,764
Provision for loan losses	<u>180,000</u>	<u>381,000</u>
Net Interest Income After Provision for Loan Losses	<u>3,079,255</u>	<u>2,579,764</u>
Other Income		
Service charges on deposit accounts	345,485	489,390
Gain (loss) on sale of real estate acquired for development	(54,411)	11,147
Net gain on sale of available-for-sale securities	20,273	72,440
ATM service fees	164,646	142,380
Other income	<u>238,826</u>	<u>138,380</u>
Total other income	<u>714,819</u>	<u>853,737</u>
Other Expenses		
Salaries and employee benefits	1,213,424	1,205,464
Net occupancy expenses	139,034	122,878
Equipment expenses	36,363	34,685
Computer processing fees	387,097	382,948
ATM transaction fees	143,004	131,205
Printing and office supplies	44,099	50,148
Legal and professional fees	133,708	93,898
Director and committee fees	64,100	67,400
Advertising expense	88,153	75,805
Repossessed property expense	315,662	194,066
Equity in losses of partnership	71,886	62,886
Other expenses	<u>371,807</u>	<u>362,858</u>
Total other expenses	<u>3,008,337</u>	<u>2,784,241</u>
Income Before Income Tax	785,737	649,260
Income tax expense	<u>275,910</u>	<u>218,810</u>
Net Income	<u>\$ 509,827</u>	<u>\$ 430,450</u>
Net Income Per Share		
Basic	\$.39	\$.33
Diluted	.39	.33

Home Financial Bancorp
Consolidated Statements of Stockholders' Equity
Years Ended June 30, 2011 and 2010

	Common Shares	Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances, July 1, 2009	1,352,926	\$ 3,070,676	\$ 108,442	\$ 4,498,593	\$ 17,125	\$ 7,694,836
Comprehensive income						
Net income				430,450		430,450
Other comprehensive income, net of tax						
Unrealized gains on securities, net of reclassification adjustment					10,834	<u>10,834</u>
Comprehensive income						<u>441,284</u>
Cash dividends (\$.12 per share)				(162,227)		(162,227)
Recognition Retention Plan and Trust (RRP) shares earned			34,016			34,016
Purchase of stock	<u>(2,321)</u>	<u>(5,802)</u>		<u>(1,331)</u>		<u>(7,133)</u>
Balances, June 30, 2010	1,350,605	3,064,874	142,458	4,765,485	27,959	8,000,776
Comprehensive income						
Net income				509,827		509,827
Other comprehensive income, net of tax						
Unrealized gains on securities, net of reclassification adjustment					(26,052)	<u>(26,052)</u>
Comprehensive income						<u>483,775</u>
Cash dividends (\$.12 per share)				(161,279)		(161,279)
Recognition Retention Plan and Trust (RRP) shares earned			34,015			34,015
Purchase of stock	<u>(5,000)</u>	<u>(12,500)</u>		<u>(3,463)</u>		<u>(15,963)</u>
Balances, June 30, 2011	<u>1,345,605</u>	<u>\$ 3,052,374</u>	<u>\$ 176,473</u>	<u>\$ 5,110,570</u>	<u>\$ 1,907</u>	<u>\$ 8,341,324</u>

Home Financial Bancorp

Consolidated Statements of Cash Flows

Years Ended June 30, 2011 and 2010

	2011	2010
Operating Activities		
Net income	\$ 509,827	\$ 430,450
Items not requiring (providing) cash		
Provision for loan losses	180,000	381,000
Investment securities amortization, net	11,158	6,880
RRP shares earned	34,015	34,016
Depreciation	88,361	85,713
Deferred income taxes	90,904	120,407
(Gain) loss on sale of real estate acquired for development	54,411	(11,147)
Foreclosed asset losses	89,587	35,258
Investment securities gains	(20,273)	(72,440)
Losses from partnership	71,886	62,886
Net change in interest receivable	3,903	(5,236)
Other adjustments	139,719	(239,929)
Net cash provided by operating activities	1,253,498	827,858
Investing Activities		
Net change in interest-bearing deposits	(144,725)	(63,669)
Purchase of securities available for sale	(4,271,856)	(4,190,204)
Proceeds from sales of securities available for sale	801,488	1,903,408
Proceeds from maturities and paydowns of securities available for sale	1,000,000	57,828
Net changes in loans	(832,752)	(1,184,460)
Proceeds from sale of foreclosed assets	692,641	316,259
Purchase of premises and equipment	(99,529)	(70,920)
Purchase of limited partnership interests	(247,310)	—
Purchase of real estate acquired for development and development cost	(3,272)	(566)
Proceeds from sale of real estate acquired for development	103,045	32,457
Proceeds from sale of FHLB of Indianapolis stock	155,200	—
Net cash used in investing activities	(2,847,070)	(3,199,867)
Financing Activities		
Net change in		
Noninterest-bearing deposits	12,251	490,319
Interest-bearing deposits	3,560,297	3,462,499
Proceeds from other borrowings	4,000,000	3,500,000
Repayment of other borrowings	(5,500,000)	(5,500,000)
Purchase of stock	(15,963)	(7,133)
Dividends paid	(202,284)	(162,227)
Net cash provided by financing activities	1,854,301	1,783,458
Net Change in Cash and Cash Equivalents	260,729	(588,551)
Cash and Cash Equivalents, Beginning of Year	4,681,294	5,269,845
Cash and Cash Equivalents, End of Year	\$ 4,942,023	\$ 4,681,294
Additional Cash Flows and Supplementary Information		
Interest paid	\$ 1,205,380	\$ 1,477,579
Income tax paid	197,274	248,765
Transfers from loans to foreclosed assets	380,399	514,075

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Notes to Consolidated Financial Statements
June 30, 2011 and 2010
(Table Dollar Amounts in Thousands, Except Share Data)

Note 1: Nature of Operations and Summary of Significant Accounting Policies

The accounting and reporting policies of Home Financial Bancorp (Company) and its wholly owned subsidiaries, Owen Community Bank, s.b. (Bank) and OCB Insurance Agency, Inc. (OCB Insurance) and the Bank's wholly owned subsidiary, BSF, Inc. (BSF), conform to accounting principles generally accepted in the United States of America and reporting practices followed by the thrift industry. The more significant of the policies are described below.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Company is a savings and loan holding company whose principal activity is the ownership and management of the Bank. The Bank operates under a federal thrift charter, known as a federal stock savings bank, and provides full banking services. As a federally chartered thrift, the Bank is subject to regulation by the Office of Thrift Supervision and the Federal Deposit Insurance Corporation.

The Bank generates mortgage and consumer loans and receives deposits from customers located primarily in Owen, Putnam and surrounding counties. The Bank's loans are generally secured by specific items of collateral including real property and consumer assets.

BSF engages in purchasing and developing large tracts of real estate. After land is purchased, BSF subdivides the real estate into lots, makes improvements such as streets, and sells individual lots, usually on contract for deed. OCB Insurance provides auto and hazard insurance primarily to customers of the Bank.

Consolidation - The consolidated financial statements include the accounts of the Company, Bank, BSF and OCB Insurance after elimination of all material intercompany transactions.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, valuation of deferred tax assets and fair values of financial instruments.

Cash Equivalents - The Company considers all liquid investments with original maturities of three months or less to be cash equivalents.

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Interest-bearing Deposits in Banks - Interest-bearing deposits in banks mature within one year and are carried at cost.

Investment Securities - Debt securities are classified as held to maturity when the Company has the positive intent and ability to hold the securities to maturity. Securities held to maturity are carried at amortized cost. Debt securities not classified as held to maturity are classified as available for sale. Securities available for sale are carried at fair value with unrealized gains and losses reported separately in accumulated other comprehensive income, net of tax.

When the Company does not intend to sell a debt security, and it is more likely than not, the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

Amortization of premiums and accretion of discounts are recorded as interest income from securities. Realized gains and losses are recorded as net security gains (losses). Gains and losses on sales of securities are determined on the specific-identification method.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoffs are reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans.

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

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days past due unless the credit 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 are 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.

Discounts and premiums on purchased residential real estate loans are amortized to income using the interest method over the remaining period to contractual maturity, adjusted for anticipated prepayments. Discounts and premiums on purchased consumer loans are recognized over the expected lives of the loans using methods that approximate the interest method.

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 uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

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The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility 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 or observable market price) 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 Company'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 Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in 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 for commercial and construction loans 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. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment measurements, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

Real estate acquired for development is carried at the lower of cost or fair value. Costs relating to development and improvements of property are allocated to individual lots and capitalized, whereas costs relating to holding the property are expensed. Gains and losses on sales of lots are determined on the specific-identification method.

Premises and equipment are carried at cost, net of accumulated depreciation. Depreciation is computed using the accelerated and straight-line methods based principally on the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred while major additions and improvements are capitalized. Gains and losses on dispositions are included in current operations.

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Federal Home Loan Bank (FHLB) stock is a required investment for institutions that are members of the FHLB system. The required investment in the common stock is based on a predetermined formula.

Pension plan costs are based on actuarial computations and charged to current operations. The funding policy is to pay at least the minimum amounts required by ERISA.

Income tax - The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Uncertain tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to the management's judgment.

The Company recognizes interest and penalties on income taxes as a component of income tax expense.

Earnings per share have been computed based upon the weighted-average common shares and potential common shares outstanding during the period. RRP shares have been excluded from the computation of average common shares and potential common shares outstanding.

Current Economic Conditions - The current protracted economic decline continues to present financial institutions with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair values of investments and other assets, constraints on liquidity and capital and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans. The consolidated financial statements have been prepared using values and information currently available to the Company.

Due to national, state and local economic conditions, values for commercial and development real estate have declined significantly, and the market for these properties is depressed.

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Given the volatility of current economic conditions, the values of assets and liabilities recorded in the consolidated balance sheets could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity.

Subsequent events have been evaluated through September 13, 2011, which is the date the consolidated financial statements were available to be issued.

Note 2: Restriction on Cash and Due From Banks

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000. At June 30, 2011, the Company's cash accounts exceeded federally insured limits by approximately \$858,000. Additionally, the Company had approximately \$3,552,000 at the Federal Home Loan Bank, a government-sponsored entity, which is not insured by the FDIC.

Note 3: Investment Securities

	2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
Federal agencies	\$ 3,473	\$ 7	\$ (32)	\$ 3,448
Corporate bonds	120	—	—	120
Municipal bonds	2,543	38	(11)	2,570
Marketable equity securities	<u>1</u>	<u>1</u>	<u>—</u>	<u>2</u>
Total investment securities	<u>\$ 6,137</u>	<u>\$ 46</u>	<u>\$ (43)</u>	<u>\$ 6,140</u>

	2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
Federal agencies	\$ 1,000	\$ 11	\$ —	\$ 1,011
Corporate bonds	120	—	—	120
Municipal bonds	2,537	49	(14)	2,572
Marketable equity securities	<u>1</u>	<u>—</u>	<u>—</u>	<u>1</u>
Total investment securities	<u>\$ 3,658</u>	<u>\$ 60</u>	<u>\$ (14)</u>	<u>\$ 3,704</u>

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Maturities of available-for-sale investments at June 30, 2011:

	Amortized Cost	Approximate Fair Value
Within one year	\$ —	\$ —
One to five years	2,391	2,402
Five to ten years	2,883	2,868
After ten years	862	868
Marketable equity securities not due on a single maturity date	<u>1</u>	<u>2</u>
	<u>\$ 6,137</u>	<u>\$ 6,140</u>

No securities were pledged at June 30, 2011 and 2010.

Proceeds from sales of securities available for sale during 2011 and 2010 were \$801,000 and \$1,903,000, respectively. Gains realized from sales of securities during 2011 and 2010 totaled \$21,000 and \$72,000, respectively. Losses realized from sales of securities during 2011 and 2010 totaled \$2,000 and \$0, respectively. Net gains on security transactions for 2011 and 2010 resulted in a tax expense of \$8,000 and \$29,000.

At June 30, 2011 and 2010, certain investments in agency and municipal bond securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at June 30, 2011 was \$2,272,000, which is approximately 37.0 percent of the Company's investment portfolio. These declines primarily resulted from changes in market interest rates.

The following table shows our investments' 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, 2011.

Description of Securities	2011				Total	
	Less Than 12 Months Fair Value	Unrealized Losses	12 Months or More Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Agency bonds	\$ 1,717	\$ (32)	\$ —	\$ —	\$ 1,717	\$ (32)
Municipal bonds	<u>303</u>	<u>(3)</u>	<u>252</u>	<u>(8)</u>	<u>555</u>	<u>(11)</u>
	<u>\$ 2,020</u>	<u>\$ (35)</u>	<u>\$ 252</u>	<u>\$ (8)</u>	<u>\$ 2,272</u>	<u>\$ (43)</u>

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Note 4: Loans and Allowance

	2011	2010
Real estate mortgage loans		
Residential	\$ 43,883	\$ 41,821
Mobile home and land	6,453	7,296
Nonresidential	5,227	6,199
Mobile home loans	2,348	2,738
Commercial and industrial	181	186
Consumer loans	<u>302</u>	<u>280</u>
	<u>58,394</u>	<u>58,520</u>
Undisbursed portion of loans	(326)	(700)
Deferred loan fees	(26)	(37)
Allowance for loan losses	<u>(663)</u>	<u>(677)</u>
	<u>(1,015)</u>	<u>(1,414)</u>
Total loans	<u>\$ 57,379</u>	<u>\$ 57,106</u>

The risk characteristics of each loan portfolio segment are as follows:

Commercial and industrial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets, such as accounts receivable or inventory, and may include a personal guarantee. Short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Nonresidential real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The characteristics of properties securing the Company's commercial real estate portfolio are diverse, but with geographic location almost entirely in the Company's market area. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In general, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate versus nonowner-occupied loans.

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Residential, mobile home and land, mobile home and consumer loans consist of two segments - residential mortgage loans and personal loans. For residential mortgage loans that are secured by 1-4 family residences or mobile homes with land and are generally owner-occupied, the Company generally establishes a maximum loan-to-value ratio. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer personal loans are secured by consumer personal assets, such as automobiles, mobile homes or recreational vehicles. Some consumer personal loans are unsecured, such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas, such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

	2011	2010
Allowance for loan losses		
Balances, July 1	\$ 677	\$ 613
Provision for loan losses	180	381
Recoveries	17	9
Loans charged off	(211)	(326)
Balances, June 30	\$ 663	\$ 677

The following tables present the balance in the allowance for loan losses and the recorded investment in loans based on the portfolio segment and impairment method as of June 30, 2011:

	Real Estate Mortgage Loans			Mobile Home Loans	Commercial	Consumer Loans	Total
	Mobile Home and Land	Residential	Nonresidential				
Allowance Balances:							
Individually evaluated for impairment	\$ 5	\$ 76	\$ 41	\$ 45	\$ —	\$ —	\$ 167
Collectively evaluated for impairment	109	246	47	77	4	13	496
Total Allowance for Loan Losses	\$ 114	\$ 322	\$ 88	\$ 122	\$ 4	\$ 13	\$ 663
Loan Balances:							
Individually evaluated for impairment	\$ 293	\$ 2,530	\$ 257	\$ 307	\$ —	\$ —	\$ 3,387
Collectively evaluated for impairment	6,160	41,353	4,970	2,041	181	302	55,007
Total Loan Balances	\$ 6,453	\$ 43,883	\$ 5,227	\$ 2,348	\$ 181	\$ 302	\$ 58,394

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Management's general practice is to charge down loans individually evaluated for impairment to the fair value of the underlying collateral.

Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company's policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except 1-4 family residential properties and consumer, the Company promptly charges-off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower's ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges-off residential, mobile home and land, mobile home, and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance which provides for the charge-down of 1-4 family first and junior lien mortgages to the net realizable value less costs to sell when the loan is 180 days past due, charge-off of unsecured open-end loans when the loan is 180 days past due, and charge-down to the net realizable value when other secured loans are 120 days past due. Loans at these respective delinquency thresholds for which the Company can clearly document that the loan is both well-secured and in the process of collection, such that collection will occur regardless of delinquency status, need not be charged off.

The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the prior three years. Management believes the historical loss experience methodology is appropriate in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed.

The following table presents the credit risk profile of the Company's loan portfolio based on rating category and payment activity as of June 30, 2011:

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
Impaired loans with no related allowance recorded:						
Real estate mortgage loans:						
Residential	\$ 43,079	\$ 246	\$ 558	\$ —	\$ —	\$ 43,883
Mobile home and land	6,403	15	35	—	—	6,453
Nonresidential	5,137	—	90	—	—	5,227
Mobile home	2,046	1	301	—	—	2,348
Commercial and industrial	—	—	181	—	—	181
Consumer loans	<u>301</u>	<u>—</u>	<u>1</u>	<u>—</u>	<u>—</u>	<u>302</u>
Total	<u>\$ 56,966</u>	<u>\$ 262</u>	<u>\$ 1,166</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 58,394</u>

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Internal Risk Categories

The pass grade is considered satisfactory. The grade of Special Mention, represents loans of lower quality and is considered criticized. The grades of Substandard, and Doubtful, refer to assets that are classified. The use and application of these grades by the bank will be uniform and shall conform to the bank's policy.

Pass - Loans of reasonable credit strength and repayment ability proving an average credit risk due to one or more underlying weaknesses.

Special Mention - A special mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Ordinarily, special mention credits have characteristics which corrective management action would remedy.

Substandard - Loans classified as substandard are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful - Loans classified as doubtful have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current known facts, conditions and values, highly questionable and improbable.

Loss - Loans classified as loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off even though partial recovery may be affected in the future.

The following table presents the Company's loan portfolio aging analysis as of June 30, 2011:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Real estate mortgage loans:							
Residential	\$ 2,210	\$ 601	\$ 803	\$ 3,614	\$ 40,269	\$ 43,883	\$ —
Mobile home and land	490	177	50	717	5,736	6,453	—
Nonresidential	104	12	—	116	5,111	5,227	—
Mobile home loans	63	40	270	373	1,975	2,348	—
Commercial and industrial	—	—	—	—	181	181	—
Consumer loans	9	1	—	10	292	302	—
Total	<u>\$ 2,876</u>	<u>\$ 831</u>	<u>\$ 1,123</u>	<u>\$ 4,830</u>	<u>\$ 53,564</u>	<u>\$ 58,394</u>	<u>\$ —</u>

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The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date.

The following table presents the Company's nonaccrual loans at June 30, 2011:

	Nonaccrual Loans June 30, 2011
Real estate mortgage loans:	
Residential	\$ 803
Mobile home and land	50
Nonresidential	—
Mobile home loans	270
Commercial and industrial	—
Consumer loans	—
Total	\$ 1,123

The following table presents impaired loans for the year ended June 30, 2011:

	Recorded Balance	Unpaid Principal Balance	Related Allowance
Impaired loans without a specific valuation allowance:			
Real estate mortgage loans:			
Residential	\$ 2,284	\$ 2,284	\$ —
Mobile home and land	184	184	—
Nonresidential	210	210	—
Mobile home loans	230	230	—
Commercial and industrial	—	—	—
Consumer loans	—	—	—
Total	2,908	2,908	—
Impaired loans with a specific valuation allowance:			
Real estate mortgage loans:			
Residential	246	246	76
Mobile home and land	109	109	5
Nonresidential	47	47	41
Mobile home loans	77	77	45
Commercial and industrial	—	—	—
Consumer loans	—	—	—
Total	479	479	167
Total impaired loans	\$ 3,387	\$ 3,387	\$ 167

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Interest income on loans individually classified as impaired is recognized on a cash basis after all past due and current principal payments have been made. Subsequent payments on nonaccrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured.

Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than six months before returning a nonaccrual loan to accrual status.

Impaired loans totaled \$1,376,000 at June 30, 2010. A specific allowance for loan losses of \$186,000 relates to impaired loans of \$326,000 at June 30, 2010. At June 30, 2010, impaired loans of \$1,050,000 had no related specific allowance for loan losses.

Interest of \$254,000 and \$34,000 was recognized on average impaired loans of \$2,973,000 and \$1,289,000 at June 30, 2011 and 2010, respectively. Interest of \$53,000 and \$5,000 was recognized on impaired loans on a cash basis at June 30, 2011 and 2010, respectively.

At June 30, 2010, there were no accruing loans delinquent 90 days or more. Nonaccruing loans at June 30, 2010 were \$2,363,000.

Note 5: Premises and Equipment

	<u>2011</u>	<u>2010</u>
Land	\$ 418	\$ 376
Buildings	2,596	2,629
Equipment	<u>1,221</u>	<u>1,149</u>
Total cost	4,235	4,154
Accumulated depreciation	<u>(2,282)</u>	<u>(2,212)</u>
Net	<u>\$ 1,953</u>	<u>\$ 1,942</u>

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Note 6: Investment in Limited Partnership

An investment in a limited partnership of \$115,000 and \$181,000 at June 30, 2011 and 2010 included in other assets represents a 99 percent equity in Cunot Apartments (Cunot), a limited partnership organized to build, own and operate a 24-unit apartment complex for senior living. No credits were recorded for the years ended June 30, 2011 and 2010. Condensed unaudited financial statements for Cunot at June 30, 2011 and 2010 and for the two years then ended are as follows:

	2011	2010
Condensed balance sheets		
Assets		
Cash	\$ 138	\$ 110
Land and property	1,057	1,084
Other assets	10	3
Total assets	\$ 1,205	\$ 1,197
Liabilities		
Notes payable	\$ 610	\$ 610
Other liabilities	463	405
Total liabilities	1,073	1,015
Partners' equity	132	182
Total liabilities and partners' equity	\$ 1,205	\$ 1,197
Condensed statements of operations		
Total revenue	\$ 88	\$ 63
Total expenses	(139)	(130)
Net loss	\$ (51)	\$ (67)

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Note 7: Deposits

	2011	2010
Noninterest-bearing demand	\$ 4,416	\$ 4,403
Interest-bearing demand	3,117	2,862
Money market deposits	870	4,078
Savings	9,366	8,575
Certificates of \$100,000 or more	18,657	13,022
Other certificates	14,365	14,278
Total deposits	\$ 50,791	\$ 47,218

Certificates maturing in years ending June 30:

2012	\$ 15,906	
2013	8,395	
2014	2,362	
2015	2,886	
2016	3,473	
	\$ 33,022	

Brokered deposits totaled approximately \$11,617,000 and \$7,044,000 at June 30, 2011 and 2010, respectively.

Note 8: Borrowings

The Federal Home Loan Bank (FHLB) advances totaled \$15,000,000 and \$16,500,000 at June 30, 2011 and 2010, respectively.

At June 30, 2011, the FHLB advances are secured by mortgage loans totaling \$26,484,000. Advances, at interest rates from 1.33 to 5.56 percent, are subject to restrictions or penalties in the event of prepayment. Advances totaling \$3,000,000 may, at certain dates, be converted to adjustable rate advances by the FHLB. If converted, the advances may be prepaid without penalty.

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FHLB advance maturities in years ending June 30:

2012	\$	3,500
2013		3,000
2014		3,000
2015		2,000
2016		1,500
Thereafter		<u>2,000</u>
	\$	<u>15,000</u>

Note 9: Income Tax

	<u>2011</u>	<u>2010</u>
Income tax expense		
Currently payable		
Federal	\$ 127	\$ 53
State	58	46
Deferred		
Federal	90	120
State	<u>1</u>	<u>—</u>
Total income tax expense	<u>\$ 276</u>	<u>\$ 219</u>

	<u>2011</u>	<u>2010</u>
Reconciliation of federal statutory to actual tax expense (benefit)		
Federal statutory income tax at 34%	\$ 267	\$ 221
Effect of state income taxes	39	31
Tax-exempt interest	(27)	(29)
Other	<u>(3)</u>	<u>(4)</u>
Actual tax expense	<u>\$ 276</u>	<u>\$ 219</u>
Effective tax rate	<u>35.1%</u>	<u>33.7%</u>

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A cumulative net deferred tax asset is included in other assets. The components of the asset are as follows:

	2011	2010
Assets		
Allowance for loan losses	\$ 301	\$ 314
Pension and employee benefit	15	13
Loan fees	11	16
Other real estate owned	61	23
Low income housing credit carry over	—	79
Unrealized capital loss carryforward	45	50
Total assets	433	495
Liabilities		
Depreciation	(113)	(97)
State income tax	(11)	(11)
FHLB stock	(43)	(50)
Prepaid expenses	(52)	(41)
Partnership	(63)	(57)
Other	—	(16)
Total liabilities	(282)	(272)
Valuation Allowance		
Beginning balance	(50)	(50)
Increase during the period	—	—
Ending balance	(50)	(50)
Net deferred tax asset	\$ 101	\$ 173

Management believes the low income housing credits will be utilized during the carry forward limitation period.

Retained earnings at June 30, 2011, include approximately \$700,000 for which no deferred federal income tax liability has been recognized. This amount represents an allocation of income to bad debt deductions as of June 30, 1988 for tax purposes only. Reduction of amounts so allocated for purposes other than tax bad debt losses including redemption of bank stock or excess dividends, or loss of “bank status” would create income for tax purposes only, which income would be subject to the then-current corporate income tax rate. The unrecorded deferred federal income tax liability on the above amount was approximately \$240,000 at June 30, 2011.

The Company’s tax years still subject to examination by authorities are years subsequent to 2007.

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Note 10: Other Comprehensive Income (Loss)

	Before-Tax Amount	2011 Tax Expense	Net-of-Tax Amount
Unrealized losses on securities			
Unrealized holding losses arising during the year	\$ (23)	\$ 9	\$ (14)
Less: reclassification adjustment for gains realized in net income	<u>20</u>	<u>(8)</u>	<u>12</u>
Other comprehensive loss	<u>\$ (43)</u>	<u>\$ 17</u>	<u>\$ (26)</u>
		2010	
	Before-Tax Amount	Before-Tax Amount	Before-Tax Amount
Unrealized gains on securities			
Unrealized holding gains arising during the year	\$ 90	\$ (36)	\$ 54
Less: reclassification adjustment for gains realized in net income	<u>72</u>	<u>(29)</u>	<u>43</u>
Other comprehensive income	<u>\$ 18</u>	<u>\$ (7)</u>	<u>\$ 11</u>

Note 11: Commitments and Contingent Liabilities

In the normal course of business, there are outstanding commitments and contingent liabilities, such as commitments to extend credit, which are not included in the accompanying consolidated financial statements. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit is represented by the contractual or notional amount of those instruments. The Company uses the same credit policies in making such commitments as it does for instruments that are included in the consolidated balance sheets.

Financial instruments whose contract amount represents credit risk as of June 30 were as follows:

	2011	2010
Commitments to extend credit	\$ 1,153	\$ 2,021
Unused lines of credit	235	266

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Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies, but may include residential real estate or other assets of the borrower.

The Company has entered into agreements with two officers, which provide for salary continuation for a three-year period under certain circumstances, primarily related to change of control of the Company or Bank, as defined. Under the terms of the agreements, these payments could occur if, following a change of control, such officers are terminated other than for cause or unreasonable changes are made in their employment relationships. These agreements extend automatically for one year on each anniversary date unless certain conditions are met.

The Company and Bank are also subject to claims and lawsuits, which arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate determination of such possible claims or lawsuits will not have a material adverse effect on the consolidated financial position of the Company or Bank.

Note 12: Stockholders' Equity

The Company's Board of Directors has approved the repurchase of up to 15 percent of the Company's outstanding shares of common stock. Such purchases will be made subject to market conditions in open market or block transactions.

Note 13: Dividends and Capital Restrictions

Without prior approval, current regulations allow the Bank to pay dividends to the Company not exceeding retained net profits for the current calendar year to date plus those for the previous two calendar years. At June 30, 2011, total stockholder's equity of the Bank was \$8,099,000 of which \$7,158,000 was restricted from dividend distribution to the Company. Although well capitalized, under current regulations in effect, the Bank is required to submit notice to the Office of Thrift Supervision to pay dividends to the Company.

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Note 14: Regulatory Capital

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies and is assigned to a capital category. The assigned capital category is largely determined by three ratios that are calculated according to the regulations: total risk adjusted capital, Tier 1 capital and Tier 1 leverage ratios. The ratios are intended to measure capital relative to assets and credit risk associated with those assets and off-balance sheet exposures of the entity. The capital category assigned to an entity can also be affected by qualitative judgments made by regulatory agencies about the risk inherent in the entity's activities that are not part of the calculated ratios.

There are five capital categories defined in the regulations, ranging from well capitalized to critically undercapitalized. Classification of a bank in any of the undercapitalized categories can result in actions by regulators that could have a material effect on a bank's operations. At June 30, 2011 and 2010, the Bank was categorized as well capitalized and met all subject capital adequacy requirements. There are no conditions or events since June 30, 2011 that management believes has changed the Bank's classification.

The Bank's actual and required capital amounts and ratios are as follows:

	Actual		2011 Required for Adequate Capital		Required To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total risk-based capital (to risk-weighted assets)	\$ 8,197	19.8%	\$ 3,307	8.0%	\$ 4,134	10.0%
Tier I capital (to risk-weighted assets)	7,680	18.6%	1,654	4.0%	2,481	6.0%
Core capital (to adjusted total assets)	7,680	10.3%	2,969	4.0%	3,712	5.0%
Core capital (to adjusted tangible assets)	7,680	10.3%	1,485	2.0%	N/A	N/A
Tangible capital (to adjusted total assets)	7,680	10.3%	1,114	1.5%	N/A	N/A

	Actual		2010 Required for Adequate Capital		Required To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total risk-based capital (to risk-weighted assets)	\$ 7,615	18.0%	\$ 3,389	8.0%	\$ 4,236	10.0%
Tier I capital (to risk-weighted assets)	7,085	16.7%	1,694	4.0%	2,542	6.0%
Core capital (to adjusted total assets)	7,085	9.9%	2,857	4.0%	3,572	5.0%
Core capital (to adjusted tangible assets)	7,085	9.9%	1,429	2.0%	N/A	N/A
Tangible capital (to adjusted total assets)	7,085	9.9%	1,071	1.5%	N/A	N/A

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Note 15: Employee Benefit Plans

The Bank is a participant in a pension fund known as the Pentegra Group. This plan is a multi-employer plan; separate actuarial valuations are not made with respect to each participating employer. On July 1, 2006, the Company elected to freeze the defined-benefit plan to stop accruing benefits to plan participants beyond what was already earned to that date and to prevent new participants from entering the plan. The plan required contributions in the amount of \$55,000 and \$20,000 for the years ended June 30, 2011 and 2010. The plan provides pension benefits for substantially all of the Bank's employees.

The Company has a Retirement Savings Section 401(k) plan in which substantially all employees may participate. The Company matches participant contributions at the rate of 50 percent of the first 6 percent of base salary contributed by participants. The Company contributes an additional 2 percent of participant base salary regardless of participant contributions. The Company's expense for the plan was \$27,000 and \$35,000 for the years ended June 30, 2011 and 2010.

The Company has an ESOP covering substantially all employees of the Bank. At June 30, 2011, all 161,896 ESOP shares have been allocated. As of June 30, 2011, no unearned shares remained. The Company is obligated at the option of each beneficiary to repurchase shares of the ESOP upon the beneficiary's termination or after retirement. The trustee expense for the ESOP was \$28,000 and \$14,000 for the years ended June 30, 2011 and 2010.

The Company has a Recognition and Retention Plan and Trust (RRP). The RRP may acquire up to 130,948 shares of the Company's common stock for awards to management. Shares awarded to management under the RRP vest at a rate of 20 percent at the end of each full 12 months of service with the Bank after the date of grant. As of June 30, 2011, 121,848 shares of common stock have been awarded to management. Expense under the RRP was \$34,000 for each of the years ended June 30, 2011 and 2010.

The Company has entered into employee agreements with certain officers that provide for the continuation of salary and certain benefits for a specified period of time.

Note 16: Related Party Transactions

The Bank has entered into transactions with certain directors and officers. Such transactions were made in the ordinary course of business on substantially the same terms and conditions, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers, and did not, in the opinion of management, involve more than normal credit risk or present other unfavorable features. The aggregate amount of loans, as defined, to such related parties were as follows:

Balances, July 1, 2010	\$	386
New loans, including renewals		332
Payments, etc. including renewals		<u>(75)</u>
Balances, June 30, 2011	\$	<u>643</u>

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Deposits from related parties held by the Bank at June 30, 2011 and 2010 totaled \$1,034,000 and \$829,000.

Note 17: Stock Option Plan

The Company has reserved 202,370 shares of Company stock for the granting of options to certain directors, officers and other key employees of the Company and the Bank. As of June 30, 2011, there were no stock options outstanding.

Note 18: Earnings Per Share

Earnings per share were computed as follows:

	Net Income	2011 Weighted- Average Shares	Per- Share Amount
Basic Earnings Per Share			
Income available to common stockholders	\$ 510	1,318,153	\$.39
Effect of Dilutive Stock Options	—	—	
Diluted Earnings Per Share			
Income available to common stockholders and assumed conversions	<u>\$ 510</u>	<u>1,318,153</u>	<u>\$.39</u>
	Net Income	2010 Weighted- Average Shares	Per- Share Amount
Basic Earnings Per Share			
Income available to common stockholders	\$ 430	1,313,788	\$.33
Effect of Dilutive Stock Options	—	114	
Diluted Earnings Per Share			
Income available to common stockholders and assumed conversions	<u>\$ 430</u>	<u>1,313,902</u>	<u>\$.33</u>

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Note 19: Condensed Financial Information (Parent Company Only)

Presented below is condensed financial information as to financial position, results of operations and cash flows of the Company:

Condensed Balance Sheets

	2011	2010
Assets		
Cash and cash equivalents	\$ 16	\$ 123
Securities available for sale	122	121
Premises and equipment	429	435
Investment in subsidiaries	8,114	7,742
Other assets	86	52
Total assets	\$ 8,767	\$ 8,473
Liabilities		
	\$ 426	\$ 472
Stockholders' Equity		
	8,341	8,001
Total liabilities and stockholders' equity	\$ 8,767	\$ 8,473

Condensed Statements of Income

	2011	2010
Income		
Dividends from Bank	\$ 198	\$ 100
Interest and other income	64	61
Total income	262	161
Expenses		
Salaries and employee benefits	20	20
Legal and professional fees	41	33
Other expenses	89	88
Total expenses	150	141
Income before income tax benefit and equity in undistributed income of Bank	112	20
Income tax benefit	(34)	(31)
Income before equity in undistributed income of Bank	146	51
Equity in undistributed income (loss) of Bank	364	379
Net Income	\$ 510	\$ 430

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Condensed Statements of Cash Flows

	2011	2010
Operating Activities		
Net income	\$ 510	\$ 430
Items not requiring (providing) cash	(400)	(238)
Net cash provided by operating activities	110	192
Investing Activity - purchases of securities available for sale	—	(120)
Financing Activities		
Dividends paid	(202)	(162)
Purchase of stock	(15)	(7)
Net cash used in financing activities	(217)	(169)
Net Change in Cash and Cash Equivalents	(107)	(97)
Cash and Cash Equivalents at Beginning of Year	123	220
Cash and Cash Equivalents at End of Year	\$ 16	\$ 123

Note 20: Disclosures About Fair Value of Financial Instruments

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

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

Available-for-Sale Securities

Where quoted market prices are not available, fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 1 securities include marketable equity securities. Level 2 securities include federal securities, municipal securities, and corporate bonds. Matrix pricing is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for specific investment securities but rather relying on the investment securities' relationship to other benchmark quoted investment securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

The following tables present the fair value measurements of assets recognized in the accompanying 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, 2011 and 2010:

	Fair Value	2011 Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities				
Federal agencies	\$ 3,448	\$ —	\$ 3,448	\$ —
Corporate bonds	120	—	120	—
Municipal bonds	2,570	—	2,570	—
Marketable equity securities	<u>2</u>	<u>2</u>	<u>—</u>	<u>—</u>
	<u>\$ 6,140</u>	<u>\$ 2</u>	<u>\$ 6,138</u>	<u>\$ —</u>

	Fair Value	2010 Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities				
Federal agencies	\$ 1,011	\$ —	\$ 1,011	\$ —
Corporate bonds	120	—	120	—
Municipal bonds	2,572	—	2,572	—
Marketable equity securities	<u>1</u>	<u>1</u>	<u>—</u>	<u>—</u>
	<u>\$ 3,704</u>	<u>\$ 1</u>	<u>\$ 3,703</u>	<u>\$ —</u>

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Following is a description of the inputs and valuation methodologies used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification pursuant to 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 if deemed necessary by management.

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 tables present the fair value measurements of assets recognized in the accompanying consolidated balance sheets 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, 2011 and 2010:

	2011			
	Fair Value Measurements Using			
	Fair Value	Quoted Prices		
		in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ <u>107</u>	\$ <u>—</u>	\$ <u>—</u>	\$ <u>107</u>

	2010			
	Fair Value Measurements Using			
	Fair Value	Quoted Prices		
		in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ <u>304</u>	\$ <u>—</u>	\$ <u>—</u>	\$ <u>304</u>

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

Cash and Cash Equivalents, Interest-Bearing Deposits, Federal Home Loan Bank Stock, Interest Receivable, and Interest Payable

The carrying amount approximates fair value.

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 time deposits is estimated using a discounted cash flow calculation that applies the rates currently offered for deposits of similar remaining maturities.

Borrowings

Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate the fair value of existing debt. Fair value of long-term debt is based on quoted market prices or dealer quotes for the identical liability when traded as an asset in an active market. If a quoted market price is not available, an expected present value technique is used to estimate fair value.

The following table presents estimated fair values of the Company's financial instruments at June 30, 2011 and 2010.

	2011		2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	\$ 4,942	\$ 4,942	\$ 4,681	\$ 4,681
Interest-bearing deposits	1,208	1,208	1,064	1,064
Available-for-sale securities	6,140	6,140	3,704	3,704
Loans, net	57,379	61,297	57,106	61,851
Federal Home Loan Bank stock	1,033	1,033	1,188	1,188
Financial liabilities				
Deposits	\$ 50,791	\$ 51,535	\$ 47,218	\$ 47,886
Borrowings	15,000	15,727	16,500	17,418
Interest payable	25	25	30	30