

First Bancorp of Indiana, Inc.

Accountants' Reports and Consolidated Financial Statements

June 30, 2008 and 2007



First Bancorp of Indiana, Inc.
June 30, 2008 and 2007

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Independent Accountants' Report

Board of Directors
First Bancorp of Indiana, Inc.
Evansville, Indiana

We have audited the accompanying consolidated balance sheet of First Bancorp of Indiana, Inc. (Company) as of June 30, 2008, and the related consolidated statements of income, stockholders' equity and cash flows for the year 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 audit.

We conducted our audit 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 audit provides 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 the Company as of June 30, 2008, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

September 29, 2008



Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors and Stockholders
First Bancorp of Indiana, Inc.
Evansville, Indiana

We have audited the accompanying consolidated balance sheet of First Bancorp of Indiana, Inc. (Company) as of June 30, 2007, and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended. The Company's management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing auditing procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. Our audit also included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audit provides 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 the Company as of June 30, 2007, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

Evansville, Indiana
September 20, 2007

First Bancorp of Indiana, Inc.
Consolidated Balance Sheets
June 30, 2008 and 2007

Assets

	<u>2008</u>	<u>2007</u>
Cash and due from banks	\$ 7,242,618	\$ 7,455,076
Interest-bearing demand deposits with banks	16,657,396	7,395,910
Federal funds sold	<u>496,856</u>	<u>-</u>
Cash and cash equivalents	24,396,870	14,850,986
Interest-bearing deposits	494,525	1,616,000
Available-for-sale securities	77,034,732	65,120,545
Held-to-maturity securities	14,716,431	14,976,789
Loans, net of allowance for loan losses of \$1,545,000 and \$1,065,000 at June 30, 2008 and 2007, respectively	226,473,828	233,236,981
Premises and equipment	9,164,760	9,322,801
Federal Home Loan Bank stock	4,564,700	4,564,700
Goodwill	6,229,152	6,229,152
Core deposit intangible	777,295	894,431
Other assets	<u>13,493,652</u>	<u>12,179,690</u>
Total assets	<u>\$ 377,345,945</u>	<u>\$ 362,992,075</u>

Liabilities and Stockholders' Equity

Liabilities

Deposits		
Noninterest-bearing	\$ 10,049,319	\$ 11,503,688
Interest-bearing	<u>234,003,857</u>	<u>239,730,019</u>
Total deposits	244,053,176	251,233,707
Borrowings	95,654,944	72,495,874
Advances from borrowers for taxes and insurance	1,020,587	695,051
Other liabilities	<u>5,042,286</u>	<u>4,349,605</u>
Total liabilities	<u>345,770,993</u>	<u>328,774,237</u>

Commitments and Contingencies

Stockholders' Equity

Preferred stock, \$0.01 par value; authorized and unissued 1,000,000 shares		
Common stock, \$0.01 par value; authorized 9,000,000 shares; issued 2008 and 2007 – 2,526,546 and 2,566,346 shares	25,265	25,663
Additional paid-in capital	27,390,180	27,959,954
Retained earnings	18,230,854	18,801,944
Accumulated other comprehensive loss		
Unrealized depreciation on available-for-sale securities, net of income taxes 2008 – \$(964,000); 2007 – \$(419,000)	<u>(1,650,631)</u>	<u>(683,548)</u>
	43,995,668	46,104,013
Unreleased employee stock ownership plan shares 2008 – 37,870 shares; 2007 – 53,020 shares	(386,588)	(541,241)
Treasury stock, at cost 2008 – 778,658 shares; 2007 – 725,445 shares	<u>(12,034,128)</u>	<u>(11,344,934)</u>
Total stockholders' equity	<u>31,574,952</u>	<u>34,217,838</u>
Total liabilities and stockholders' equity	<u>\$ 377,345,945</u>	<u>\$ 362,992,075</u>

First Bancorp of Indiana, Inc.
Consolidated Statements of Income
Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Interest Income		
Loans	\$ 15,824,738	\$ 14,863,159
Investment securities	4,492,612	3,835,793
Deposits with banks	403,379	373,967
Federal funds sold	7,062	12,311
Other	<u>225,781</u>	<u>209,928</u>
Total interest income	<u>20,953,572</u>	<u>19,295,158</u>
Interest Expense		
Deposits	8,699,020	8,607,024
Borrowings	<u>4,228,701</u>	<u>3,341,032</u>
Total interest expense	<u>12,927,721</u>	<u>11,948,056</u>
Net Interest Income	8,025,851	7,347,102
Provision for Loan Losses	<u>1,090,000</u>	<u>400,000</u>
Net Interest Income After Provision for Loan Losses	<u>6,935,851</u>	<u>6,947,102</u>
Noninterest Income		
Service charges on deposit accounts	814,866	425,656
Net gains on sales of loans	182,131	156,679
ATM transaction and POS interchange fees	331,394	258,883
Increase in cash surrender value of life insurance	202,113	203,372
Net gain on sales of premises and equipment	-	71,954
Other	<u>718,550</u>	<u>891,180</u>
Total noninterest income	<u>2,249,054</u>	<u>2,007,724</u>
Noninterest Expense		
Salaries and employee benefits	4,204,604	4,157,869
Impairment of securitization residual	-	270,928
Net occupancy expense	733,085	693,656
Equipment expense	490,967	422,885
Data processing fees	512,453	448,201
Legal and professional fees	217,425	217,841
Amortization of intangible assets	117,136	134,435
Advertising	244,418	246,882
Other	<u>1,754,060</u>	<u>1,784,561</u>
Total noninterest expense	<u>8,274,148</u>	<u>8,377,258</u>
Income Before Income Taxes	910,757	577,568
Provision for Income Taxes	<u>107,257</u>	<u>59,291</u>
Net Income	<u>\$ 803,500</u>	<u>\$ 518,277</u>

First Bancorp of Indiana, Inc.
Consolidated Statements of Stockholders' Equity
Years Ended June 30, 2008 and 2007

	Comprehensive Income (Loss)	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Unallocated ESOP Shares	Treasury Stock	Total
Balance, June 30, 2006		\$ 22,724	\$22,360,757	\$19,305,925	\$ (1,659,119)	\$ (695,893)	\$(11,128,046)	\$ 28,206,348
Net income	\$ 518,277	-	-	518,277	-	-	-	518,277
Dividends on common stock, \$.60 per share	-	-	-	(1,022,258)	-	-	-	(1,022,258)
Purchase of treasury stock (31,399 shares)	-	-	-	-	-	-	(584,478)	(584,478)
Exercise of stock options (23,586 shares)	-	-	(143,429)	-	-	-	367,590	224,161
Employee Stock Ownership Plan shares allocated (15,150 shares)	-	-	121,557	-	-	154,652	-	276,209
Tax benefit of employee benefit plans	-	-	218,341	-	-	-	-	218,341
Stock issued for acquisition (293,946 shares)	-	2,939	5,402,728	-	-	-	-	5,405,667
Change in unrealized depreciation on available-for-sale securities, net of income tax expense of \$609,000	<u>975,571</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>975,571</u>	<u>-</u>	<u>-</u>	<u>975,571</u>
Comprehensive income	<u>\$ 1,493,848</u>							
Balance, June 30, 2007		25,663	27,959,954	18,801,944	(683,548)	(541,241)	(11,344,934)	34,217,838
Net income	\$ 803,500	-	-	803,500	-	-	-	803,500
Dividends on common stock, \$.76 per share	-	-	-	(1,374,590)	-	-	-	(1,374,590)
Purchase of treasury stock (60,065 shares)	-	-	-	-	-	-	(796,340)	(796,340)
Exercise of stock options (6,852 shares)	-	-	(44,622)	-	-	-	107,146	62,524
Employee Stock Ownership Plan shares allocated (15,150 shares)	-	-	47,715	-	-	154,653	-	202,368
Tax benefit of employee benefit plans	-	-	57,755	-	-	-	-	57,755
Purchase of fractional shares in connection with reverse split	-	(398)	(630,622)	-	-	-	-	(631,020)
Change in unrealized depreciation on available-for-sale securities, net of income tax benefit of \$545,000	<u>(967,083)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(967,083)</u>	<u>-</u>	<u>-</u>	<u>(967,083)</u>
Comprehensive loss	<u>\$ (163,583)</u>							
Balance, June 30, 2008		<u>\$ 25,265</u>	<u>\$27,390,180</u>	<u>\$18,230,854</u>	<u>\$ (1,650,631)</u>	<u>\$ (386,588)</u>	<u>\$(12,034,128)</u>	<u>\$ 31,574,952</u>

First Bancorp of Indiana, Inc.
Consolidated Statements of Cash Flows
Years Ended June 30, 2008 and 2007

	2008	2007
Operating Activities		
Net income	\$ 803,500	\$ 518,277
Items not requiring (providing) cash		
Provision for loan losses	1,090,000	400,000
Depreciation	479,146	452,459
Amortization of premiums and discounts on securities	(109,722)	(9,856)
Amortization of net loan origination fees	(322,112)	(300,823)
Amortization of intangible assets	117,136	134,435
Deferred income taxes	96,000	(77,000)
Increase in cash surrender value of life insurance	(202,113)	(203,372)
Loans originated for sale	(7,801,100)	(11,462,660)
Proceeds from sales of loans	7,983,231	11,619,339
Net gain on loan sales	(182,131)	(156,679)
(Gain) loss on sales of premises and equipment	6,429	(71,954)
Compensation expense related to employee stock ownership plan and management recognition plan	202,368	276,209
Tax benefit of employee benefit plans	57,755	75,404
Changes in		
Other assets	(754,754)	(228,370)
Other liabilities	<u>692,681</u>	<u>1,297,206</u>
Net cash provided by operating activities	<u>2,156,314</u>	<u>2,262,615</u>
Investing Activities		
Net change in interest-bearing deposits	1,121,475	4,250,970
Proceeds from maturities of available-for-sale securities	37,382,332	9,852,365
Proceeds from maturities of held-to-maturity securities	1,671,017	1,303,523
Purchases of available-for-sale securities	(50,592,467)	(9,254,567)
Purchases of held-to-maturity securities	(1,433,955)	-
Net change in loans	5,995,265	(7,003,624)
Purchase of premises and equipment	(346,011)	(616,110)
Proceeds from sales of premises and equipment	31,335	113,028
Redemption of Federal Home Loan Bank stock	-	61,600
Acquisition of bank, net of cash received	<u>-</u>	<u>(2,556,155)</u>
Net cash used in investing activities	<u>(6,171,009)</u>	<u>(3,848,970)</u>

First Bancorp of Indiana, Inc.
Consolidated Statements of Cash Flows
Years Ended June 30, 2008 and 2007
(Continued)

	<u>2008</u>	<u>2007</u>
Financing Activities		
Net increase (decrease) in demand deposits, money market, NOW and savings accounts	\$ 32,356,927	\$ (5,485,658)
Net increase (decrease) in certificates of deposit	(39,537,458)	22,837,885
Proceeds from issuance of long-term debt	38,155,000	12,000,000
Repayments of long-term debt	(15,000,000)	(21,500,000)
Net increases in advances from borrowers for taxes and insurance	325,536	87,050
Dividends paid	(1,374,590)	(1,022,258)
Purchase of treasury stock	(796,340)	(584,478)
Exercise of stock options	62,524	224,161
Windfall tax benefit of stock options exercised	-	142,937
Purchase of fractional shares in connection with reverse split	<u>(631,020)</u>	<u>-</u>
Net cash provided by financing activities	<u>13,560,579</u>	<u>6,699,639</u>
Increase in Cash and Cash Equivalents	9,545,884	5,113,284
Cash and Cash Equivalents, Beginning of Year	<u>14,850,986</u>	<u>9,737,702</u>
Cash and Cash Equivalents, End of Year	<u>\$ 24,396,870</u>	<u>\$ 14,850,986</u>
Supplemental Cash Flows Information		
Interest paid	\$ 12,659,983	\$ 11,231,392
Income taxes paid, net of refunds	\$ (194,935)	\$ 175,000

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
June 30, 2008 and 2007
(Table Dollar Amounts in Thousands, Except Share Data)

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

Nature of Operations

The accounting and reporting policies of First Bancorp of Indiana, Inc. (Company) and its wholly owned subsidiaries, First Federal Savings Bank (Bank) and First Bancorp of Indiana Statutory Trust I (Trust), conform to accounting principles generally accepted in the United States of America and reporting practices followed by the thrift industry. The Bank operates some of its branches under Home Building Savings Bank (HBSB), a division of First Federal Savings Bank. The Bank has four wholly owned subsidiaries, FFSL Service Corporation (FFSL), FFSB Financial Corporation (FFSB Financial), FBEI Investments, Inc. (FBEI) and White River Service Corporation (WRSC). The more significant of the policies are described below.

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 savings bank charter and provides full banking services in a single significant business segment. As a federally chartered savings bank, the Bank is subject to regulation by the Office of Thrift Supervision and the Federal Deposit Insurance Corporation.

The Bank generates commercial, mortgage and consumer loans and receives deposits from customers located primarily in Vanderburgh County and Daviess County, Indiana and surrounding counties. The Bank's loans are generally secured by specific items of collateral, including real property and consumer assets. Although the Bank has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent upon economic conditions in Southwestern Indiana.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, Bank, FFSL, FBEI, FFSB Financial and WRSC. All significant intercompany accounts and transactions have been eliminated in consolidation.

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. In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
June 30, 2008 and 2007
(Table Dollar Amounts in Thousands, Except Share Data)

Cash Equivalents and Cash Concentration

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents. The Bank maintains cash in bank deposit accounts, which at times may exceed federally insured limits. At June 30, 2008, the Company's cash accounts exceeded federally insured limits by approximately \$17,637,000.

Trading Activities

Securities that are held principally for resale in the near term are recorded in the trading assets account at fair value with changes in fair value recorded in earnings. Interest and dividends are included in net interest income.

Quoted market prices, when available, are used to determine the fair value of trading instruments. If quoted market prices are not available, then fair values are estimated using pricing models, quoted prices of instruments with similar characteristics or discounted cash flows.

Securities

Available-for-sale securities, which include any security for which the Company has no immediate plan to sell but which may be sold in the future, are carried at fair value. Unrealized gains and losses are recorded, net of related income tax effects, in other comprehensive income.

Held-to-maturity securities, which include any security for which the Company has the positive intent and ability to hold until maturity, are carried at historical cost adjusted for amortization of premiums and accretion of discounts.

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

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 any charge-offs, the allowance for loan losses, any deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans. Interest income is reported on the interest method and includes amortization of net deferred loan fees and costs over the loan term. Generally, loans are placed on nonaccrual status at 90 days past due and interest is considered a loss, unless the loan is well-secured and in the process of collection.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
June 30, 2008 and 2007
(Table Dollar Amounts in Thousands, Except Share Data)

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

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. 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.

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.

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 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.

Large groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
June 30, 2008 and 2007
(Table Dollar Amounts in Thousands, Except Share Data)

Automobile Loan Securitization

In 2005, the Bank used the securitization of automobile loans as a source of funding and as a mechanism to reduce its volume of automobile loans. Automobile loans were transferred into a qualifying special purpose entity (SPE) then to a trust in a transaction that is effective under applicable banking rules and regulations to legally isolate the assets from the Bank. Where the transferor is a depository institution such as the Bank, legal isolation is accomplished through compliance with specific rules and regulations of the relevant regulatory authorities. Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, (SFAS 140) requires, for certain transactions completed after the initial adoption date, a “true sale” analysis of the treatment of the transfer under state law as if the Bank were a debtor under the bankruptcy code. A “true sale” legal analysis includes several legally relevant factors, such as the nature and level of recourse to the Bank and the nature of retained servicing rights. The analytical conclusion as to a true sale is never absolute and unconditional, but contains qualifications based on the inherent equitable powers of a bankruptcy court, as well as the unsettled state of the common law. Once the legal isolation test has been met under SFAS 140, other factors concerning the nature and extent of the Bank’s control over the transferred assets are taken into account in order to determine whether derecognition of assets is warranted, including whether the SPE has complied with rules concerning qualifying special purpose entities.

A legal opinion was obtained for the automobile loan securitization transaction in 2005, which was structured as a two-step securitization. While noting that the transaction fell within the meaning of a securitization under the FDIC regulation, Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation (Securitization Rule), in accordance with accounting guidance, an analysis was also rendered under state law as if the Bank was a debtor under the bankruptcy code. The true sale opinion provides reasonable assurance that the purchased assets would not be characterized as the property of the Bank’s receivership or conservatorship estate in the event of insolvency and also states the Bank would not be required to substantively consolidate the assets and liabilities of the purchaser SPE with those of the Bank upon such event.

In a securitization, the trust issues beneficial interests in the form of senior and subordinated asset-backed securities backed or collateralized by the assets sold to the trust. The senior classes of the asset-backed securities typically receive investment grade credit ratings at the time of issuance. These ratings are generally achieved through the creation of lower-rated subordinated classes of asset-backed securities, the retention of subordinated interests by the Bank or its affiliate, and, possibly, the acquisition of a financial guarantee policy. The subordinated interests retained by the Bank or its affiliate may take the form of seller certificates, subordinated tranches, cash reserve balances, servicing assets and interest-only strips representing the net cash flows generated by the assets after all contractual payments and other obligations, including servicing fees, have been satisfied.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
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In accordance with SFAS 140, securitized automobile loans are removed from the balance sheet and a net gain or loss is recognized as a noninterest component of income at the time of the sale. Transaction costs associated with the automobile loan securitization are recognized as a component of the gain or loss.

Retained interests in the subordinated tranches and interest-only strips are recorded at their fair value and accounted for as available-for-sale securities with subsequent adjustments to fair value recorded through other comprehensive income within stockholders' equity or in other noninterest expense in the income statement if the fair value has declined below the carrying amount and such decline has been determined to be other than temporary. At June 30, 2007, the retained interests are included in other assets in the consolidated balance sheets. At June 30, 2007, management determined that the unrealized loss on the retained interest was other than temporary and recorded an impairment charge of approximately \$271,000 in other noninterest expense. Beginning July 1, 2007, management accounts for the retained interest as a trading security and records changes in fair value through the income statement. The Bank uses assumptions and estimates in accordance with SFAS 140 for determining the fair value allocated to the retained interests at the time of sale. These assumptions and estimates include projections concerning rates charged to customers, the expected life of the receivables, credit loss experience, loan repayment rates, the cost of funds and discount rates commensurate with the risks involved.

On a quarterly basis, management reviews the historical performance of the retained interest and the assumptions used to project future cash flows. If past performance and future expectations dictate, assumptions are revised and the present value of future cash flows is recalculated. Refer to the automobile loan securitization footnote for further analysis of the assumptions used in the determination of fair value.

The retained interest represents the Bank's maximum loss exposure with respect to securitization transactions. The investors in the debt securities issued by the trust have no further recourse against the Bank if cash flows generated by the securitized automobile loans are inadequate to service the obligations of the trust.

Premises and Equipment

Depreciable assets are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are capitalized and depreciated using the straight-line method over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter.

Federal Home Loan Bank Stock

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.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
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(Table Dollar Amounts in Thousands, Except Share Data)

Goodwill

Goodwill is tested annually for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value. Subsequent increases in goodwill value are not recognized in the financial statements.

Intangible Assets

Intangible assets consist of core deposit intangibles associated with acquisitions and are being amortized over approximately 10 years on the straight-line basis. The intangible assets are periodically evaluated as to the recoverability of their carrying value.

Mortgage and Consumer Servicing Rights

Mortgage and consumer servicing rights on originated loans that have been sold are initially recorded at fair value. Capitalized servicing rights are amortized in proportion to and over the period of estimated servicing revenues. Impairment of mortgage and consumer loan servicing rights is assessed based on the fair value of those rights. Fair values are estimated using discounted cash flows based on a current market interest rate. For purposes of measuring impairment, the rights are stratified based on the predominant risk characteristics of the underlying loans. The predominant characteristic currently used for stratification is type of loan. The amount of impairment recognized is the amount by which the capitalized servicing rights for a stratum exceed their fair value.

Income Taxes

Deferred tax liabilities and assets are recognized for the tax effects of differences between the financial statement and tax bases of assets and liabilities. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that a deferred tax asset will not be realized. The Company files consolidated income tax returns with its subsidiaries.

Stock Options

At June 30, 2008, the Company has a stock-based employee compensation plan, which is described more fully in Note 19. The Company accounts for this plan under the recognition and measurement principles of SFAS 123R, *Share-Based Payment*, (SFAS 123R).

Reclassifications

Certain reclassifications have been made to the 2007 financial statements to conform to the 2008 financial statement presentation. These reclassifications had no effect on net earnings.

First Bancorp of Indiana, Inc.
Notes to Consolidated Financial Statements
June 30, 2008 and 2007
(Table Dollar Amounts in Thousands, Except Share Data)

Note 2: Acquisition of Home Building Bancorp, Inc.

On October 1, 2006, the Company acquired 100% of the outstanding common stock of Home Building Bancorp, Inc. (Home Building). The results of Home Building's operations have been included in the consolidated financial statements since that date. Home Building is a savings institution located in Washington, Indiana. As a result of the acquisition, the Company will have an opportunity to increase its deposit base and reduce transaction costs. The Company also expects to reduce costs through economies of scale.

The aggregate purchase price was \$11.3 million, including \$5.6 million of cash and common stock valued at \$5.4 million.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

Cash and cash equivalents	\$ 3,356
Interest-bearing time deposits	5,638
Investment securities	10,032
Loans	39,581
Premises and equipment	618
Core deposits	942
Goodwill	4,443
Other assets	<u>1,496</u>
 Total assets acquired	 <u>66,106</u>
 Deposits	 44,540
Long-term debt	8,993
Other liabilities	<u>1,255</u>
 Total liabilities assumed	 <u>54,788</u>
 Net assets acquired	 <u>\$ 11,318</u>

The only significant intangible asset acquired was the core deposit base, which has a useful life of approximately 10 years and will be amortized using the straight-line method. None of the goodwill is expected to be deductible for tax purposes.

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The following proforma disclosures, including the effect of the purchase accounting adjustments, depict the results of operations as though the merger had taken place as follows:

	Year Ended June 30, 2007
Net interest income	\$ 7,627
Net income	\$ 521

Note 3: Restriction on Cash and Due From Banks

The Bank is required to maintain reserve funds in cash and/or on deposit with the Federal Reserve Bank. The reserve required at June 30, 2008, was \$2,315,000.

Note 4: Trading Activities

The fair value of trading assets are as follows:

	June 30	
	2008	2007
Trading assets, at fair value		
Retained interest in auto loan securitization	\$ <u>1,251</u>	\$ <u>-</u>

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Note 5: Investments

Available-for-Sale Securities

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

	June 30, 2008			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
Mortgage-backed securities	\$ 52,429	\$ 147	\$ (1,462)	\$ 51,114
U.S. Government agencies	22,747	40	(359)	22,428
Corporate obligations	4,242	-	(903)	3,339
Equity securities	<u>232</u>	<u>-</u>	<u>(78)</u>	<u>154</u>
	<u>\$ 79,650</u>	<u>\$ 187</u>	<u>\$ (2,802)</u>	<u>\$ 77,035</u>
	June 30, 2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
Mortgage-backed securities	\$ 33,691	\$ 54	\$ (817)	\$ 32,928
U.S. Government agencies	28,060	-	(369)	27,691
Corporate obligations	<u>4,480</u>	<u>25</u>	<u>(3)</u>	<u>4,502</u>
	<u>\$ 66,231</u>	<u>\$ 79</u>	<u>\$ (1,189)</u>	<u>\$ 65,121</u>

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The amortized cost and fair value of available-for-sale securities at June 30, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale	
	Amortized Cost	Fair Value
Within one year	\$ 1,608	\$ 1,531
One to five years	985	1,011
Five to ten years	-	-
After ten years	<u>24,628</u>	<u>23,379</u>
	27,221	25,921
Mortgage-backed securities	<u>52,429</u>	<u>51,114</u>
	<u>\$ 79,650</u>	<u>\$ 77,035</u>

Held-to-Maturity Securities

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

	June 30, 2008			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
Mortgage-backed securities	\$ 1,909	\$ 41	\$ -	\$ 1,950
Municipal bonds	11,828	36	(174)	11,690
Collateralized auto obligations	<u>979</u>	<u>7</u>	<u>-</u>	<u>986</u>
	<u>\$ 14,716</u>	<u>\$ 84</u>	<u>\$ (174)</u>	<u>\$ 14,626</u>

	June 30, 2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Approximate Fair Value
Mortgage-backed securities	\$ 2,568	\$ 25	\$ -	\$ 2,593
Municipal bonds	11,480	-	(315)	11,165
Collateralized auto obligations	<u>929</u>	<u>-</u>	<u>(15)</u>	<u>914</u>
	<u>\$ 14,977</u>	<u>\$ 25</u>	<u>\$ (330)</u>	<u>\$ 14,672</u>

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The amortized cost and fair value of held-to-maturity securities at June 30, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Held to Maturity	
	Amortized Cost	Fair Value
Within one year	\$ 1,364	\$ 1,374
One to five years	452	457
Five to ten years	388	383
Over ten years	10,603	10,462
	12,807	12,676
Mortgage-backed securities	1,909	1,950
	\$ 14,716	\$ 14,626

Securities with a carrying value of approximately \$47,084,000 at June 30, 2008, and \$45,384,000 at June 30, 2007, were pledged as collateral to secure FHLB advances and repurchase agreements.

There were no sales of securities during 2008 and 2007.

There were no transfers of securities between classifications during 2008 and 2007.

Certain investments in debt securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at June 30, 2008 and 2007, was \$62,681,000 and \$65,900,000, respectively, which is approximately 68% and 82% of the Company's available-for-sale and held-to-maturity investment portfolios, respectively.

Based on evaluation of available evidence, including recent changes in market interest rates and information from regulatory filings, management believes the declines in fair value for these securities are temporary.

Should the impairment of any these 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.

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The following tables show the 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.

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2008						
U.S. Government agencies	\$ 19,410	\$ (359)	\$ -	\$ -	\$ 19,410	\$ (359)
Mortgage-backed securities	26,949	(1,087)	5,612	(375)	32,561	(1,462)
Municipal bonds	7,960	(174)	-	-	7,960	(174)
Corporate obligations	2,499	(899)	97	(4)	2,596	(903)
Equity securities	<u>154</u>	<u>(78)</u>	<u>-</u>	<u>-</u>	<u>154</u>	<u>(78)</u>
Total temporarily impaired securities	<u>\$ 56,972</u>	<u>\$ (2,597)</u>	<u>\$ 5,709</u>	<u>\$ (379)</u>	<u>\$ 62,681</u>	<u>\$ (2,976)</u>

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2007						
U.S. Government agencies	\$ 9,810	\$ (77)	\$ 17,881	\$ (292)	\$ 27,691	\$ (369)
Mortgage-backed securities	1,723	(6)	23,929	(811)	25,652	(817)
Municipal bonds	6,466	(166)	4,700	(149)	11,166	(315)
Corporate obligations	99	(1)	378	(2)	477	(3)
Collateralized loan obligations	<u>914</u>	<u>(15)</u>	<u>-</u>	<u>-</u>	<u>914</u>	<u>(15)</u>
Total temporarily impaired securities	<u>\$ 19,012</u>	<u>\$ (265)</u>	<u>\$ 46,888</u>	<u>\$ (1,254)</u>	<u>\$ 65,900</u>	<u>\$ (1,519)</u>

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Note 6: Loans and Allowance for Loan Losses

Categories of loans at June 30 include:

	<u>2008</u>	<u>2007</u>
Mortgage loans		
One-to-four family	\$ 95,976	\$ 102,293
Construction	4,501	3,420
Commercial and multi-family	29,305	28,740
Commercial business loans	19,554	17,233
Consumer loans	73,368	76,971
Consumer lines of credit	5,840	5,310
Loans to depositors secured by savings	<u>299</u>	<u>317</u>
 Total loans	 228,843	 234,284
 Deferred loan (fees) costs, net	 273	 283
Undisbursed portion of construction loans	(1,097)	(265)
Allowance for loan losses	<u>(1,545)</u>	<u>(1,065)</u>
 Net loans	 <u>\$ 226,474</u>	 <u>\$ 233,237</u>

Activity in the allowance for loan losses was as follows:

	<u>2008</u>	<u>2007</u>
Balance, beginning of year	\$ 1,065	\$ 836
Provision charged to expense	1,090	400
Allowance added in acquisition	-	266
Losses charged off, net of recoveries of \$93 for 2008 and \$118 for 2007	<u>(610)</u>	<u>(437)</u>
 Balance, end of year	 <u>\$ 1,545</u>	 <u>\$ 1,065</u>

Loans delinquent 90 days or more and still accruing totaled \$103,000 and \$14,000 at June 30, 2008 and 2007, respectively. Nonaccruing loans at June 30, 2008 and 2007, were \$354,000 and \$311,000, respectively.

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There was one impaired commercial relationship totaling approximately \$905,000 at June 30, 2008. An allowance for loan losses of \$500,000 relates to this impaired loan at June 30, 2008. There were no impaired loans at June 30, 2008 or 2007, having no related allowance for loan losses.

Interest of \$88,000 was recognized on average impaired loans of \$947,000 during 2008. Interest of \$84,000 was recognized on impaired loans on a cash basis during 2008.

Note 7: Automobile Loan Securitization

The Bank completed an automobile loan securitization transaction in June 2005. The transaction resulted in the sale of \$47.7 million of AAA rated class A notes, \$2.0 million of A rated class B notes and \$1.0 million of BBB rated class C notes.

A summary of the components of managed loans, which represents both owned and securitized loans, follow. The automobile loans presented represent the managed portfolio of indirect prime automobile loans.

	June 30, 2008	
	Principal Balance	Loans Past Due Over 30 Days
Total managed automobile loans	\$ 84,423	\$ 2,113
Less: automobile loans securitized	7,175	312
Less: automobile loans sold to other investors	4,533	64
Total automobile loans held in portfolio	\$ 72,715	\$ 1,737

Certain cash flows received from the securitization trust follow:

	2008	2007
Servicing fees received	\$ 58	\$ 115

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The Bank estimated the fair value of the retained interest at the date of the transfer and during the period of the transaction based on a discounted cash flow analysis. The Bank receives annual servicing fees based on the loan balances outstanding, the rights to future cash flows arising after investors in the securitization trust have received their contractual return and after certain administrative costs of operating the trust. These cash flows are estimated over the life of the loans using prepayment, default and interest rate assumptions that market participants would use for financial instruments subject to similar levels of prepayment, credit and interest rate risk.

A summary of the fair values of the interest-only strips and servicing assets retained, key economic assumptions used to arrive at the fair values and the sensitivity of the June 30, 2008, fair values to immediate 10% and 20% adverse changes in those assumptions follows. The sensitivities are hypothetical. Changes in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of the retained interests is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments and increased credit losses), which might either magnify or counteract the sensitivities.

	Fair Value	Weighted-average Life (in months)	Monthly Prepayment Speed (% ABS)	Expected Cumulative Credit Losses	Annual Discount Rate	Weighted-average Coupon
Interest-only strip						
As of the date of securitization	\$ 2,985	54	1.60%	0.65%	8.0%	7.34%
As of June 30, 2008	\$ 1,251	25	1.60%	1.00%	8.0%	7.28%
Decline in fair value of 10% adverse change	\$ -	\$ -	\$ 8	\$ 2	\$ 12	\$ -
Decline in fair value of 20% adverse change	\$ -	\$ -	\$ 14	\$ 5	\$ 24	\$ -
Servicing asset						
As of the date of securitization	\$ 170	54	1.60%	0.65%	8.0%	-
As of June 30, 2008*	\$ 25	25	1.60%	1.00%	8.0%	-
Decline in fair value of 10% adverse change	\$ -	\$ -	\$ 2	\$ -	\$ -	\$ -
Decline in fair value of 20% adverse change	\$ -	\$ -	\$ 3	\$ -	\$ -	\$ -

*Carrying value of the servicing asset approximated fair value at June 30, 2008

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Note 8: Premises and Equipment

Major classifications of premises and equipment, stated at cost, are as follows:

	<u>2008</u>	<u>2007</u>
Land	\$ 2,108	\$ 2,108
Buildings	7,404	7,343
Equipment	2,298	2,140
Construction in progress	<u>81</u>	<u>-</u>
	11,891	11,591
Less accumulated depreciation	<u>2,726</u>	<u>2,268</u>
Net premises and equipment	<u>\$ 9,165</u>	<u>\$ 9,323</u>

Note 9: Goodwill

The changes in the carrying amount of goodwill for the years ended June 30 were:

	<u>2008</u>	<u>2007</u>
Balance, beginning of year	\$ 6,229	\$ 1,786
Acquisition of Home Building Bancorp	<u>-</u>	<u>4,443</u>
Balance, end of year	<u>\$ 6,229</u>	<u>\$ 6,229</u>

Note 10: Other Intangible Assets

The carrying basis and accumulated amortization of recognized intangible assets at June 30 were:

	<u>2008</u>		<u>2007</u>	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Core deposit intangible	\$ <u>1,474</u>	\$ <u>(697)</u>	\$ <u>1,474</u>	\$ <u>(580)</u>

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Amortization expense for each of the years ended June 30, 2008 and 2007, was \$117,100 and \$134,400, respectively. Estimated amortization expense for each of the following five years is:

2009	\$	94
2010		94
2011		94
2012		94
2013		94
Thereafter		<u>307</u>
	\$	<u>777</u>

Note 11: Loan Servicing

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balance of mortgage loans serviced for others was \$43,036,000 and \$39,955,000 at June 30, 2008 and 2007, respectively. Contractually specified servicing fees, late fees and “ancillary fees” of approximately \$52,000 and \$55,000 are included in loan servicing fees in the statements of income at June 30, 2008 and 2007, respectively.

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in demand deposits, were approximately \$455,000 and \$312,000 at June 30, 2008 and 2007, respectively.

The aggregate fair value of capitalized mortgage servicing rights at June 30, 2008 and 2007, approximated carrying value. A valuation model that calculates the present value of future cash flows was used to estimate fair value. For purposes of measuring impairment, risk characteristics including product type, investor type and interest rates were used to stratify the originated mortgage servicing rights.

	<u>2008</u>	<u>2007</u>
Mortgage servicing rights		
Balances, beginning of year	\$ 438	\$ 402
Servicing rights capitalized	89	78
Amortization of servicing rights	<u>(54)</u>	<u>(42)</u>
Balance, end of year	\$ <u>473</u>	\$ <u>438</u>

Consumer loans are also serviced for others and are not included in the accompanying consolidated balance sheets. The unpaid principal balances of consumer loans serviced for others totaled \$11,707,000 and \$25,098,000 at June 30, 2008 and 2007, respectively.

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The aggregate fair value of capitalized consumer loan servicing rights at June 30, 2008 and 2007, approximated carrying value. A valuation model that calculates the present value of future cash flows was used to estimate fair value. For purposes of measuring impairment, risk characteristics including product type, investor type and interest rates were used to stratify the originated consumer loan servicing rights.

	<u>2008</u>	<u>2007</u>
Consumer servicing rights		
Balance, beginning of year	\$ 277	\$ 370
Servicing rights capitalized	28	211
Amortization of servicing rights	<u>(183)</u>	<u>(304)</u>
Balance, end of year	<u>\$ 122</u>	<u>\$ 277</u>

Note 12: Other Assets and Other Liabilities

	<u>2008</u>	<u>2007</u>
Other assets		
Interest receivable		
Investment securities	\$ 941	\$ 750
Loans	928	1,052
Cash surrender value of life insurance	5,534	5,332
Investment in limited partnership	-	76
Net deferred tax asset	1,174	539
Retained interest in auto loan securitization	1,441	1,601
Mortgage and consumer servicing rights	595	715
Prepaid expenses and other	<u>2,880</u>	<u>2,115</u>
Total other assets	<u>\$ 13,493</u>	<u>\$ 12,180</u>
Other liabilities		
Interest payable		
Deposits	\$ 1,104	\$ 896
Other borrowings	237	181
Deferred directors' fees and officers' compensation	695	784
Payments due investors on sold consumer loans	322	624
Accounts payable – dealer fees	100	167
Accrued expenses and other	<u>2,584</u>	<u>1,698</u>
Total other liabilities	<u>\$ 5,042</u>	<u>\$ 4,350</u>

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The investment in limited partnership of \$0 and \$76,100 at June 30, 2008 and 2007, respectively, represents a 40% equity interest in Vann Park II, L.P., a limited partnership organized to build, own and operate a 44-unit apartment complex. The Bank has recorded equity in the losses of the partnership totaling \$(76,100) and \$(1,200) for the years ended June 30, 2008 and 2007, respectively.

Note 13: Deposits

	<u>2008</u>	<u>2007</u>
Demand deposits	\$ 71,463	\$ 37,283
Savings deposits	28,739	30,554
Certificates of deposit of \$100,000 or more	74,869	121,977
Other certificates of deposit	<u>68,982</u>	<u>61,420</u>
Total deposits	\$ <u>244,053</u>	\$ <u>251,234</u>

At June 30, 2008, the scheduled maturities of time deposits are as follows:

2009	\$ 109,121
2010	23,097
2011	8,832
2012	1,734
2013	633
Thereafter	<u>434</u>
	<u>\$ 143,851</u>

Time deposits at June 30, 2008 and 2007, included brokered deposits of \$19,768,000 and \$79,439,000, respectively.

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Note 14: Income Taxes

The provision for income taxes includes these components:

	<u>2008</u>	<u>2007</u>
Taxes currently payable		
Federal	\$ 31	\$ 103
State	(20)	33
Deferred income taxes		
Federal	83	(67)
State	<u>13</u>	<u>(10)</u>
Income tax expense	<u>\$ 107</u>	<u>\$ 59</u>

A reconciliation of income tax expense at the statutory rate to the Company's actual income tax expense is shown below:

	<u>2008</u>	<u>2007</u>
Computed at the statutory rate (34%)	\$ 319	\$ 196
Increase (decrease) resulting from		
State income taxes, net of federal benefit	(5)	16
Cash surrender value of life insurance	(69)	(69)
Tax-exempt interest	(149)	(146)
Nondeductible expenses	51	71
Other	<u>(40)</u>	<u>(9)</u>
Actual tax expense	<u>\$ 107</u>	<u>\$ 59</u>

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The tax effects of temporary differences related to deferred taxes shown on the balance sheets were:

	2008	2007
Deferred tax assets		
Differences in accounting for loan losses	\$ 579	\$ 399
Deferred compensation and directors' fees	332	354
Exercise of nonqualified options	-	58
Unrealized losses on available-for-sale securities	966	419
Accrued vacation	64	64
Loss on impairment	141	102
Other adjustments from acquisition	47	84
State net operating loss carryforward	-	75
Other	178	14
	2,307	1,569
Deferred tax liabilities		
Differences in depreciation methods	(169)	(70)
Federal Home Loan Bank dividends	(160)	(160)
Mortgage servicing rights	(177)	(164)
Consumer servicing rights	(10)	(26)
State taxes	(8)	(11)
Deposit-based intangibles	(193)	(241)
Goodwill	(312)	(264)
Prepaid intangibles	(104)	(94)
	(1,133)	(1,030)
Net deferred tax asset	\$ 1,174	\$ 539

Retained earnings at June 30, 2008 and 2007, included approximately \$4,102,000 for which no deferred income tax liability has been recognized. This amount represents an allocation of income to bad debt deductions for tax purposes only. Reductions of amounts so allocated for purposes other than tax, bad debt losses or adjustment arising from carryback of net operating losses would create income for tax purposes only, which income would be subject to the then-current corporate income tax rate. The unrecorded deferred income tax liability on the above amount was approximately \$1,395,000.

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Note 15: Borrowings

Borrowings consisted of the following components:

	2008	2007
FHLB advances		
Fixed rate of 5.31%, due in June 2008	\$ -	\$ 4,000
Fixed rate of 4.35%, due in September 2015	10,000	10,000
Fixed rate of 3.70%, due in September 2015	10,000	10,000
Fixed rate of 4.14%, due in August 2017	5,000	-
Fixed rate of 3.91%, due in September 2017	5,000	-
Fixed rate of 3.32%, due in December 2017	5,000	-
Fixed rate of 3.49%, due in December 2017	5,000	-
Fixed rate of 3.43%, due in December 2017	5,000	-
Fixed rate of 5.37%, due in February 2011	10,000	10,000
Fixed rate of 4.83%, due in July 2011	10,000	10,000
Fixed rate of 4.61%, due in June 2017	15,000	15,000
Fixed rate of 4.98%, due in December 2010	2,000	2,000
Floating at three-month London Interbank Offered Rate (LIBOR), due in March 2008	-	2,500
Fixed rate of 3.29%, due in August 2007	-	500
Fixed rate of 4.30%, due in June 2010	500	500
Structured Repurchase Agreement 4.46%, due in July 2017	8,000	8,000
Junior subordinated debentures, 6.905%, due in September 2037	5,155	-
Discount on purchased borrowings	-	(4)
Total borrowings	\$ 95,655	\$ 72,496

The FHLB advances are secured by a blanket pledge of qualifying first-mortgage loans totaling \$80,474,000 and investment securities with market values totaling \$47,084,000 at June 30, 2008.

The repurchase agreement is secured by U.S. agency securities and such collateral is held by a third-party safekeeping agent. The maximum amount outstanding at any given month end during 2008 was \$8,000,000 and the monthly average of such agreements totaled \$8,000,000 during 2008. The maximum amount outstanding at any given month end during 2007 was \$8,000,000 and the monthly average of such agreements totaled \$3,670,000 during 2007.

The repurchase agreement at June 30, 2008, had a maturity date of July 17, 2017, with a rate of 4.46%, with options to terminate the transaction by the counterparty.

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The junior subordinated debentures were issued to the Trust on August 1, 2007. The Trust is wholly owned by the Company. The debentures mature in September 2037 and bear a fixed interest rate of 6.905% for the first five years and 141 basis points over the three-month LIBOR rate for the remaining term. Interest is payable on a quarterly basis.

Aggregate annual maturities of borrowings at June 30, 2008, were:

2009	\$	-
2010		500
2011		12,000
2012		10,000
2013		-
Thereafter		<u>73,155</u>
	\$	<u>95,655</u>

On April 25, 2008, the board of directors unanimously approved and the Company executed a 1-for-300 reverse stock split. The reverse stock split was immediately followed by a 300-for-1 forward stock split. The Company then terminated the registration of its common stock by filing Form 15E with the Securities and Exchange Commission. This resulted in the delisting of its shares on the NASDAQ. All share and per share data in the accompanying financial statements has been adjusted for the above stock splits.

Note 16: Other Comprehensive Income (Loss)

Other comprehensive income (loss) components and related taxes were as follows:

	<u>2008</u>	<u>2007</u>
Unrealized gains (losses) on securities available for sale and equity securities	\$ (1,512)	\$ 1,314
Reclassification for realized amount included in income	<u>-</u>	<u>271</u>
Other comprehensive income (loss) before tax effect	(1,512)	1,585
Tax expense (benefit)	<u>(545)</u>	<u>609</u>
Other comprehensive income (loss)	\$ <u>(967)</u>	\$ <u>976</u>

The components of other comprehensive income are the unrealized gains (losses) on securities available for sale (including assets available for sale in connection with the automobile loan securitization).

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Note 17: Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of June 30, 2008 and 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of June 30, 2008, the most recent notification from the regulators categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based and Tier I leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Bank's category.

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The Bank's actual capital amounts and ratios are also presented in the table.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of June 30, 2008						
Total capital (to risk-weighted assets)	\$ 28,136	11.99%	\$ 18,774	8.00%	\$ 23,468	10.00%
Tier I capital (to risk-weighted assets)	\$ 28,084	11.65%	\$ 9,387	4.00%	\$ 14,081	6.00%
Core capital (to adjusted total assets)	\$ 28,084	7.60%	\$ 14,773	4.00%	\$ 18,467	5.00%
Core capital (to adjusted tangible assets)	\$ 28,084	7.60%	\$ 7,384	2.00%	N/A	N/A
Tangible capital (to adjusted total assets)	\$ 27,962	7.57%	\$ 5,540	1.50%	N/A	N/A
As of June 30, 2007						
Total capital (to risk-weighted assets)	\$ 25,680	10.81%	\$ 19,010	8.00%	\$ 23,763	10.00%
Tier I capital (to risk-weighted assets)	\$ 25,675	10.40%	\$ 9,505	4.00%	\$ 14,258	6.00%
Core capital (to adjusted total assets)	\$ 25,675	7.23%	\$ 14,200	4.00%	\$ 17,750	5.00%
Core capital (to adjusted tangible assets)	\$ 25,675	7.23%	\$ 7,100	2.00%	N/A	N/A
Tangible capital (to adjusted total assets)	\$ 25,398	7.16%	\$ 5,321	1.50%	N/A	N/A

The Bank is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. Current regulations allow the Bank to pay dividends to the Company not exceeding net income for the current year plus those for the preceding two years. The Bank normally restricts dividends to a lesser amount because of the need to maintain an adequate capital structure.

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Note 18: Employee Benefit Plans

401(k) Plan

The Bank has a retirement savings Section 401(k) plan in which substantially all employees may participate. The Bank's expense for the plan was \$8,300 and \$111,900 for 2008 and 2007, respectively. Due to the withdrawal from the multi-employer pension plan, the Bank began providing a discretionary match of employees' contributions at the rate of 100% of the first 6% of base salary contributed by participants effective July 1, 2004. The Company match ceased on May 31, 2007.

Supplemental Retirement Plan

The Bank also has supplemental retirement plan arrangements for the benefit of certain officers. These arrangements are funded by life insurance contracts which have been purchased by the Bank. The Bank's expense for the plan was \$161,300 and \$145,600 for the years ended June 30, 2008 and 2007, respectively. The Bank also established deferred compensation arrangements with certain directors whereby; in lieu of currently receiving fees, the directors or their beneficiaries will be paid benefits for an established period following the director's retirement or death. These arrangements are also funded by life insurance contracts which have been purchased by the Bank. The Bank's expense for the plan was \$49,400 and \$65,900 for the years ended June 30, 2008 and 2007, respectively.

Employee Stock Ownership Plan

In 1999, the Bank established an employee stock ownership plan for the benefit of substantially all of its employees. At June 30, 1999, the ESOP had borrowed \$874,000 from the Company and used those funds to acquire 87,400 shares of the Company's stock at \$10 per share. During 2000, the ESOP borrowed an additional \$980,411 from the Company and used those funds to acquire 94,392 shares of the Company's stock at an average price of \$10.39 per share.

The Bank makes annual contributions to the ESOP equal to the ESOP's debt service less dividends received by the ESOP. All dividends received by the ESOP are used to pay debt service. The ESOP shares initially were pledged as collateral for its debt. As the debt is repaid, shares are released from collateral and allocated to plan participants, based on the proportion of debt service paid in the year to total expected debt service. The Bank accounts for its ESOP in accordance with Statement of Position 93-6. Accordingly, the shares pledged as collateral are reported as unallocated ESOP shares in the balance sheets. As shares are committed to be released from collateral, the Bank reports compensation expense equal to the current fair value of the shares. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings; dividends on unallocated ESOP shares are recorded as a reduction of debt and accrued interest.

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Stock totaling 15,150 shares for each of the years 2008 and 2007, with an average fair value of \$13.27 and \$18.23, respectively, per share, were released or committed to be released, resulting in ESOP compensation expense of approximately \$202,400 and \$276,000, respectively. Shares held by the ESOP at June 30 were as follows:

	<u>2008</u>	<u>2007</u>
Allocated shares	106,902	95,006
Shares committed to be released	1,823	1,415
Unreleased shares	<u>45,429</u>	<u>60,583</u>
Total ESOP shares	<u>154,154</u>	<u>157,004</u>
Fair value of unallocated shares at June 30	\$ <u>465,647</u>	\$ <u>912,986</u>

Management Recognition Plan

On April 25, 2000, the Company established a Management Recognition Plan (MRP) to enable the Company to retain executive personnel of experience and ability in key positions of responsibility. Under the MRP, the board of directors was authorized to acquire and grant 90,896 shares of the Company's common stock. The funds used to acquire these shares were contributed by the Bank. Participants vested in shares awarded under the MRP over five years at the rate of 20% per year. As of June 30, 2000, all 90,896 shares authorized under the plan had been granted. As of June 30, 2005, all 90,896 shares had vested. No expense was recognized under the MRP during the years ended June 30, 2008 or 2007.

Note 19: Stock Option Plan

The Company has a shareholder-approved stock option plan under which 327,240 shares were reserved for future issuance by the Company to directors and employees of the Company and the Bank. The plan has a term of 10 years, after which no awards may be made, unless earlier terminated by the board of directors. During 2008 and 2007, no options were granted.

Under the Company's stock option plan, the Company grants selected executives and other key employees stock option awards which vest according to a schedule fixed by a committee made up of two or more "disinterested" directors of the Company. The options become fully exercisable upon vesting. The Company generally issues shares from treasury stock to satisfy exercises of stock options.

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The following is a summary of the status of the Company's stock option plan and changes in that plan as of and for the year ended June 30, 2008.

Options	Shares	Weighted- average Exercise Price	Weighted- average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding, beginning of year	89,563	\$ 13.02		
Granted	-	\$ -		
Exercised	(6,852)	\$ 9.13		
Forfeited/expired	<u>-</u>	\$ -		
Outstanding, end of year	<u>82,711</u>	\$ 13.35	<u>3.6 years</u>	<u>N/A</u>
Options exercisable at year end	<u>82,711</u>	\$ 13.35	<u>3.6 years</u>	<u>N/A</u>

There were no options granted during the years ended June 30, 2008 or 2007. The total intrinsic value of options exercised during the years ended June 30, 2008 and 2007, was \$39,000 and \$206,000, respectively.

Cash received from option exercises for the years ended June 30, 2008 and 2007, was approximately \$63,000 and \$224,000, respectively. The actual tax benefit realized for the tax deductions from option exercises totaled \$21,000 and \$77,000 for the years ended June 30, 2008 and 2007, respectively.

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Note 20: Disclosures About Fair Value of Financial Instruments

The following table presents estimated fair values of the Company's financial instruments. The fair values of certain of these instruments were calculated by discounting expected cash flows, which method involves significant judgments by management and uncertainties. Fair value is the estimated amount at which financial assets or liabilities could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Because no market exists for certain of these financial instruments and because management does not intend to sell these financial instruments, the Company does not know whether the fair values shown below represent values at which the respective financial instruments could be sold individually or in the aggregate.

	June 30, 2008		June 30, 2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	\$ 24,397	\$ 24,397	\$ 14,851	\$ 14,851
Interest-bearing deposits	495	495	1,616	1,616
Available-for-sale securities	77,035	77,035	65,121	65,121
Held-to-maturity securities	14,716	14,626	14,977	14,672
Loans, net of allowance for loan losses	226,474	227,239	233,237	232,294
Interest receivable	1,869	1,869	1,802	1,802
FHLB stock	4,565	4,565	4,565	4,565
Retained interest in securitized loans	1,441	1,441	1,601	1,601
Financial liabilities				
Deposits	\$ 244,053	\$ 246,090	\$ 251,234	\$ 250,585
Borrowings	95,655	97,952	72,496	71,713
Advances from borrowers for taxes and insurance	1,021	1,021	695	695
Interest payable	1,341	1,341	1,077	1,077
Unrecognized financial instruments, net of contract amount				
Commitments to extend credit	-	-	-	-
Letters of credit	-	-	-	-
Lines of credit	-	-	-	-

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The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

Cash and Cash Equivalents

For these short-term instruments, the carrying amount approximates fair value.

Interest-bearing Deposits

The fair value of interest-bearing time deposits approximates carrying value.

Investment Securities

Fair values for investment securities equal quoted market prices, if available. If quoted market prices are not available, fair value is estimated based on quoted market prices of similar securities.

Loans

The fair value of loans is estimated by discounting the future cash flows using the current 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.

FHLB Stock

The fair value of FHLB stock is based upon the price at which it may be resold to the FHLB.

Retained Interest in Securitized Loans

The fair value of the retained interest is estimated using a valuation model that calculates the present value of future cash flows using assumptions related to credit losses and prepayment speeds of the underlying loans.

Deposits

The fair value of demand deposits, savings accounts, NOW accounts and certain money market deposits is the amount payable on demand at the reporting date, *i.e.*, their carrying amount. 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. The carrying amount of accrued interest payable approximates its fair value.

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Advances from Borrowers for Taxes and Insurance

The fair value of advances from borrowers for taxes and insurance approximates carrying value.

Borrowings

Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate fair value of existing debt.

Commitments to Extend Credit, Letters of Credit and Lines of Credit

The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates.

Note 21: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Estimates related to the allowance for loan losses are reflected in the note regarding loans. Current vulnerabilities due to certain concentrations of credit risk are discussed in the note on commitments and credit risk.

The Company invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying financial statements.

Note 22: Commitments and Credit Risk

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 a portion of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the counterparty. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, commercial real estate and residential real estate.

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At June 30, 2008 and 2007, the Bank had outstanding commitments to originate loans aggregating approximately \$2,090,000 and \$3,168,000, respectively. The commitments extended over varying periods of time with the majority being disbursed within a one-year period. Loan commitments at fixed rates of interest amounted to \$965,000 and \$2,324,000 at June 30, 2008 and 2007, respectively, with the remainder at floating market rates.

Letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

The Bank had total outstanding letters of credit amounting to \$1,718,000 and \$2,923,000 at June 30, 2008 and 2007, respectively. The letters of credit all expire within one year.

Lines of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Lines of credit generally have fixed expiration dates. Since a portion of the line may expire without being drawn upon, the total unused lines do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, commercial real estate and residential real estate. Management uses the same credit policies in granting lines of credit as it does for on-balance sheet instruments.

At June 30, 2008 and 2007, the Bank had granted unused lines of credit to borrowers aggregating approximately \$24,222,000 and \$22,368,000, respectively.

The Bank entered into agreements with other institutions in conjunction with consumer loan sales that guarantee to the purchaser that the Bank would repurchase any consumer loans that exceed a 30-day or 60-day delinquency status, depending upon the particular agreement or whether the consumer is in bankruptcy. The original amount of the loans sold was \$35,536,000 and \$35,536,000 at June 30, 2008 and 2007, respectively, and the remaining amount outstanding totaled \$4,533,000 and \$9,380,000 at June 30, 2008 and 2007, respectively. As of June 30, 2008 and 2007, the Bank has repurchased a total of \$485,000 and \$345,000, respectively, of loans that exceeded the delinquency period since inception of the agreements.

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Note 23: Related-party Transactions

At June 30, 2008 and 2007, the Bank had loans outstanding to executive officers, directors, significant shareholders and their affiliates (related parties), in the amount of \$3,701,000 and \$3,154,000, respectively.

Additionally, the Bank had \$397,000 and \$294,000 of commitments under credit lines with related parties at June 30, 2008 and 2007, respectively.

In management's opinion, such loans and other extensions of credit and deposits were made in the ordinary course of business and were made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons. Further, in management's opinion, these loans did not involve more than normal risk of collectibility or present other unfavorable features.

Deposits from related parties held by the Bank at June 30, 2008 and 2007, totaled \$1.8 million and \$2.8 million, respectively.

Note 24: Subsequent Event

The Company has numerous investment securities for which fair value differs from book value. Four particular securities have experienced additional, significant declines in fair value subsequent to year end. As of September 30, 2008, the fair value of these four securities was approximately \$2.5 million (book value of approximately \$3.7 million) as compared to a fair value of approximately \$2.85 million at June 30, 2008. The Company's calculations indicate that no other than temporary impairment of these securities had occurred at either June 30 or September 30.

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Note 25: 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

	2008	2007
Assets		
Cash and cash equivalents	\$ 1,258	\$ 507
Investment in common stock of subsidiary	33,576	32,187
Loans to First Federal Savings Bank	520	702
Other assets	1,250	911
Investment in trust (TRUP)	155	-
Total assets	\$ 36,759	\$ 34,307
Liabilities		
Other liabilities	\$ 29	\$ 89
Subordinated debentures	5,155	-
	5,184	89
Stockholders' Equity	31,575	34,218
Total liabilities and stockholders' equity	\$ 36,759	\$ 34,307

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Condensed Statements of Income

	2008	2007
Income		
Dividends from subsidiaries	\$ -	\$ 1,500
Other income	195	82
	195	1,582
Expenses		
Interest expense	325	-
Other expenses	226	390
	551	390
Income (Loss) Before Income Tax and Equity in Undistributed Income of Subsidiary	(356)	1,192
Income tax benefit	(142)	(122)
Income (Loss) Before Equity in Undistributed Income of Subsidiary	(214)	1,314
Equity in Undistributed Income (Distributions in Excess of Equity in Income) of Subsidiary	1,018	(796)
Net Income	\$ 804	\$ 518

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Condensed Statements of Cash Flows

	2008	2007
Operating Activities		
Net income	\$ 804	\$ 518
Adjustments to reconcile net income to net cash provided by operating activities		
Distributions in excess of income (equity in undistributed income) of subsidiary	(1,018)	796
Tax benefit of employee benefit plans	-	218
Net change in		
Other assets	(341)	194
Other liabilities	<u>(60)</u>	<u>(175)</u>
Net cash provided by (used in) operating activities	<u>(615)</u>	<u>1,551</u>
Investing Activities		
Proceeds from borrowings	5,155	-
Repayments of loans to subsidiary	182	168
Purchase of equity securities	(232)	(165)
Capital injection from borrowings	<u>(1,000)</u>	<u>-</u>
Net cash provided by investing activities	<u>4,105</u>	<u>3</u>
Financing Activities		
Cash dividends	(1,375)	(1,022)
Purchase of treasury stock	(796)	(584)
Exercise of stock options	63	224
Purchase of fractional shares in connection with reverse split	<u>(631)</u>	<u>-</u>
Net cash used in financing activities	<u>(2,739)</u>	<u>(1,382)</u>
Net Change in Cash and Equivalents	751	172
Cash and Cash Equivalents, Beginning of Year	<u>507</u>	<u>335</u>
Cash and Cash Equivalents, End of Year	\$ <u>1,258</u>	\$ <u>507</u>