Operator: Good morning. Thank you for joining us for today's First Defiance Financial Corp's Second Quarter 2010 Earnings Release Conference Call. This call is also being webcast, and the audio replay will be available at the First Defiance website at www.fdef.com. Providing commentary this morning will be Bill Small, Chairman, President and CEO of First Defiance, and Don Hileman, Executive Vice President and Chief Financial Officer. Following their prepared comments on the company's strategy and performance, they will be available to take your questions.

Before we begin, I would like to remind you that during the conference call today, including during the Q&A period, you may hear forward-looking statements related to future financial results and business operations for the First Defiance Financial Corp. Actual results may differ materially from current management forecast and projections as a result of factors over which the company has no control. Information on these risk factors and additional information on forward-looking statements are included in the news release and in the company's reports on file with the Securities and Exchange Commission.

All participants will be in a listen-only mode. [Operator Instructions] After today's presentation there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded. I would now like to turn the conference over to Bill Small, President and CEO. Please, go ahead.

**William J. Small, President and Chief Executive Officer**
Thank you. Good morning, and thank you for joining us to review the First Defiance Financial Corp. 2010 second quarter results. Last night, we issued our 2010 second quarter earnings release and this morning we would like to discuss performance during the quarter and what we see ahead of us for the balance of 2010. We will also offer some comments regarding recent regulatory activity in Washington and its impact on First Defiance. At the conclusion of our presentation, we will answer any questions you might have.

Joining me on the call this morning to give more detail on the financial performance for the quarter is our CFO, Don Hileman and also, with us this morning to assist in answering questions is Jim Rohrs, President and CEO of First Federal Bank.

Second quarter 2010 net income on a GAAP basis was 2.1 million, or $0.19 per diluted common share, compared to 2.9 million and $0.29 per diluted share in the 2009 second quarter. For the sixmonth period ended June 30, 2010, First Defiance earned 3.6 million, or $0.31 per diluted common share, compared to 6.3 million, or $0.65 per diluted common share for the six-month period ended June 30, 2009.

Significant net interest margin improvement was a positive in the second quarter that earnings were again challenged by provision expense, as well as mortgage servicing rights impairment. The 2010 second quarter results are still not back to a normal run-rate showed a number of significant indicators that the core operation is running strong.

Net interest income was up $1.4 million over second quarter 2009 and almost $500,000 over the linked quarter on lower overall loan balances. We're also pleased to see non-interest expense drop over $1 million year-over-year, even while operating at higher OREO and collection expenses during the same period, as we stayed focused on cost control. The deposit mix continued its favorable trend as period-end balances and non-interest bearing deposits were up and TD balances were down, compared to the linked quarter and second quarter 2009.

The quarter was not without its challenges however. Asset quality had a significant negative impact again during the second quarter as we booked $5.4 million in provision expense. Don will give you more detail on the provision and allowance coverage in his remarks. The lower interest rates during the period resulted in a mortgage servicing rights impairment charge of over $500,000. We also recognized additional other than a temporary impairment on certain collateralize debt obligations in our portfolio during the second quarter.

Asset quality remains our primary focus. We continue to make it our priority to identify any weaknesses in performance or collateral as early as possible, and to monitor and analyze each credit to assure profit levels of reserves. Charge-offs for the quarter were up significantly as we had anticipated due to a number of credits migrating through the workout process for final disposition. The provision expense in the second quarter was significantly driven by adjustments to several previously-recognized problem loans where additional reserves were added for deteriorating collateral values and the reassessment of some loan guarantees. We have increased the allowance for loan losses to total loans from 1.6% at June 30, 2009 to 2.47% as of June 30, 2010. We are encouraged by the positive direction of several of our credit quality metrics in the first half of 2010, and are cautiously optimistic that this trend will continue.

The improvement in the net interest margin was obviously a highlight of the quarter. We were very pleased to see the efforts of a disciplined pricing strategy pay off in the margin performance, maintaining that discipline is going to be very important, as it appears we are going to remain in a low-interest rate environment for several more quarters.

Non-interest income results for the second quarter 2010 were significantly lower than June 30, 2009 results primarily due to the much lower mortgage loan production. The first half of 2009 was a record-setting period for residential mortgage loan production, but we have returned to more normalized levels in 2010.

This was further compounded by impairment charges taken this quarter for mortgage servicing rights, compared to a $1.5 million recapture of MSRs in the second quarter 2009. This was somewhat offset by lower OTTI charges in 2010, compared to last year.
On the plus side, we saw improvement in insurance commissions, trust income, and income from bank loan life insurance over last year, and the linked quarter. The acquisition of the group benefits book of business from an end market insurance agency during the second quarter will present additional revenue opportunities going forward.

The improvement in non-interest expense reflects an ongoing focus on cost control, and is very evident in lower compensation costs and occupancy expense. FDIC insurance expense was lower this quarter even with higher premiums and higher deposit balances due to the special assessment of approximately $900,000 incurred in the second quarter of 2009.
I will now ask Don Hileman to give you additional financial details for the quarter before I wrap up with an overview, and look at what we see developing in the months ahead. Don?

**Donald P. Hileman, Executive Vice President and Chief Financial Officer**
Thank you, Bill, and good morning, everyone. The second quarter saw improvement from a credit perspective, with improvement in delinquency and a reduction in problem loans. Our markets are still showing the impacts of the demanding economic environment. We are seeing some moderation and reduction and unemployment in our market area, but it remains well into doubledigits in the majority of the counties we serve.

We continue to see signs of improvement in our markets, with some businesses showing stronger 2010 operating results, compared to 2009 because signs are more isolated than across the board. We believe the overall trend is toward improved economic activity, however, it will be a slower growth pattern with an extended ramp-up period.
As we review our financial performance, credit quality remains a major driver and impact on our performance. We also had several other areas with stabilizing or improving trends, such as net interest income.

I will begin with a discussion of credit quality. Our provision expense totaled 5.4 million, down from 6.9 million in the first quarter of 2010, and up from 4 million in the second quarter of 2009.
Our allowance for loan loss remained flat at 38.9 million, or 2.47% of total loans at June 30, 2010, compared with 39 million, or 2.47% of total loans, at March 31, 2010, and up from 25.8 million, or

1.6 million – or 1.6% of total loans on June 30, 2009.

The second quarter provision was slightly less than net charge-offs. Annualized net charge-offs were 1.44% of the loans for the second quarter of 2010, compared with 1.14 on a linked quarter basis, and 96 basis points for the second quarter of 2009. Of the total charge-offs, 55% related to commercial and 22% related to commercial real estate loans. Of the total commercial charge-offs, 3.2 million – 2.8 million, or 88% related to one credit relationship, and 961,000 or 77% of the total commercial real estate charge-offs of 1.1 million related to one credit relationship.

The provision this quarter was driven primarily by a decrease in the specific allowance necessary for substandard loans, but the decrease was offset somewhat by an overall increase needed in the general reserve. The general reserve was impacted by an increase in the quantitative component of the general allowance, which is based on historical charge-off levels, which have increased. The qualitative component of the general reserve decreased based on improved trends in nonaccrual loans, classified loans and delinquency. Due to the continued environment of high unemployment, lower real estate values and sustained economic weakness in our market area, as well as the current regulatory environment, we believe that it's appropriate to operate with higher than historic levels of general loan loss reserves at this time.

As we continue to see improvements in our asset quality trends, as well as the economy, we become more encouraged about future results. However, we will need to see a sustained period of improvement to be comfortable that the economy in our market has truly turned the corner.
We calculate the allowance for loan losses by analyzing all loans on our internally rated classified and special mentioned list, and making informed judgments about the risk of loss based on the cash flow of the borrower, the value of any collateral and the financial strength of any guarantors. based on those judgments, we record a specific amount of loan loss against each loan that we analyzed for impairment. We analyzed all internally rated classified and special mentioned loans on at least a quarterly basis. The total of these categories have declined from March 31, 2010. The provision for loan losses, the adjustment we make and the allowance for loan losses necessary for the allowance to be adequate, based on the losses we estimate to be in the portfolio.
Our review considers numerous factors in determining if it is appropriate to adjust the economic, environmental and risk factors we use in determining the general portion of the reserve for loss when we assess the adequacy of the reserve.

This quarter we made some downward modifications to the economic and environmental factors used in the general reserve calculations. We believe this is consistent with the improvement in delinquency levels and the reduction in classified loans along with the operating environment we perceive for the near-term in 2010.

We maintain a continuous process of analysis and review of our loan portfolio. As loans move through the credit resolution process, one of the alternatives for the bank to take control of the real estate collateral by either way of foreclosure or pertaining – obtaining title voluntarily from the borrower in lieu of foreclosure.

We're moving more loans at this stage, which is evidenced by a higher level of charge-offs and OREO activity this quarter. Our OREO balance remained relatively flat on a linked quarter basis and ended the second quarter at 12.7 million.

We had additions of 6.1 million in the second quarter of 2010 offset by payouts of 5.3 million. This compares to additions of 3.1 million and sales of 1.7 million in the first quarter of 2010. We're seeing more interest from potential buyers of these properties as they go to auction or are listed for sale.

At June 30, our allowance for loan losses represented 2.47% of total loans outstanding, flat on a linked quarter basis, represents 95.41% of our non-performing loans, which is up from 64% of nonperforming loans at June 30, 2009.

The allowance to non-performing assets was 73% at June 30, 2010, flat with the first quarter and up from 53% at June 30, 2009. Non-performing assets ended the quarter at 53.5 million, or 2.62% of total assets, broadly unchanged from 53.4 million last quarter, which was 2.59% of our total assets.

Total non-performing loans increased to 40.7 million from 40.6 million in the first quarter. But nonaccrual loans decreased 1.8 million to 31.8 million from 33.6 million on a linked quarter basis. Restructured loans increased 1.9 million from last quarter. Restructured loans are considered nonperforming because of the changes during the original terms granted to borrowers. It is important to note that these loans are still accruing. This is a process in which we can work with borrowers who have the ability to repay to mitigate potential loss.

Total classified loans declined 12.3 million to 114.4 million from 126.7 million at March 31, 2010, from 127.7 million at June 30, 2009. Total delinquency rate was 2.7% at June 30, down from 3.36% at March 31, 2010, and down from 3.18 at December 31, 2009, and 3.78 at June 30, 2009. The delinquency rate for loans 90 days past due [inaudible] non-accrual decreased to 2.01% this quarter from 2.10 in the first quarter of 2010 and 2.5% at December 31, 2009. Improving credit quality and reducing the level of non-performing assets and classified assets is a major focus of the company.

Mortgage banking was down in the first quarter, but we were pleased with the results considering in a difficult economic environment. Overall mortgage banking income for the quarter was 985,000, compared with 4 million in the first quarter of 2009, and 1.8 million in the first quarter of 2010. The gain on sale income of 1.2 million in the second quarter of 2010, compared with 2.9 million in the second quarter of 2009 and 1.2 million in the first quarter of 2010. We also recorded a negative valuation adjustment to mortgage servicing rights of 571,000 in the second quarter of 2010, compared with positive valuation adjustment of 321,000 in the first quarter of 2010 and 1.5 million in the second quarter of 2009, reflecting the change in the level of market interest rates that affect the assumed prepayments fees of the underlying collateral. We are close to historically low rates.

At June 30, 2010, First Defiance had 1.2 billion of loan services for others. The mortgage servicing rights associated with those loans had a fair value of 8.7 million, or 72 basis points of the outstanding loan balances serviced. Total impairment reserves, which are available for recapture in future periods, totaled 1.7 million at the quarter-end. We anticipate the trend to continue with an increase in market rates accelerating in the latter half of 2010.

Economic environment continues to add stress on our investments and trust preferred collateralized debt obligations or CDOs and required additional other than temporary impairment write-downs in the first and the second quarter. The OTTI charge recognized in the second quarter of 2010 totaled 71,000, compared to a charge of 875,000 in the second quarter of 2009.

Trust Preferred CDO investments in the portfolio have a total book value of 3.8 million and market value is at 1.5 million at June 30, 2010. The book of CDOs with OTTI at June 30th has a 1.8 million book value with a market value of 521,000. The book of CDOs without credit impairment has 2 million with a market value of 1 million. The decline in the value of those investments is primarily due to the continue lack of liquidity in the CDO market.

These investments continue to pay principal and interest in accordance with the contractual terms of the securities. Management has not deemed the impairment and value of these CDO investments to be other than temporary and, therefore, has not recognized the reduction in value of those investments in earnings.

Turning to other operating results, our net interest income of 17.6 million for the quarter, compared with 17.1 million on a linked quarter basis and up from 16.2 million in the second quarter of 2009. For the quarter our margin was 3.89%, which was a 28 basis point increase from the second quarter of 2009 and a 4 basis point increase on a linked quarter basis.

The continued low rate environment has given us opportunity to re-price on the liability side and has also driven us to focus on changing the mix of our balance sheet to improve the margin as well. We've been successful in lowering our cost of funds, but the level of decrease has modified recently. Our cost of funds declined 8 basis points on a linked quarter basis with the yield on assets declining 5 basis points. We also have seen the downward pressure on overall asset yields and the downward re-pricing of variable rate loans. The increase in our liquidity position has also impacted the margin, but we believe our liquidity position continues to be important and gives us added flexibility and overall liability pricing.

We've been able to shift the asset mix somewhat this quarter from cash into intermediate-term securities. We continue have a strong emphasis on non-interest bearing deposit accounts and saw the balances grow this quarter. We're focused on pricing opportunity to maintain and expand the margin. We're particularly focused on asset pricing discipline.

We've had the opportunity to look at more credits and are concentrating on building the overall deposit balances of the relationship and the return on equity the relationship can generate. This helps us to focus on getting deposits and other revenue sources to make the relationship more profitable.

Fee income continues to be resilient and was 3.4 million in the second quarter of 2010 up from 3.2 million on linked quarter basis, compared with 3.3 million in the second quarter of 2009. Insurance revenue was 1.3 million in the second quarter of 2010 up slightly from the first quarter. The second quarter results include one month of revenue from the group benefits business line acquisition of approximately 75,000.

Overall, non-interest expense decreased to 15 million this quarter, compared with 16.1 million the second quarter of 2009. Second quarter compensation and benefits expense was down 996,000 or 13% from the first quarter of 2009. The second quarter of 2010 had lower levels of variable compensation, due to the overall level of our performance.

FDIC insurance expense decreased 568,000 in the second quarter of 2010, compared to the second quarter 2009. The reduction included 904,000 due to a special assessment in the second quarter of 2009, partially offset by rate increases on higher insured deposit balances.
Other non-interest expense increased to 3.8 million in the second quarter from 3 million in the second quarter of 2009. Increases in expenses of 254,000 for credit collection and OREO, consulting 253,000, attorneys and legal fees of 133,000, which was partially offset by 387,000 related to deferred compensation valuation.

On a linked-quarter, other non-interest expense increased to 3.8 million from 3.3 million. The second quarter 2010 included 346,000 related to the core system conversion scheduled for the fourth quarter of this year.

Our compensation and benefits expenses have been positively impacted by decisions to preemptively reduce staff levels, as well as to allow attrition to reduce staffing levels. We believe that we have a balanced approach to cost control in this difficult environment, as well as a sustained focus on customer service. We continue to look for opportunities to expand our market presence in strategic growth markets.

We saw the balance sheet contracting in the second quarter with total assets shrinking 20 million from March 2010 to 2.04 billion at June 30, 2010. On the asset side, cash and equivalents grew 33 million over the year to 122.1 million at June 30, 2010.

Securities grew 27 million over the year to 161 million, gross loans balance decline 39 million year-over-year, and declined 5 million on a linked-quarter basis. Loan activity in general continues to be weak, but we are seeing some signs of increased activity. We are intent on making sure service levels have not suffered as a result of an increased level of loan workouts. We have been able to develop strong new relationships with good commercial clients. We believe our controlled growth strategy is reflective of the environment, and we're well-positioned for future growth. Total deposits grew 27 million from June of 2009, and decreased 19 million on a linked quarter basis as we allowed higher priced CDs to run-off.

We are also pleased with our growth in non-interest bearing deposits to 190 million at June 30, 2010, up from 180 million at June 30, 2009. We continue to focus on growth in non-interest-bearing balances in correlation with an overall strategy, and efforts to reduce our cost of funds. Our capital position remains strong with shareholders' equity to assets improving to 11.7% at June 30, 2010 from 11.45% at March 31, 2010. Our risk-based capital ratio is strong at 13.51%.
That completes my overview for the quarter, and I'll turn the call back to Bill.

**William J. Small, President and Chief Executive Officer**
Thank you, Don. As we move into the second half of 2010, we are staying focused to address the challenges that face the entire banking industry. The overall economic climate throughout our market area remains among the biggest of these challenges. Unemployment numbers continue to run higher in this region, compared to national numbers, and we may see this continue for months as employment recovery seems tentative.

We're certainly encouraged by the fact that several of the automotive facilities in or near our market area are receiving substantial capital investments. As we have indicated in the past, First Federal Bank has a very small direct credit exposure to the automotive industry, but we know that many of our customers have great dependence on it. We are encouraged by the fact that many of these plants are increasing production, and we have heard reports from suppliers that new orders are being received, and there are plans for some to begin adding staff soon to meet these production needs.

The other significant challenge right now is the legislative and regulatory environment. Both Houses of Congress have now passed the financial regulatory reform bill and the President is expected to sign it into law this week. Several of the 16 titles in this act could have significant impact on our bank. We will be closely observing the task of writing the regulations and implementing them. We know for sure we will have a new primary regulator within a year as the Office of Thrift Supervision has been abolished, and we will subsequently be regulated by the Office of the Comptroller of the Currency.

The creation of the Consumer Financial Protection Bureau as a consumer watchdog will introduce another layer of regulatory oversight focused on consumer products. We will now be subject to direct examination of this bureau, but their power and influence is sure to be felt by all financial service providers. The saying goes that the devil is in the details, and for that reason, we will be keeping a close eye on the development of the regulatory details as they are formulated.
We are currently in the process of working with our existing customers on the new opt-in/opt-out requirements related to overdraft protection programs on debit and ATM transactions. This new regulation could have a large impact on a segment of significant fee income to the bank.
Our staff has been working hard to contact and educate customers on the ramifications of opting out of this service. We have had good early results for this effort, but we need to stay at this project as we potentially still have a significant amount of fee income at risk.

The additional challenges of this regulatory landscape and the continuing struggles of the economy certainly present a tough environment for the financial services industry. However, we have seen some positive indicators, and that gives us a sense of optimism for the future. Our focus needs to remain with our proven community financial service strategy, and with the staff and plan we have in place, we look forward to an improving future.

We thank you for joining us this morning, and now we would be happy to take your questions.

## QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] Our first question will come from John Barber from KBW. Please go ahead.

**<Q – John Barber>:** Good morning.

**<A – Donald Hileman>:** Good morning, John.

**<Q – John Barber>:** I know, Don, you touched on this in your prepared remarks, but could you talk about the margin outlook for the second half of the year? And what – do you think the company has room to lower deposit rates further?

**<A – Donald Hileman>:** Hi, John. I think we do – in my remarks I did talk about the slower of the pace that we've been able to lower deposit rates. But I think we still have some opportunity to continue the lowering.

**<Q – John Barber>:** Okay. And does company have any plans in place to repay TARP given that MPA is kind of stabilized over the past few quarters, or do you think it's still too early to start thinking about repaying TARP?

**<A – Donald Hileman>:** John, it's something that we've – from the outset, we've constantly keep an eye on it. We assess it. We have no immediate plans to move forward with repayment. We think we've got ourselves in a position that if we need to react quickly, we're prepared to do that. But we don't feel any compelling pressure at this point to move forward to pay off the TARP.

**<Q – John Barber>:** Okay, great. And the last question I had; I'm not sure if this is something you've disclosed before; but what percentage of service fees are NSF-related?

**<A – James Rohrs>:** I'm not sure if I have it right handy; John. A pretty high percentage of our fees would be NSF-related. I don't have the exact percentage.

**<Q – John Barber>:** Okay. That's all I had. Thank you.

**<A – Donald Hileman>:** Thanks, John.

Operator: [Operator Instructions] our next question will come from Christopher Marinac from Fig Partners Please go ahead.

**<Q – Christopher Marinac>:** Thanks. Good morning. Bill and Don, can you talk about TDRs and to what extent you are or are not using them and kind of what your guidance has been from your regulators on that topic?

**<A – Donald Hileman>:** I'll start, and then I'll probably let Jim answer some of that as well. And this is Don. Hi. Chris. Yeah, we are using and as I mentioned, we did see our TDRs going up this quarter as we were able to review some loans, modify them. And like I said most of what we classify as TDRs still, or all that we show separately as TDRs, are accruing interest. Our regulators have not given us any difficulty with that. I think we – don't tend to be overly aggressive in trying to move them out of TDRs too soon. We are generally looking at, at least a six-month pattern of repayment as agreed on those terms before we would re-classify anything out of TDR. And I would expect that we would see some increase in that balance as we start to move more credits that have the ability to repay into that category. Jim?

**<A – James Rohrs>:** This is Jim Rohrs. I'd agree with that. There are situations where keeping the borrower in the property, so to speak, is a good thing in terms of minimizing whatever potential loss there might be. We are very conservative in how we look at loans. If we give preferential treatment, we will classify that as a TDR which by definition is also a non-performing loan, whether we accrue interest on it or not. And as Don said, we typically would require at least a six-month period of time with the loan performing on normal terms as opposed to preferential terms before we would upgrade that out of troubled debt restructure. There are situations when it is the right thing to do.

**<Q – Christopher Marinac>:** Okay. And then are there situations where you take impairments on these just like you would look at any other non-accruing loan?

**<A – James Rohrs>:** Yes.

**<Q – Christopher Marinac>:** Okay., and so that's embedded in the charge-offs and provision expenses for you?

**<A – James Rohrs>:** In the provision, yes.

**<Q – Christopher Marinac>:** Okay. And one kind of related question just as are there any OREO write-downs that are embedded in the other non-interest expense?

**<A – James Rohrs>:** Yes. There is approximately –

**<A – James Rohrs>:** [inaudible] 600,000 entered for the quarter is the OREO, right now.

**<Q – Christopher Marinac>:** Okay. And do you bet what there would have been corresponding last quarter at Q1?

**<A – James Rohrs>:** Q1 would have been 421,000.

**<Q – Christopher Marinac>:** 421, great. Okay. Great. That's my third question. Thank you very much, guys.

**<A – James Rohrs>:** Thank you.

Operator: [Operator Instructions] Showing no questions, I would like to turn the conference back over to Mr. Small for any closing remarks.

**William J. Small, President, Chairman and Chief Executive Officer**
Thank you very much, Camille , and thank you, to everybody that joined us this morning and we look forward to chatting with you next quarter. Thanks, again.
Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.