CLOVER LEAF FINANCIAL CORP
Form 10KSB
March 30, 2004

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB

[X]ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2003

OR

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

For the transaction period from to

Commission File Number: 0-33413

CLOVER LEAF FINANCIAL CORP.

(Exact Name of Registrant as Specified in its Charter)

DELAWARE	37-1416016
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)
200 EAST PARK STREET, EDWARDSVILLE, ILLINOIS	62025
(Address of Principal Executive Office)	(Zip Code)

(618) 656-6122

(Registrant's Telephone Number including area code)

Securities Registered Pursuant to Section 12(b) of the Act: NONE

Securities Registered Pursuant to Section 12(g) of the Act:

(Title of Class) COMMON STOCK, PAR VALUE $0.10 PER SHARE

Check whether the Registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such requirements for the past 90 days. YES X NO ___

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendments to this Form 10-KSB. [x]

The registrant's revenues for the fiscal year ended December 31, 2003 were $5.8 million.

As of February 29, 2004, there were issued and outstanding 629,950 shares of the Registrant's Common Stock. The aggregate value of the voting stock held by non-affiliates of the Registrant, computed by reference to the closing price of the Common Stock as of February 29, 2004 was $8.3 million.

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of the 2003 Annual Report to Stockholders (Parts II and IV)

2. Proxy Statement for the 2004 Annual Meeting of Stockholders (Part III)

PART I

ITEM 1. DESCRIPTION OF BUSINESS

CLOVER LEAF FINANCIAL CORP.

Clover Leaf Financial Corp. was organized at the direction of the Board of Directors of Clover Leaf Bank, SB for the purpose of acting as the stock holding company of Clover Leaf Bank. Clover Leaf Financial's assets consist primarily of the outstanding capital stock of Clover Leaf Bank and cash and investments of $1.3 million, representing a portion of the net proceeds from Clover Leaf Financial's stock offering completed December 27, 2001. At December 31, 2003, 635,950 shares of Clover Leaf Financial's common stock, par value $0.10 per share, were held by the public. Clover Leaf Financial's principal business is overseeing and directing the business of Clover Leaf Bank and investing the net stock offering proceeds retained by it. At December 31, 2003, Clover Leaf Financial had total consolidated assets of $102.7 million, total deposits of $80.5 million and stockholders' equity of $12.7 million.

Clover Leaf Financial's office is located at 200 East Park Street, Edwardsville, Illinois 62025. Its telephone number is (618) 656-6122.

CLOVER LEAF BANK

Founded in 1889, Clover Leaf Bank converted its charter from an Illinois-chartered savings bank to an Illinois-chartered commercial bank in December 2002. Clover Leaf Bank operates from its main office in Edwardsville, Illinois, and one branch office. Clover Leaf Bank's deposits are insured by the Bank Insurance Fund, as administered by the Federal Deposit Insurance Corporation, up to the maximum amount permitted by law.

Clover Leaf Bank's executive office is located at 200 East Park Street, Edwardsville, Illinois 62025. Its telephone number is (618) 656-6122.

MARKET AREA

Clover Leaf Bank's lending and deposit-gathering area is concentrated in the neighborhoods surrounding its two offices in Edwardsville, Illinois, which is located in Madison County. The population of Madison County grew 3.9% from 1990 to 2000, compared to an 8.6% increase in the population of the State of Illinois during the same period. During this same period, however, our local market area, consisting of Edwardsville and surrounding towns, has experienced a significant increase in housing starts. The economy in Clover Leaf Bank's market area is not dependent on any single employer or type of business. While Madison County's economy is primarily industrial, Edwardsville, as the county seat, has a primarily service-oriented economy. The three largest employers in Madison County, all of which are headquartered in Edwardsville, are Southern Illinois University at Edwardsville, the Madison County Government and Edwardsville

Community Schools.

COMPETITION

We face significant competition in both originating loans and attracting deposits. Madison County has a significant number of financial institutions, many of which are significantly larger and have greater financial resources than Clover Leaf Bank, and all of which are our competitors to varying degrees. Our competition for loans comes principally from commercial banks, savings institutions, mortgage banking companies, credit unions and insurance companies. Our most direct competition for deposits historically has come from commercial banks and credit unions. We face additional competition for deposits from non-depository competitors such as mutual funds, securities and brokerage firms and insurance companies. Management believes that the Gramm-Leach-Bliley Act, which permits affiliation among banks, securities firms and insurance companies, will increase competition in our market area.

LENDING ACTIVITIES

GENERAL. Our loan portfolio consists primarily of one- to four-family residential real estate loans. The vast majority of these loans have fixed rates of interest. In addition to one- to four-family residential real estate loans, our loan portfolio consists of commercial and consumer loans, and, to a lesser extent, construction and overdraft loans.

In an effort to increase our interest income and to reduce the risk to our net income from changes in market interest rates, we have emphasized the origination of commercial real estate and commercial business loans. Compared to our residential mortgage loans, commercial real estate and commercial business loans generally have higher interest rates and are more sensitive to changes in market interest rates because they have adjustable interest rates and shorter terms to maturity. In addition, in order to improve our asset quality and reduce our delinquencies, we have discontinued our indirect automobile lending.

LOAN PORTFOLIO COMPOSITION. The following table shows the composition of our loan portfolio in dollar amounts and in percentages (before deductions for deferred fees and allowances for loan losses) as of the dates indicated.

	AT DECEMBER 31,			
	2003		2002	
	AMOUNT	PERCENT	AMOUNT	PERCENT
	(DOLLARS IN THOUSANDS)			
Real Estate Loans:				
One- to four-family...............	$ 31,709	46.98%	$ 34,300	50.26%
Commercial........................	24,335	36.06	22,797	33.40
Construction and land.............	1,105	1.64	761	1.12
Total real estate loans.......	57,149	84.68	57,858	84.78
Other Loans:				

Consumer:				
Automobile......................	1,014	1.50	1,425	2.09
Home equity.....................	1,843	2.73	1,611	2.36
Other...........................	1,351	2.00	1,595	2.34
Total consumer loans..........	4,208	6.23	4,631	6.79
Commercial business..............	6,133	9.09	5,759	8.43
Total gross loans..........	67,490	100.00%	68,248	100.00%
Less:				
Deferred fees and discounts.......	10		14	
Allowance for loan losses.........	725		690	
Total loans receivable, net.......	$ 66,755		$ 67,544	

The following table illustrates the interest rate sensitivity of our loan portfolio at December 31, 2003. Mortgages that have adjustable or renegotiable interest rates are shown as maturing in the period during which the full principal amount of the mortgage is due. The schedule does not reflect the effects of possible prepayments or enforcement of due-on-sale clauses.

	DUE IN ONE YEAR OR LESS		DUE AFTER ONE YEAR THROUGH FIVE YEARS		DUE AFTER F YEARS	
	AMOUNT	WEIGHTED AVERAGE RATE	AMOUNT	WEIGHTED AVERAGE RATE	AMOUNT	WE AV
			(DOLLARS IN THOUSANDS)			
Real Estate loans:						
One- to four-family................	$ 1,880	5.77%	$ 10,386	5.87%	$ 19,443	5
Commercial.........................	11,105	5.04	13,155	6.20	75	7
Construction and land..............	1,105	5.85	--	--	--	
Commercial business loans.............	3,710	4.91	2,257	5.94	166	5
Consumer loans........................	2,787	6.14	1,180	6.60	241	6
Gross loans...........................	$ 20.587	5.28%	$ 26,978	6.07%	$ 19,925	5

The total amount of loans due after December 31, 2004 which have predetermined interest rates is $34 million, while the total amount of loans due after such date which have floating or adjustable interest rates is $13 million.

ONE- TO FOUR-FAMILY RESIDENTIAL REAL ESTATE LOANS. Historically, we have emphasized the origination of one- to four-family loans secured by residential real estate. As of December 31, 2003, these loans totaled $31.7 million, or 47.0% of our total loan portfolio. 99.0% of our residential real estate loans have fixed rates of interest. The remaining 1.0% are adjustable rate mortgages that were originated several years ago. Currently, we do not offer adjustable interest rates on our one- to four-family mortgage loans primarily because our customers prefer fixed-rate mortgage loans in the relatively low interest rate environment that currently exists. We generally retain most of the loans that we originate, although in the past we have sold loans on a servicing-retained basis. We intend to sell a greater percentage of our residential real estate loan originations on a servicing-retained basis. At December 31, 2003, we were servicing $17.6 million in loans for others.

We currently offer one- to four-family residential mortgage loans with terms of 5, 15 and 30 years. Our five-year loans provide for principal and interest amortization of up to 30 years with a balloon payment at the end of the five-year term. All of our 15- and 30-year loans amortize over the term of the loan.

For one- to four-family residential real estate loans, we may lend up to 80% of the property's appraised value, or up to 90% of the property's appraised value if the borrower obtains private mortgage insurance. We require title insurance on all of our one- to four-family mortgage loans, and we also require that fire and extended coverage casualty insurance (and, if appropriate, flood insurance) be maintained in an amount equal to at least the lesser of the loan balance or the replacement cost of the improvements on the property. We require a property appraisal for all mortgage loans that are underwritten to comply with secondary market standards. Appraisals are conducted by our on-staff appraisers as well as independent appraisers from a list approved by our board of directors. Our residential real estate loans include "due-on-sale" clauses.

COMMERCIAL REAL ESTATE LOANS. We have increased our emphasis on commercial real estate lending in recent years. Loans secured by commercial real estate totaled $24.3 million, or 36.1% of our total loan portfolio as of December 31, 2003. Our commercial real estate loans are secured predominately by office buildings, and to a lesser extent warehouse properties and more specialized properties such as churches. We originate commercial real estate loans with a maximum term of three years. We offer both adjustable and fixed rates of interest on commercial real estate loans, with the interest rate for adjustable rate loans tied to the prime interest rate. Our largest commercial real estate loan at December 31, 2003 had a principal balance of $2.2 million and was collateralized by an apartment complex. This loan is performing in accordance with its payment terms.

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Commercial real estate loans generally have higher interest rates than the interest rates on residential mortgage loans, and are more sensitive to changes in market interest rates because they often have adjustable interest rates and shorter terms. Commercial real estate loans have significant additional risk compared to one- to four-family residential mortgage loans, as they typically involve large loan balances concentrated with single borrowers or groups of related borrowers. In addition, the repayment of commercial real estate loans typically depends on the successful operation of the related real estate project, and thus may be subject to a greater extent than residential mortgage loans to adverse conditions in the real estate market or in the economy generally.

In our underwriting of commercial real estate loans, we may lend up to

80% of the property's appraised value in the case of loans secured by apartments, and up to 75% of the property's appraised value on loans secured by other commercial properties. We require independent appraisals for all commercial real estate loans in excess of $250,000. For loans that do not exceed this amount, we require that an officer prepare a memorandum of value detailing comparable values based upon tax bills, prior appraisals, and income information on revenue-producing property. Decisions to lend are based on the economic viability of the property and the creditworthiness of the borrower. Creditworthiness is determined by considering the character, experience, management and financial strength of the borrower, and the ability of the property to generate adequate funds to cover both operating expenses and debt service. In evaluating whether to make a commercial real estate loan, we place primary emphasis on the ratio of net cash flow to debt service on the property, and we generally require a ratio of cash flow to debt service of at least 120%, computed after deduction for a vacancy factor and property expenses we deem appropriate.

We require title insurance on all of our commercial real estate loans, and we also require that fire and extended coverage casualty insurance (and, if appropriate, flood insurance) be maintained. In addition, we generally require that the borrower personally guarantee the repayment of the loan.

CONSTRUCTION AND LAND LOANS. We originate two types of residential construction loans: (i) construction/speculative loans, and (ii) construction/permanent loans. As of December 31, 2003, construction and land loans totaled $1.1 million, or 1.6% of our total loan portfolio.

Construction/speculative loans are made to area homebuilders who do not have, at the time the loan is originated, a signed contract with a homebuyer who has a commitment for permanent financing with either Clover Leaf Bank or another lender. The homebuyer may enter into a purchase contract either during or after the construction period. These loans have the risk that the builder will have to make interest and principal payments on the loan and finance real estate taxes and other holding costs of the completed home for a significant time after the completion of construction. Funds are disbursed in phases as construction is completed. All construction/speculative loans require that the builder-borrower personally guarantee the full repayment of the principal and interest on the loan. These loans are generally originated for a term of twelve months, with interest rates that are tied to the prime lending rate, and with a loan-to-value ratio of no more than 75% of the lower of cost or the estimated value of the completed property. Generally, we limit our construction/speculative loans to one property per borrower at any given time, and the largest number of construction/speculative loans we have originated to a single borrower at any given time was for three properties. At December 31, 2003, the largest outstanding concentration of credit to one builder consisted of one construction/speculative loan with an aggregate balance of $441,724, which was performing in accordance with its payment terms.

Construction/permanent loans are made to either a homebuilder or a homeowner who, at the time of construction, has a signed contract together with a commitment for permanent financing from Clover Leaf Bank for the finished home. The construction phase of a loan generally lasts up to six months, and the interest rate charged generally corresponds to the rate of the committed permanent loan, with loan-to-value ratios of up to 80% (or up to 90% if the borrower obtains private mortgage insurance) of the appraised estimated value of the completed property or cost, whichever is less. Following the initial 6-month period, construction/permanent loans convert to permanent loans, regardless of whether the construction phase has been completed. At December 31, 2003 the largest single outstanding construction loan of this type had an outstanding balance of $0, but had a committed line of credit of $500,000.

Construction lending generally involves a greater degree of risk than other one- to four-family mortgage lending. The repayment of the construction loan is, to a great degree, dependent upon the successful and timely completion of the home construction. Construction delays or the financial impairment of the builder may further impair the borrower's ability to repay the loan.

Our procedures for underwriting construction/speculative loans include an assessment of the borrower's credit history and the borrower's ability to meet other existing debt obligations, as well as payment of principal and interest on the proposed loan. We use the same underwriting standards and procedures for construction/permanent lending as we do for one- to four-family residential real estate lending.

We also originate land development loans to area homebuilders that are secured by individual unimproved or improved residential building lots. Land loans are generally offered with variable prime-based interest rates with terms of up to two years. The maximum loan-to-value ratio is 65% of the lower of cost or appraised value of the property.

CONSUMER LOANS. Our consumer loans consist primarily of automobile loans, home equity lines of credit and overdraft loans, loans secured by deposits and securities, and unsecured personal loans. As of December 31, 2003, consumer loans totaled $4.2 million, or 6.2% of our total loan portfolio.

Automobile loans are generally offered with maturities of up to 60 months for new automobiles, while loans secured by used automobiles will have maximum terms that vary depending on the age of the automobile. We require all borrowers to maintain collision insurance on automobiles securing loans in excess of $1,000, with Clover Leaf Bank listed as loss payee. In those instances where the borrower fails to maintain adequate insurance coverage, we are further protected against loss by vendors single interest insurance coverage.

Our indirect automobile loans have experienced higher than average delinquency and loss rates, and we discontinued this type of automobile lending in July 2000. Our automobile loan portfolio totaled $1.0 million or 1.5% of total loans at December 31, 2003, compared to $1.4 million, or 2.1% of total loans at December 31, 2002.

Home equity lines of credit are generally made for owner-occupied homes, and are secured by first or second mortgages on residential properties. We are attempting to increase our originations of home equity loans through targeted marketing. We generally offer home equity lines of credit with a maximum loan to appraised value ratio of 85% (including senior liens on the subject property). We currently offer these loans for terms of up to 10 years, and with adjustable rates that are tied to the prime lending rate.

We offer overdraft loans by providing unsecured lines of credit to qualifying checking accountholders. The line of credit must be pre-approved by Clover Leaf Bank's loan department. Overdraft loans totaled $140,000, or 0.2% of our total loan portfolio as of December 31, 2003.

Consumer loans generally entail greater credit risk than residential mortgage loans, particularly in the case of loans that are unsecured or are secured by assets that tend to depreciate in value, such as automobiles. In these cases, repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and the remaining value often does not warrant further substantial collection efforts against the borrower. Further, consumer loan collections depend on the borrower's continuing financial stability, and therefore are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy.

Our procedures for underwriting consumer loans include an assessment of the borrower's credit history and ability to meet other existing debt obligations, as well as payments of principal and interest on the proposed loans. The stability of the borrower's monthly income may be determined by verification of gross monthly income from primary employment, and additionally from any verifiable secondary income. Although the borrower's creditworthiness is a primary consideration, the underwriting process also includes a comparison of the value of the collateral security, if any, to the proposed loan amount. We require independent appraisals for all consumer loans in excess of $50,000. For loans that do not exceed this amount, we require that an officer prepare a memorandum of value detailing comparable values based upon tax bills or other available information.

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COMMERCIAL BUSINESS LOANS. We currently offer commercial business loans to existing customers in our market area, some of which are secured in part by additional real estate collateral. We make various types of secured and unsecured commercial business loans for the purpose of financing equipment acquisition, expansion, working capital and other general business purposes. The terms of these loans are generally for less than three years. Equipment loans usually involve a one-time disbursement of funds, with repayment over the term of the loan, while operating lines of credit involve multiple disbursements and revolving notes that can be renewed annually. The loans are either negotiated on a fixed-rate basis or carry variable interest rates indexed to the prime rate. At December 31, 2003, we had 88 commercial business loans outstanding with an aggregate balance of $6.1 million, or 9.1%, of the total loan portfolio. As of December 31, 2003, our largest commercial business loan consisted of our participation interest in a $604,148 loan to a car dealer, which is secured by stock of the car dealership.

In recent years, we have increased our emphasis on commercial business lending. These loans tend to have higher rates of interest than residential mortgage loans, and are more sensitive to changes in market interest rates because they often have adjustable interest rates and shorter terms. In addition, commercial business lending gives us greater access to commercial borrowers that may open transactional checking accounts with Clover Leaf Bank.

Commercial credit decisions are based upon a complete credit review of the borrower. A determination is made as to the borrower's ability to repay in accordance with the proposed terms as well as an overall assessment of the credit risks involved. Personal guarantees of borrowers are generally required. In evaluating a commercial real estate loan, we place primary emphasis on the ratio of net cash flow to debt service for the property, generally requiring a ratio of at least 120%. Credit agency reports of the borrower's credit history as well as bank checks and trade investigations supplement the analysis of the borrower's creditworthiness. Collateral supporting a secured transaction is also analyzed to determine its marketability and liquidity. Commercial business loans generally bear higher interest rates than residential loans, but they also may involve a higher risk of default since their repayment generally depends on the successful operation of the borrower's business.

LOAN ORIGINATIONS, PURCHASES, SALES AND SERVICING. Although we originate both fixed-rate and adjustable-rate loans, our ability to generate each type of loan depends upon borrower demand, market interest rates, borrower preference for fixed- versus adjustable-rate loans, and the interest rates offered on each type of loan by competing lenders in our market area. This includes banks, savings institutions, credit unions, mortgage banking companies, and life insurance companies. Loan originations are derived from a number of sources, including existing or prior customers and walk-in customers.

Loan originations are adversely affected by rising interest rates, which typically result in decreased loan demand. Accordingly, the volume of our loan originations and the interest rates we can charge on loans vary from period to period. One- to four-family residential mortgage loans are generally underwritten to conform to Fannie Mae and Freddie Mac seller/servicer guidelines, and are currently originated on a fixed interest rate basis only. We generally retain the loans that we originate. When we do sell mortgage loans, we generally retain the servicing rights, which means that we will continue to collect payments on the loans and supervise foreclosure proceedings, if necessary. We retain a portion of the interest paid by the borrower on the loans, generally 25 basis points, as consideration for our services. We currently service $17.6 million of loans for others, and we intend to sell a portion of our one- to four-family residential mortgage loans in the future in an effort to reduce our interest rate risk.

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The following table summarizes our loan origination and repayment activities for the periods indicated. We did not purchase any loans during the periods indicated.

	YEARS ENDED DECEMBER,	
	2003	2002
	(IN THOUSANDS)	
Loans receivable, net, at beginning of period.	$ 67,544	$ 62,435
Originations by type:		
Real estate		
One- to four-family	24,793	26,076
Commercial	10,094	13,289
Non-real estate		
Consumer	1,456	1,614
Commercial business	9,091	--
Total loans originated	45,434	40,979
Sales and Repayments		
Sales:		
Real estate		
One- to four-family	13,314	8,204
Commercial	1,400	--
Non-real estate		
Commercial business	500	--
Total loans sold	15,214	8,204
Principal repayments	30,974	27,709
Total reductions	46,188	35,913
Increase (decrease) in other items, net	(35)	43

Net increase..................................	789	5,109
Loans receivable, net, at end of period..................	$ 66,755	$ 67,544

LOAN APPROVAL PROCEDURES AND AUTHORITY. Our lending activities are subject to written underwriting standards and loan origination procedures adopted by management and the Board of Directors. For single family, owner-occupied real estate loans, the President of Clover Leaf Bank is authorized to approve loans up to $250,000, while the Senior Vice President is authorized to approve loans up to $200,000. For secured commercial real estate loans and construction and land loans, the President and Senior Vice President are authorized to approve loans up to $150,000 and $75,000, respectively; for secured consumer loans, these officers may approve loans up to $50,000; and for overdrafts and unsecured credits, these officers may approve loans up to $25,000 and $15,000, respectively. When acting together, these officers may approve new loans in amounts up to 150% of their combined lending limits, and may approve renewals of commercial business and commercial real estate loans in amounts up to 200% of their combined lending limits where there has been no deterioration in either the payment pattern or financial strength of the borrower. However, the entire Board of Directors must approve all loans in excess of $625,000. In addition, the Board of Directors generally ratifies all pre-authorized loan approvals.

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ASSET QUALITY

DELINQUENT LOANS. The following table sets forth Clover Leaf Bank's loan delinquencies by type, amount and percentage at December 31, 2003.

	LOANS DELINQUENT FOR:						
	60-89 DAYS			90 DAYS AND OVER			TOTA
	NUMBER	AMOUNT	PERCENT OF LOAN CATEGORY	NUMBER	AMOUNT	PERCENT OF LOAN CATEGORY	NUMBER
	(DOLLARS IN THOUSANDS)						
Real Estate:							
Commercial	1	$ 171	0.7%	--	$ --	--%	
One- to four-family...	8	250	0.8	1	12	0.03	
Consumer...............	18	73	1.7	--	--	--	1
Commercial business.....	--	--	--	--	--	--	-
Total.............	27	$ 494	0.7%	1	$ 12	--%	2

LOAN DELINQUENCIES AND COLLECTION PROCEDURES. When a borrower fails to make required payments on a loan, we take a number of steps to induce the borrower to correct the delinquency and restore the loan to a current status. We will send a borrower a reminder notice 15 days after an account becomes delinquent, and our employees are authorized to use their discretion whether direct telephone contact is required at that time. If the borrower does not remit the entire payment due by the end of the month, we try to make direct contact with the borrower to arrange a payment plan. If a satisfactory payment plan is not established within 50 days of a delinquency, we will send a demand letter to the borrower. If a satisfactory payment plan has not been arranged within 60 days following a delinquency, we may instruct our attorneys to institute foreclosure proceedings depending on the loan-to-value ratio or our relationship with the borrower. Foreclosed property is held as other real estate owned.

Our policies require that management continuously monitor the status of the loan portfolio and report to the Board of Directors on a monthly basis. These reports include information on delinquent loans and foreclosed real estate and our actions and plans to cure the delinquent status of the loans and to dispose of any real estate acquired through foreclosure.

NON-PERFORMING LOANS. All loans are reviewed on a regular basis and are placed on non-accrual status when, in the opinion of management, there is reasonable probability of loss of principal or the collection of additional interest is deemed insufficient to warrant further accrual. Generally, we place all loans 90 days or more past due on non-accrual status. In addition, we place any loan on non-accrual status if any part of it is classified as loss or if any part has been charged-off. When a loan is placed on non-accrual status, total interest accrued and unpaid to date is reversed. Subsequent payments are either applied to the outstanding principal balance or recorded as interest income, depending on the assessment of the ultimate collectibility of the loan. Loans are charged-off no later than 120 days following their delinquency, unless the loans are well-collateralized or in the process of collection.

As of December 31, 2003, our total non-accrual loans amounted to $896,000 compared to $1.5 million at December 31, 2002. As of December 31, 2003,the largest contributor of these loans was a residential mortgage loan with an outstanding balance of $141,391. The decline in non-accrual loans was the result of several loans paying off in the fourth quarter of 2003, the largest being a settlement from an insurance company on a commercial business loan.

The table below sets forth the amounts and categories of non-performing assets in our loan portfolio. For all years presented, we had no troubled debt restructurings (which involve forgiving a portion of interest or principal on loans or making loans at materially less than market interest rates), and no foreclosed assets.

	YEARS ENDED DECEMBER 31,	
	2003	2002
	(DOLLARS IN THOUSANDS)	
Non-accruing loans:		
One- to four-family	$ 644	$ 809
Construction	--	182
Commercial business	160	283
Commercial real estate	--	59

Consumer	92	196
Total	$ 896	$ 1,529
Accruing loans delinquent more than 90 days:		
One- to four-family	12	29
Commercial business	--	10
Commercial real estate	--	151
Consumer	--	5
Total	12	195
Total non-performing loans	$ 908	$ 1,724
Total non-performing loans as a percentage of total assets.	0.88%	1.80%
Allowance for loan losses as a percentage of non-performing loans	79.85%	40.02%
Allowance for loan losses as a percentage of gross loans receivable	1.07%	1.01%

For the years ended December 31, 2003 and 2002, respectively, $90,000 and $119,000 of gross interest income would have been recorded had our non-accruing loans been current in accordance with their original terms.

TROUBLED DEBT RESTRUCTURINGS. A troubled debt restructuring occurs when we, for economic or legal reasons related to a borrower's financial difficulties, grant a concession to the borrower, either as a deferment or reduction of interest or principal on the loan, that we would not otherwise consider. We had no troubled debt restructurings as of December 31, 2003 or 2002.

REAL ESTATE OWNED. Real estate owned consists of property acquired through formal foreclosure or by deed in lieu of foreclosure and is recorded at the lower of recorded investment or fair value. Write-downs from recorded investment to fair value which are required at the time of foreclosure are charged to the allowance for loan losses. After transfer, the property is carried at the lower of recorded investment or fair value, less estimated selling expenses. Adjustments to the carrying value of the properties that result from subsequent declines in value are charged to operations in the period in which the declines occur. We held no property that was classified as real estate owned as of December 31, 2003 or, 2002.

CLASSIFICATION OF ASSETS. Our policies, consistent with regulatory guidelines, require that we classify loans and other assets, such as securities, that are considered to be of lesser quality, as substandard, doubtful, or loss assets. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the savings institution will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as loss are those considered uncollectable and of such little value that their continuance as assets is not warranted. Assets that do not expose us to risk sufficient to warrant classification in one of the aforementioned categories, but which possess some weaknesses, are required to be designated as special mention by management.

When we classify assets as either substandard or doubtful, we allocate for analytical purposes a portion of our general valuation allowances or loss reserves to these assets as deemed prudent by management. General allowances represent loss allowances that have been established to recognize the probable risk associated with lending activities, but which have not been allocated to particular problem assets. When we classify problem assets as loss, we are required either to establish a specific allowance for losses equal to 100% of the amount of the assets so classified, or to charge-off the amount of the assets. Our determination as to the classification of assets and the amount of valuation allowances is subject to review by regulatory agencies, which can order the establishment of additional loss allowances. Management regularly reviews our asset portfolio to determine whether any assets require classification in accordance with applicable regulatory guidelines and generally accepted accounting principles.

On the basis of management's review of our assets, at December 31, 2003, we had classified a total of $3.9 million of our loans and other assets as follows:

	AT OR FOR THE YEAR ENDED DECEMBER 31, 2003
	(IN THOUSANDS)
Special Mention..................	$ 2,692
Substandard.....................	1,177
Doubtful assets.................	--
Loss assets.....................	--
Total......................	$ 3,869
General loss allowance...........	$ 725
Specific loss allowance..........	--
Charge-offs.....................	41

ALLOWANCE FOR LOAN LOSSES. The following table sets forth information regarding our allowance for loan losses and other ratios at or for the dates indicated.

	YEARS ENDED DECEMBER 31,	
	2003	2002
	(DOLLARS IN THOUSANDS)	
Balance at beginning of period............................	$ 690	$ 646
Charge-offs:		
Commercial business.....................................	40	-

Consumer	28	(105)
	68	(105)
Recoveries:		
Commercial business	2	4
Consumer	25	52
	27	56
Net charge-offs	41	(49)
Additions charged to operations	76	93
Balance at end of period	$ 725	$ 690
Ratio of net charge-offs during the period to average loans outstanding during the period	0.06%	0.07%
Ratio of net charge-offs during the period to average non-performing assets	2.57%	2.84%

The allowance for loan losses is a valuation account that reflects our evaluation of the credit losses inherent in our loan portfolio. We maintain the allowance through provisions for loan losses that we charge to income. We

charge losses on loans against the allowance for loan losses when we believe the collection of loan principal is unlikely.

Our evaluation of risk in maintaining the allowance for loan losses includes the review of all loans on which the collectibility of principal may not be reasonably assured. We consider the following factors as part of this evaluation: our historical loan loss 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, peer group information and prevailing economic conditions. There may be other factors that may warrant our consideration in maintaining an allowance at a level sufficient to provide for probable losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available or as future events change. Although we believe that we have established and maintained the allowance for loan losses at adequate levels, future additions may be necessary if economic and other conditions in the future differ substantially from the current operating environment.

In addition, the Illinois Office of Banks and Real Estate and the Federal Deposit Insurance Corporation, as an integral part of their examination process, periodically review our loan portfolio and the related allowance for loan losses. The Illinois Office of Banks and Real Estate and the Federal Deposit Insurance Corporation may require us to increase the allowance for loan losses based on their judgments of information available to them at the time of their examination, thereby adversely affecting our results of operations.

ALLOCATION OF THE ALLOWANCE FOR LOAN LOSSES. The following table presents our allocation of the allowance for loan losses by loan category and the percentage of loans in each category to total loans at the periods indicated.

	YEARS ENDED DECEMBER 31,				
	2003			2002	
	AMOUNT OF LOAN LOSS ALLOWANCE	LOAM AMOUNTS BY CATEGORY	PERCENT OF LOANS IN EACH CATEGORY TO TOTAL LOANS	AMOUNT OF LOAN LOSS ALLOWANCE	LOAN AMOUNTS BY CATEGOR
	(DOLLARS IN THOUSANDS)				
Real Estate Loans:					
One- to four-family..........	$ 209	$ 31,709	46.98%	$ 253	$ 34,3
Commercial...................	409	24,335	36.06	279	22,7
Construction and land........................	--	1,105	1.64	--	7
Commercial business............	40	6,133	9.09	44	5,7
Consumer.......................	67	4,208	6.23	114	4,6
Total.....................	$ 725	$ 67,490	100.00%	$ 690	$ 68,2

Management evaluates the total balance of the allowance for loan losses based on several factors that are not loan specific but are reflective of the losses inherent in the loan portfolio, including management's periodic review of loan collectibility 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, prevailing economic conditions such as housing trends, inflation rates and unemployment rates, geographic concentrations of loans within Clover Leaf Bank's immediate market area, and both peer financial institution historic loan loss experience and allowance for loan loss levels.

INVESTMENT ACTIVITIES

Clover Leaf Bank is permitted under federal and state law to invest in various types of liquid assets, including U.S. Government obligations, securities of various federal agencies and of state and municipal governments, deposits at the Federal Home Loan Bank of Chicago, certificates of deposit of federally insured institutions, certain bankers' acceptances and federal funds. Within certain regulatory limits, Clover Leaf Bank may also invest a portion of its assets in commercial paper and corporate debt securities. We are also required to invest

in Federal Home Loan Bank stock. See "Regulation" and "Management's Discussion and Analysis of Financial Condition and Results of Operations--Liquidity and Capital Resources."

SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," requires that securities be categorized as "held to maturity," "trading securities" or "available for sale," based on management's intent as to the ultimate disposition of each security. SFAS No. 115 allows debt securities to be classified as "held to maturity" and reported in financial statements at amortized cost only if the reporting entity has the positive intent and ability to hold those securities to maturity. Securities that might be sold in response to changes in market interest rates, changes in the security's prepayment risk, increases in loan demand, or other similar factors cannot be classified as "held to maturity."

Debt and equity securities held for current resale are classified as "trading securities." These securities are reported at fair value, and unrealized gains and losses on the securities are included in earnings. Clover Leaf Bank does not currently use or maintain a trading account. Debt and equity securities not classified as either "held to maturity" or "trading securities" are classified as "available for sale." These securities are reported at fair value, and unrealized gains and losses on the securities are excluded from earnings and reported, net of deferred taxes, as a separate component of equity. Clover Leaf Bank has classified all of its securities as available for sale.

All of our securities carry market risk insofar as increases in market interest rates may cause a decrease in their market value. Many also carry prepayment risk insofar as they may be called prior to maturity in times of low market interest rates, so that we may have to invest the funds at a lower interest rate. Investments in securities are made based on certain considerations, which include the interest rate, tax considerations, yield, settlement date and maturity of the security, our liquidity position, and anticipated cash needs and sources. The effect that the proposed security would have on our credit and interest rate risk and risk-based capital is also considered. We purchase securities to provide necessary liquidity for day-to-day operations, and when investable funds exceed loan demand.

Generally, the investment policy of Clover Leaf Bank, as established by the Board of Directors, is to invest funds among various categories of investments and maturities based upon our liquidity needs, asset/liability management policies, investment quality, marketability and performance objectives.

Our investment policy does not permit engaging directly in hedging activities or purchasing high-risk mortgage derivative products.

Our debt securities are mainly composed of securities issued by the U.S. Government and government agencies (primarily Federal Home Loan Bank, Fannie Mae and Freddie Mac), although from time to time we make other investments as permitted by applicable laws and regulations.

The following table sets forth information relating to the amortized cost and fair value of our securities, all of which are classified as available for sale. For further information, see Notes 1 and 3 of the Notes to Consolidated Financial Statements.

	DECEMBER 31,			
	2003		2002	
	AMORTIZED COST	FAIR VALUE	AMORTIZED COST	FAIR VALUE
	(IN THOUSANDS)			
Federal agencies...........	$ 16,120	$ 16,121	$ 9,352	$ 9,426
State and municipal........	1,820	1,853	844	852
Mortgage-backed securities.	4,814	4,813	2,601	2,613
Corporate.................	1,011	1,070	509	557

Total................	$ 23,765	$ 23,857	$ 13,306	$ 13,448

The following table sets forth the scheduled maturities, amortized cost and weighted average yields for our securities at December 31, 2003. Due to the current interest rate environment, the Company has experienced significant calls on securities. Therefore, the following schedule reflects maturity by call date if that date is different than the stated maturity date.

	DUE IN ONE YEAR OR LESS		DUE AFTER ONE YEAR THROUGH FIVE YEARS		DUE AFTER FIVE YEARS THROUGH TEN YEARS		DUE AFTER
	AMORTIZED COST	WEIGHTED AVERAGE RATE	AMORTIZED COST	WEIGHTED AVERAGE RATE	AMORTIZED COST	WEIGHTED AVERAGE RATE	AMORTIZED COST
					(DOLLARS IN THOUSANDS)		
U. S. Government agency securities	$ 13,399	4.47%	$ 2,721	5.09%	$ --	--%	$ --
Obligations of states and political subdivisions..	1,525	4.14	295	5.76	--	--	--
Mortgage-backed securities....	--	--	261	8.13	3,542	4.42	404
Asset-backed securities....	--	--	--	--	607	2.19	--
Corporate.......	--	--	1,011	5.44	--		--
Total.........	$ 14,924	4.43%	$ 4,288	5.40%	$ 4,149	4.09%	$ 404

SOURCES OF FUNDS

GENERAL. Deposits have been our primary source of funds for lending and other investment purposes. In addition to deposits, we derive funds primarily from principal and interest payments on loans. Loan repayments are a relatively stable source of funds, while deposit inflows and outflows are significantly influenced by market interest rates. Borrowings may be used on a short-term basis to compensate for reductions in the availability of funds from other sources, and may be used on a longer-term basis for general business purposes.

DEPOSITS. Residents of our primary market area are our main source of deposits. Deposit account terms vary, with the principal differences being the minimum balance required, the time periods the funds must remain on deposit and the interest rate. We do not use brokers to obtain deposits. Our deposit products include demand and NOW, money market, savings, and term certificate accounts. In recent years, and in connection with our emphasis on the origination of commercial business loans, we have promoted money market accounts with adjustable interest rates. Interest rates paid, maturity terms, service fees and withdrawal penalties are established by Clover Leaf Bank on a periodic basis. Management determines the rates and terms based on rates paid by our competitors, our needs for funds or liquidity, growth goals and federal and state regulations.

DEPOSIT ACCOUNTS BY TYPE. The following table sets forth the dollar amount of our deposits in the various types of deposit programs as of the dates indicated.(See separate worksheet for all CD and IRA comments. I believe we should add some more detail to the interest rates to make it more meaningful. If you choose to leave as is, see comments below for footing/rounding differences.)

	YEARS ENDED DECEMBER 31,			
	2003		2002	
	AMOUNT	PERCENT	AMOUNT	PERCENT
	(DOLLARS IN THOUSANDS)			
Transactions and savings deposits:				
Demand accounts......................	$ 8,002	9.94%	$ 7,153	9.87%
Savings accounts.....................	4,391	5.46	3,998	5.52
NOW accounts.........................	3,128	3.89	2,844	3.92
Money market accounts................	18,401	22.87	17,329	23.90
Total non-certificates.............	33,922	42.16	31,324	43.21
Certificates of deposit:				
1.00 - 1.99%.........................	11,465	14.25	136	0.19
2.00 - 2.99%.........................	12,058	14.99	16,310	22.50
3.00 - 3.99%.........................	8,231	10.23	3,841	5.30
4.00 - 4.99%.........................	5,742	7.14	5,175	7.14
5.00 - 5.99%.........................	3,302	4.10	4,445	6.13
6.00 - 6.99%.........................	189	0.23	1,240	1.71
7.00 - 7.25%.........................	--	--	5,046	6.96
Total certificates of deposit......	40,987	50.94	36,193	49.93
Individual retirement accounts:				
1.00 - 1.99%.........................	920	1.14	--	--
2.00 - 2.99%.........................	1,343	1.67	1,140	1.57
3.00 - 3.99%.........................	1,160	1.44	513	0.71
4.00 - 4.99%.........................	1,137	1.41	1,077	1.49
5.00 - 5.99%.........................	796	0.99	1,314	1.81
6.00 - 6.99%.........................	200	0.25	608	0.84
7.00 - 7.25%.........................	--	--	318	0.44
Total individual retirement accounts...........................	5,556	6.90	4,970	6.86%
Total time deposits................	$ 46,543	57.84%	$ 41,163	56.79%

Total deposits......................	$ 80,465	100.00%	$ 72,487	100.00%

TIME DEPOSIT RATES AND MATURITIES. The following table indicates interest rate and maturity information for our time deposits as of December 31, 2003.

INTEREST RATE	MATURITY			
	ONE YEAR OR LESS	OVER 1 TO 2 YEARS	OVER 2 TO 3 YEARS	OVER 3 YEARS
	(In Thousands)			
1.00 - 1.99%....................	$ 8,717	$ 3,500	$ 168	$ --
2.00 - 2.99%....................	10,901	1,937	563	--
3.00 - 3.99%....................	1,567	2,259	1,995	3,570
4.00 - 4.99%....................	690	307	931	4,951
5.00 - 5.99%....................	404	362	99	3,233
6.00 - 6.99%....................	169	220	--	--
Total time deposits.............	$ 22,448	$ 8,585	$ 3,757	$ 11,753

TIME DEPOSIT BALANCES AND MATURITIES. The following table indicates balance and maturity information for our time deposits as of December 31, 2003.

	MATURITY			
	3 MONTHS OR LESS	OVER 3 TO 6 MONTHS	OVER 6 TO 12 MONTHS	OVER 12 MONTHS
	(IN THOUSANDS)			
Time deposits less than $100,000......	$ 6,038	$ 6,011	$ 5,591	$ 21,855
Time deposits of $100,000 or more.....	3,140	622	1,053	2,233
Total time deposits..................	$ 9,178	$ 6,633	$ 6,644	$ 24,088

BORROWINGS. Clover Leaf Bank may obtain advances from the Federal Home Loan Bank of Chicago upon the security of the common stock it owns in that bank and certain of its residential mortgage loans and mortgage-backed securities, provided certain standards related to creditworthiness have been met. These advances are made pursuant to several credit programs, each of which has its own interest rate and range of maturities. Federal Home Loan Bank advances are generally available to meet seasonal and other deposit withdrawals and to permit increased lending.

The following table sets forth the maximum month-end balance and average balance of Federal Home Loan Bank advances for the periods indicated. Other than Federal Home Loan Bank advances, we had no other borrowings during the periods indicated.

	YEARS ENDED DECEMBER 31, 2003	2002
	(IN THOUSANDS)	
Maximum Balance:		
FHLB advances	$ 9,000	$ 9,000
Average Balance:		
FHLB advances	$ 8,830	$ 5,675

The following table sets forth total borrowings and the weighted average interest rate paid on such borrowings at the dates indicated.

	YEARS ENDED DECEMBER 31, 2003	2002
	(DOLLARS IN THOUSANDS)	
FHLB advances	$ 8,000	$ 9,000
Weighted average interest rate of FHLB advances	2.11%	2.83%

REGULATION

The following summarizes certain laws and regulations that are considered material to Clover Leaf Financial and Clover Leaf Bank. However, this summary does not purport to be complete and is qualified in its entirety by reference to applicable laws and regulations. Any change in this regulation, whether by the Federal Deposit Insurance Corporation, the Illinois Office of Banks and Real Estate, the Board of Governors of the Federal Reserve System, the Illinois General Assembly or Congress, could have a material adverse impact on Clover Leaf Financial and Clover Leaf Bank.

CLOVER LEAF FINANCIAL

HOLDING COMPANY ACQUISITIONS. Clover Leaf Financial is a bank holding company within the meaning of the Bank Holding Company Act and is registered with and regulated by the Federal Reserve Board. Federal law generally prohibits a company, without prior Federal Reserve approval, from acquiring the ownership or control of

any bank. In accordance with Federal Reserve Board policy, Clover Leaf Financial is expected to act as a source of financial strength to Clover Leaf Bank and to commit resources to support Clover Leaf Bank in circumstances where Clover Leaf Financial might not do so absent such policy. Under the Bank Holding Company Act, Clover Leaf Financial is subject to periodic examination by the Federal Reserve Board and will be required to file periodic reports of its operations and such additional information as the Federal Reserve Board may require. Clover Leaf Financial also is subject to regulation by, the Commissioner under the Illinois Bank Holding Company Act.

BANK HOLDING COMPANY ACT ACTIVITIES AND OTHER LIMITATIONS. A bank holding company is a legal entity separate and distinct from its subsidiary bank. Normally, the major source of a holding company's revenue is dividends from its subsidiary bank. The right of a bank holding company to participate as a stockholder in any distribution of assets of its subsidiary bank upon its liquidation or reorganization is subject to the prior claims of creditors of the subsidiary bank. The subsidiary bank is subject to claims by creditors for long-term and short-term debt obligations, including obligations for federal funds purchased and securities sold under repurchase agreements, as well as deposit liabilities.

The Bank Holding Company Act also prohibits a bank holding company, with certain exceptions, from acquiring more than 5% of the voting shares of any company that is not a bank and from engaging in any business other than banking or managing or controlling banks. Under the Bank Holding Company Act, the Federal Reserve Board is authorized to approve the ownership of shares by a bank holding company in any company, the activities of which the Federal Reserve Board has determined to be so closely related to banking or to managing or controlling banks as to be a proper incident thereto. The Federal Reserve Board has by regulation determined that certain activities are closely related to banking within the meaning of the Bank Holding Company Act. These activities include operating a mortgage company, finance company, credit card company, factoring company, trust company or savings association; performing certain data processing operations; providing limited securities brokerage services; acting as an investment or financial advisor; acting as an insurance agent for certain types of credit-related insurance; leasing personal property on a full-payout, non-operating basis; providing tax planning and preparation services; operating a collection agency; and providing certain courier services. The Federal Reserve Board also has determined that certain other activities, including real estate brokerage and syndication, land development and property management, are not closely related to banking and a proper incident thereto. In making such determinations, the Federal Reserve Board is required to weigh the expected benefit to the public, such as greater convenience, increased competition or gains in efficiency, against the possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices.

A bank holding company that is registered as a "financial holding company" is also permitted to engage in activities that are financial in nature or incidental to such financial activities. Activities that are considered financial in nature include: securities underwriting, dealing and market making; insurance underwriting; and merchant banking. Clover Leaf Financial has not elected to qualify as a financial holding company, although it may seek to do so in the future. Bank holding companies may qualify to become a financial holding company if:

- each of its depository institution subsidiaries is "well capitalized";
- each of its depository institution subsidiaries is "well managed";
- each of its depository institution subsidiaries has at least a "satisfactory" Community Reinvestment Act rating at its most recent examination; and
- the bank holding company has filed a certification with the Federal Reserve Board that it elects to become a financial holding company.

SARBANES-OXLEY ACT OF 2002. The Sarbanes-Oxley Act of 2002 implemented legislative reforms intended to address corporate and accounting irregularities. In addition to the establishment of a new accounting oversight board that enforces auditing, quality control and independence standards and is funded by fees from all publicly traded companies, the Act restricts accounting companies from providing both auditing and consulting services. To ensure auditor independence, any non-audit services being provided to an audit client will require preapproval by the

company's audit committee members. In addition, the audit partners must be rotated. The Act requires chief executive officers and chief financial officers, or their equivalent, to certify to the accuracy of periodic reports filed with the SEC, subject to civil and criminal penalties if they knowingly or willfully violate this certification requirement. In addition, under the Act, counsel will be required to report evidence of a material violation of the securities laws or a breach of fiduciary duty by a company to its chief executive officer or its chief legal officer, and, if such officer does not appropriately respond, to report such evidence to the audit committee or other similar committee of the board of directors or the board itself.

The legislation accelerates the time frame for disclosures by public companies, as they must immediately disclose any material changes in their financial condition or operations. Directors and executive officers must also provide information for most changes in ownership in a company's securities within two business days of the change. The period during which certain types of law suits can be instituted against a company or its officers has been extended, and bonuses issued to top executives prior to restatement of a company's financial statements are now subject to disgorgement if such restatement was due to corporate misconduct. Executives are also prohibited from insider trading during retirement plan "blackout" periods, and loans to company executives are restricted. In addition, civil and criminal penalties have been enhanced.

The Act also increases the oversight of, and codifies certain requirements relating to, audit committees of public companies and how they interact with the company's "registered public accounting firm" (RPAF). Audit Committee members must be independent and are barred from accepting consulting, advisory or other compensatory fees from the issuer. In addition, companies must disclose whether at least one member of the committee is a "financial expert" (as such term will be defined by the SEC) and if not, why not. Under the Act, a RPAF is prohibited from performing statutorily mandated audit services for a company if such company's chief executive officer, chief financial officer, comptroller, chief accounting officer or any person serving in equivalent positions has been employed by such firm and participated in the audit of such company during the one-year period preceding the audit initiation date. The Act also prohibits any officer or director of a company or any other person acting under their direction from taking any action to fraudulently influence, coerce, manipulate or mislead any independent public or certified accountant engaged in the audit of the company's financial statements for the purpose of rendering the financial statement's materially misleading. In accordance with the Act, the SEC proposed rules requiring inclusion of an internal control report and assessment by management in the annual report to shareholders. The Act requires the RPAF that issues the audit report to attest to and report on management's assessment of the company's internal controls. In addition, the Act requires that each financial report required to be prepared in accordance with (or reconciled to) generally accepted accounting principles and filed with the SEC reflect all material correcting adjustments that are identified by a RPAF in accordance with generally accepted accounting principles and the rules and regulations of the SEC.

CAPITAL REQUIREMENTS. The Federal Reserve Board has adopted capital adequacy guidelines for bank holding companies (on a consolidated basis) substantially similar to those of the FDIC for Clover Leaf Bank. Clover Leaf Financial's pro forma Tier 1 and total capital significantly exceed the Federal Reserve Board's capital adequacy requirements.

RESTRICTIONS ON TRANSACTIONS WITH AFFILIATES. Transactions between a bank and its "affiliates" are subject to quantitative and qualitative restrictions under Sections 23A and 23B of the Federal Reserve Act and FDIC regulations. Affiliates of a bank include, among other entities, the bank's holding company and companies that are controlled by or under common control with the bank.

In general, the extent to which a bank or its subsidiaries may engage in certain "covered transactions" with affiliates is limited to an amount equal to 10% of the institution's capital and surplus, in the case of covered transactions with any one affiliate, and to an amount equal to 20% of such capital and surplus, in the case of covered transactions with all affiliates. In addition, a bank and its subsidiaries may engage in covered transactions and certain other transactions only on terms and under circumstances that are substantially the same, or at least as favorable to the bank or its subsidiary, as those prevailing at the time for comparable transactions with nonaffiliated companies. A "covered transaction" is defined to include a loan or extension of credit to an affiliate; a purchase of investment securities issued by an affiliate; the purchase of assets from an affiliate, with certain exceptions; the

acceptance of securities issued by an affiliate as collateral for a loan or extension of credit to any party; or the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

In addition, Sections 22(h) and (g) of the Federal Reserve Act place restrictions on loans to executive officers, directors and principal stockholders. Under Section 22(h), loans to a director, an executive officer and to a greater than 10% stockholder of a bank, and certain affiliated interests of either, may not exceed, together with all other outstanding loans to such person and affiliated interests, the bank's loans to one borrower limit (generally equal to 15% of the institution's unimpaired capital and surplus). Section 22(h) also requires that loans to directors, executive officers and principal stockholders be made on terms substantially the same as offered in comparable transactions to other persons and also requires prior board approval for certain loans. In addition, the aggregate amount of extensions of credit by a bank to all insiders cannot exceed the institution's unimpaired capital and surplus. Furthermore, Section 22(g) places additional restrictions on loans to executive officers.

FEDERAL SECURITIES LAWS. Clover Leaf Financial's common stock is registered with the SEC under Section 12(g) of the Securities Exchange Act of 1934. Clover Leaf Financial is subject to the proxy and tender offer rules, insider trading reporting requirements and restrictions, and certain other requirements under the Exchange Act.

CLOVER LEAF BANK

GENERAL. Clover Leaf Bank is an Illinois-chartered commercial bank, the deposit accounts of which are insured by the Bank Insurance Fund of the FDIC. As an FDIC insured, Illinois-chartered commercial bank, Clover Leaf Bank is subject to the examination, supervision, reporting and enforcement requirements of the Illinois Office of Banks and Real Estate, as the chartering authority for Illinois banks, and the FDIC, as administrator of the Bank Insurance Fund, and to the statutes and regulations administered by the Illinois Office of Banks and

Real Estate and the FDIC governing such matters as capital standards, mergers, establishment of branch offices, subsidiary investments and activities and general investment authority. Clover Leaf Bank is required to file reports with the Illinois Office of Banks and Real Estate and the FDIC concerning its activities and financial condition, and will be required to obtain regulatory approvals prior to entering into certain transactions, including mergers with, or acquisitions of, other financial institutions.

The Illinois Office of Banks and Real Estate and the FDIC have extensive enforcement authority over Illinois-chartered commercial banks, such as Clover Leaf Bank. This enforcement authority includes, among other things, the ability to issue cease-and-desist or removal orders, to assess civil money penalties and to initiate injunctive actions. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe and unsound practices.

INSURANCE OF DEPOSIT ACCOUNTS. The Federal Deposit Insurance Corporation has adopted a risk-based system for assessing deposit insurance premiums. The Federal Deposit Insurance Corporation assigns an institution to one of three capital categories based on the institution's financial information, as of the reporting period ending seven months before the assessment period, and one of three supervisory subcategories within each capital group. The three capital categories are well capitalized, adequately capitalized and undercapitalized. The supervisory subgroup to which an institution is assigned is based on a supervisory evaluation provided to the Federal Deposit Insurance Corporation by the institution's primary federal regulator and information which the Federal Deposit Insurance Corporation determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance funds. An institution's assessment rate depends on the capital category and supervisory category to which it is assigned. The Federal Deposit Insurance Corporation is authorized to raise the assessment rates. The Federal Deposit Insurance Corporation has exercised this authority several times in the past and may raise insurance premiums in the future. If this type of action is taken by the Federal Deposit Insurance Corporation, it could have an adverse effect on the earnings of Clover Leaf Bank.

CAPITAL REQUIREMENTS. The FDIC has capital adequacy regulations and policies regarding the capital adequacy of state-chartered commercial banks that, like Clover Leaf Bank, are not members of the Federal Reserve System. The FDIC's capital regulations establish a minimum 3.0% Tier 1 leverage capital requirement for the most highly-rated state-chartered, non-member banks, with additional capital of at least 100 to 200 basis points for all

other state-chartered, non-member banks, which effectively will increase the minimum Tier 1 leverage ratio for such other banks to 4.0% to 5.0% or more. Under the FDIC's regulation, the highest-rated banks are those that the FDIC determines are not anticipating or experiencing significant growth and have well diversified risk, including no undue interest rate risk exposure, excellent asset quality, high liquidity, good earnings and, in general, are considered strong banking organizations, rated composite 1 under the Uniform Financial Institutions Rating System. Leverage or core capital is defined as the sum of common stock, capital surplus, retained earnings, noncumulative perpetual preferred stock and related surplus, and minority interests in consolidated subsidiaries, minus all intangible assets other than certain qualifying supervisory goodwill, and certain purchased mortgage servicing rights and purchased credit and relationships.

The FDIC also requires that banks meet a risk-based capital standard. Under the risk-based capital standard, total capital, which is defined as Tier 1 capital and supplementary (Tier 2 capital), must equal at least 8% of risk-weighted assets. In determining the amount of risk-weighted assets, all assets, plus certain off balance sheet assets, are multiplied by a risk-weight of 0% to 100%, based on the risks the FDIC believes are inherent in the type of asset.

The components of Tier 1 capital are equivalent to those discussed above under the 3% leverage standard. The components of supplementary (Tier 2) capital include certain perpetual preferred stock, certain mandatory convertible securities, certain subordinated debt and intermediate preferred stock and general allowances for loan and lease losses. Allowance for loan and lease losses includable in supplementary capital is limited to a maximum of 1.25% of risk-weighted assets. Overall, the amount of capital counted toward supplementary capital cannot exceed 100% of core capital. At December 31, 2003, Clover Leaf Bank met each of its capital requirements.

A bank which has less than the minimum leverage capital requirement must, within 60 days from the date it fails to comply with this requirement, submit to its FDIC regional director for review and approval a reasonable plan describing the means and timing by which the bank will achieve its minimum leverage capital requirement. A bank that fails to file such a plan with the FDIC is deemed to be operating in an unsafe and unsound manner and may be subject to a cease-and-desist order from the FDIC. FDIC regulations also provide that any insured depository institution with a ratio of Tier 1 capital to total assets that is less than 2.0% is deemed to be operating in an unsafe or unsound condition and is subject to potential termination of deposit insurance. However, such an institution will not be subject to an enforcement proceeding solely on account of its capital ratios if it has entered into and is in compliance with a written agreement with the FDIC to increase its Tier 1 leverage capital ratio and to take such other action as may be necessary to operate in a safe and sound manner. The FDIC capital regulation also provides, among other things, for the issuance by the FDIC of a capital directive, which is a final order issued to a bank that fails to maintain minimum capital to restore its capital to the minimum leverage capital requirement within a specified time period. Such directive is enforceable in the same manner as a final cease-and-desist order.

At December 31, 2003, Clover Leaf Bank exceeded all of its regulatory capital requirements, with leverage, Tier 1 risk-based and total risk-based capital ratios of 10.51%, 16.42% and 17.53%, respectively.

Any bank that fails any of the capital requirements is subject to possible enforcement actions by the FDIC. These actions could include a capital directive, a cease and desist order, civil money penalties, the establishment of restrictions on the institution's operations, termination of Federal deposit insurance and the appointment of a conservator or receiver.

At December 31, 2003, Clover Leaf Bank was deemed a well-capitalized institution for purposes of the above regulations and as such is not subject to the above-mentioned restrictions.

Clover Leaf Bank would not be able to pay dividends on its capital stock if its capital were reduced below the remaining balance of the liquidation account established in connection with the conversion.

SAFETY AND SOUNDNESS GUIDELINES. The FDIC and the other federal banking agencies have established guidelines for safety and soundness, addressing operational and managerial standards, as well as compensation matters for insured financial institutions. Institutions failing to meet these standards are required to submit compliance plans to their appropriate federal regulators. The FDIC and the other agencies also have established guidelines regarding asset quality and earnings standards for insured institutions. Clover Leaf Bank believes that it is in compliance with these guidelines and standards.

COMMUNITY REINVESTMENT ACT AND FAIR LENDING LAWS. Commercial banks, such as Clover Leaf Bank, have a responsibility under the Community Reinvestment Act and related regulations of the FDIC to help meet the credit needs of their communities, including low- and moderate-income neighborhoods. In addition, the Equal Credit Opportunity Act and the Fair Housing Act (together, the "Fair Lending Laws") prohibit lenders from discriminating in their lending practices on the basis of characteristics specified in those statutes. An institution's failure to comply with the provisions of Community Reinvestment Act could, at a minimum, result in regulatory restrictions on its activities. Failure to comply with the Fair Lending Laws could result in enforcement actions by the FDIC, as well as the Department of Justice.

FEDERAL HOME LOAN BANK SYSTEM. Clover Leaf Bank is a member of the Federal Home Loan Bank of Chicago, which is one of 12 regional Federal Home Loan Banks that administers the home financing credit function of savings institutions. Each Federal Home Loan Bank serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the Federal Home Loan Bank System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the Board of Directors of the Federal Home Loan Bank. At December 31, 2003, Clover Leaf Bank had $8.0 million of Federal Home Loan Bank advances. See the Notes to the Consolidated Financial Statements.

As a member, Clover Leaf Bank is required to purchase and maintain stock in the Federal Home Loan Bank of Chicago in an amount equal to at least 1% of its aggregate unpaid residential mortgage loans or similar obligations at the beginning of each year. At December 31, 2003, Clover Leaf Bank had $3.7 million in Federal Home Loan Bank stock, which was in compliance with this requirement.

The Federal Home Loan Banks are required to provide funds for the resolution of troubled savings institutions and to contribute to affordable housing programs through direct loans or interest subsidies on advances targeted for community investment and low- and moderate-income housing projects. These contributions have adversely affected the level of Federal Home Loan Bank dividends paid in the past and could do so in the future. These contributions also could have an adverse effect on the value of Federal Home Loan Bank stock in the future. The average dividend yield on Clover Leaf Bank's Federal Home Loan Bank stock was 6.16% in 2003 and 5.20% in 2002.

FEDERAL RESERVE SYSTEM. The Federal Reserve Board requires all depository institutions to maintain reserves against their transaction accounts (primarily NOW and Super NOW checking accounts) and non-personal time deposits. As of November 3, 1999, no reserves were required to be maintained on the first $5.0 million of transaction accounts, reserves of 3% were required to be maintained against the next $44.3 million of net transaction accounts, and a reserve of $1.3 million plus 10% against net transaction accounts above this amount. The above dollar amounts and percentages are subject to periodic adjustment by the Federal Reserve Board. Because required reserves must be maintained in the form of vault cash or a noninterest-bearing account at a Federal Reserve Bank, the effect of this reserve requirement is to reduce an institution's earning assets and constrain its ability to lend.

TAXATION

FEDERAL TAXATION

For federal income tax purposes, Clover Leaf Financial and Clover Leaf Bank file a consolidated federal income tax return on a calendar year basis using the accrual method of accounting.

Deferred income taxes arise from the recognition of items of income and expense for tax purposes in years different from those in which they are recognized in the consolidated financial statements. Clover Leaf Financial accounts for deferred income taxes by the asset and liability method, applying the enacted statutory rates in effect at

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the balance sheet date to differences between the book basis and the tax basis of assets and liabilities. The resulting deferred tax liabilities and assets are adjusted to reflect changes in the tax laws.

Clover Leaf Financial is not currently subject to the alternative minimum tax. Clover Leaf Financial may be subject to the corporate alternative minimum tax in the future, to the extent it exceeds Clover Leaf Financial's regular income tax for the year if its annual gross receipts for a three-year consecutive period exceed $7 million. The alternative minimum tax will be imposed at the rate of 20% of a specially computed tax base. Included in this base are a number of preference items, including interest on certain tax-exempt bonds issued after August 7, 1986, and an "adjusted current earnings" computation which is similar to a tax earnings and profits computation. In addition, for purposes of the alternative minimum tax, the amount of alternative minimum taxable income that may be offset by net operating losses is limited to 90% of alternative minimum taxable income.

Clover Leaf Bank's income tax returns have not been audited by the Internal Revenue Service for the past five years.

STATE TAXATION

ILLINOIS STATE TAXATION. Clover Leaf Financial is required to file Illinois income tax returns and pay tax at a stated tax rate of 7.30% of Illinois taxable income. For these purposes, Illinois taxable income generally means federal taxable income subject to certain modifications, the primary one of which is the exclusion of interest income on United States obligations.

DELAWARE TAXATION. As a Delaware holding company not earning income in Delaware, Clover Leaf Financial is exempt from Delaware corporate income tax but is required to file an annual report with and pay an annual franchise tax to the State of Delaware.

ITEM 2. DESCRIPTION OF PROPERTIES

At December 31, 2003, Clover Leaf Financial conducted its business from our main office at 200 East Park Street, Edwardsville, Illinois. The following table sets forth certain information with respect to the offices of Clover Leaf Bank at December 31, 2003.

LOCATION	LEASED OR OWNED	ORIGINAL YEAR LEASED OR ACQUIRED	NET BOOK VALUE

200 East Park Street Edwardsville, Illinois 62025	Owned	1976	$137,673
2143 South State Route 157 Edwardsville, Illinois 62025	Owned	1999	$1,198,091

ITEM 3. LEGAL PROCEEDINGS

Clover Leaf Bank is involved, from time to time, as plaintiff or defendant in various legal actions arising in the normal course of its business. Other than litigation previously disclosed, at December 31, 2003, Clover Leaf Financial and Clover Leaf Bank were not involved in any material legal proceedings.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of stockholders during the fourth quarter of the year under report.

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PART II

ITEM 5. MARKET FOR COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The section entitled "Market for Common Stock" section of Clover Leaf Financial's Annual Report to Stockholders is incorporated herein by reference.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" of Clover Leaf Financial's Annual Report to Stockholders is incorporated herein by reference.

ITEM 7. FINANCIAL STATEMENTS

The financial statements of Clover Leaf Financial's Annual Report to Stockholders are incorporated herein by reference.

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 8A. CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by this quarterly report, that the Company's disclosure controls and procedures (as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e)) are effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART III

ITEM 9. DIRECTORS AND EXECUTIVE OFFICERS

The "Proposal I--Election of Directors" section of the Company's definitive Proxy Statement for the Company's 2004 Annual Meeting of Stockholders (the "2004 Proxy Statement") is incorporated herein by reference.

ITEM 10. EXECUTIVE COMPENSATION

The "Proposal I--Election of Directors" section of the Company's 2004 Proxy Statement is incorporated herein by reference.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The "Proposal I--Election of Directors" section of the Company's 2004 Proxy Statement is incorporated herein by reference.

The Company does not have any equity compensation plan that was not approved by stockholders, other than its employee stock ownership plan.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The "Transactions with Certain Related Persons" section of the Company's 2004 Proxy Statement is incorporated herein by reference.

PART IV

ITEM 13. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a)(1) FINANCIAL STATEMENTS

The exhibits and financial statement schedules filed as a part of this Form 10-KSB are as follows:

(A) Independent Auditors' Report

(B) Consolidated Balance Sheets

(C) Consolidated Statements of Income

(D) Consolidated Statements of Changes in Stockholders' Equity

(E) Consolidated Statements of Cash Flows

(F) Notes to Consolidated Financial Statements

(a)(2) FINANCIAL STATEMENT SCHEDULES

All financial statement schedules have been omitted as the required information is inapplicable or has been included in the Notes to Consolidated Financial Statements.

(b) REPORTS ON FORM 8-K

On November 12, 2003, the company filed a current report on Form 8-K, Item 12. Results of Operations and Financial Condition, in which it announced its September 30, 2003 financial results.

(c) EXHIBITS

3.1 Certificate of Incorporation of Clover Leaf Financial Corp.*

3.2 Bylaws of Clover Leaf Financial Corp.*

4 Form of Common Stock Certificate of Clover Leaf Financial Corp.*

10.1 Form of Employee Stock Ownership Plan*

10.2 Director Emeritus Plan*

10.3 Form of Director's Deferred Compensation Agreement*

10.4 Officer's Deferred Bonus Compensation Agreement*

10.5 Employment Agreement with Dennis M. Terry

10.6 Change in Control Agreement with Dennis M. Terry

10.7 Change in Control Agreement with Darlene McDonald

10.8 Change in Control Agreement with Lisa Fowler

13 Portions of 2003 Annual Report to Stockholders

14 Code of Ethics

21 Subsidiaries of the Registrant*

31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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* Incorporated by reference to the Registration Statement on Form SB-2 of Clover Leaf Financial Corp. (Registration No. 333-69762) initially filed with the Securities and Exchange Commission on September 21, 2001.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The "Proposal II--Ratification of Appointment of Auditors" section of the Company's 2004 Proxy Statement is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CLOVER LEAF FINANCIAL CORP.

Date: March 26, 2004 By: /s/ Dennis M. Terry

Dennis M. Terry
President and Chief Executive Officer
(Duly Authorized Representative)

Pursuant to the requirements of the Securities Exchange of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Signatures	Title	Date
/s/ Dennis M. Terry Dennis M. Terry	President, Chief Executive Officer and Director (Principal Executive Officer)	March 26, 2004
/s/ Darlene F. McDonald Darlene F. McDonald	Senior Vice President and Treasurer (Principal Financial and Accounting Officer)	March 26, 2004
/s/ Joseph J. Gugger Joseph J. Gugger	Director	March 26, 2004
/s/ Kenneth P. Highlander Kenneth P. Highlander	Director	March 26, 2004
/s/ Gary D. Niebur Gary D. Niebur	Director	March 26, 2004
/s/ Robert W. Schwartz Robert W. Schwartz	Director	March 26, 2004
/s/ Dennis Ulrich Dennis Ulrich	Director	March 26, 2004