

WASHINGTON FEDERAL INC  
Form 10-Q  
May 08, 2012  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q  
(Mark One)

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

For the quarterly period ended March 31, 2012

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 001-34654

WASHINGTON FEDERAL, INC.  
(Exact name of registrant as specified in its charter)

Washington  
(State or other jurisdiction of  
incorporation or organization)

91-1661606  
(I.R.S. Employer  
Identification No.)

425 Pike Street Seattle, Washington 98101  
(Address of principal executive offices and zip code)  
(206) 624-7930  
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

**APPLICABLE ONLY TO CORPORATE ISSUERS**

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

Title of class: \_\_\_\_\_ at May 4, 2012

Common stock, \$1.00 par value

106,875,953

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## WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

PART IItem 1. Financial Statements (Unaudited)

The Condensed Consolidated Financial Statements of Washington Federal, Inc. and Subsidiaries filed as a part of the report are as follows:

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION  
(UNAUDITED)

|  | March 31, 2012                    | September 30,<br>2011 |
|--|-----------------------------------|-----------------------|
|  | (In thousands, except share data) |                       |
| <b>ASSETS</b>  |                                   |                       |
| Cash and cash equivalents  | \$890,347                         | \$816,002             |
| Available-for-sale securities, including encumbered securities of \$1,001,116 and \$965,927, at fair value   | 3,687,625                         | 3,255,144             |
| Held-to-maturity securities, including encumbered securities of \$37,912 and \$45,086, at amortized cost   | 38,707                            | 47,036                |
| Loans receivable, net  | 7,676,017                         | 7,935,877             |
| Covered loans, net   | 321,634                           | 382,183               |
| Interest receivable  | 54,119                            | 52,332                |
| Premises and equipment, net  | 174,580                           | 166,593               |
| Real estate held for sale  | 120,095                           | 159,829               |
| Covered real estate held for sale  | 35,809                            | 56,383                |
| FDIC indemnification asset   | 100,875                           | 101,634               |
| FHLB stock   | 151,747                           | 151,755               |
| Intangible assets, net   | 257,250                           | 256,271               |
| Federal and state income taxes   | 4,406                             | —                     |
| Other assets   | 50,897                            | 59,710                |
|  | \$13,564,108                      | \$13,440,749          |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                                   |                       |
| <b>Liabilities</b>   |                                   |                       |
| Customer accounts  |                                   |                       |
| Transaction deposit accounts   | \$2,864,624                       | \$2,662,188           |
| Time deposit accounts  | 5,933,816                         | 6,003,715             |
|  | 8,798,440                         | 8,665,903             |
| FHLB advances  | 1,960,041                         | 1,962,066             |
| Other borrowings   | 800,000                           | 800,000               |
| Advance payments by borrowers for taxes and insurance  | 29,415                            | 39,548                |
| Federal and State income taxes   | —                                 | 1,535                 |
| Accrued expenses and other liabilities   | 68,155                            | 65,164                |
|  | 11,656,051                        | 11,534,216            |
| <b>Stockholders' equity</b>  |                                   |                       |
| Common stock, \$1.00 par value, 300,000,000 shares authorized;<br>129,919,851 and 129,853,534 shares issued; 106,867,527 and 108,976,410 shares<br>outstanding | 129,920                           | 129,854               |
| Paid-in capital  | 1,584,803                         | 1,582,843             |
| Accumulated other comprehensive income, net of taxes   | 65,183                            | 85,789                |
| Treasury stock, at cost; 23,052,324 and 20,877,124 shares  | (298,972)                         | (268,665)             |
| Retained earnings  | 427,123                           | 376,712               |
|  | 1,908,057                         | 1,906,533             |
|  | \$13,564,108                      | \$13,440,749          |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS



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CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

|   | Quarter Ended March 31,               |                  | Six Months Ended March 31, |                  |
|---|---------------------------------------|------------------|----------------------------|------------------|
|   | 2012                                  | 2011             | 2012                       | 2011             |
|   | (In thousands, except per share data) |                  |                            |                  |
| <b>INTEREST INCOME</b>  |                                       |                  |                            |                  |
| Loans   | \$ 123,772                            | \$ 128,634       | \$ 251,251                 | \$ 266,550       |
| Mortgage-backed securities  | 28,682                                | 26,163           | 54,978                     | 49,857           |
| Investment securities and cash equivalents  | 2,127                                 | 3,742            | 4,278                      | 7,722            |
|   | 154,581                               | 158,539          | 310,507                    | 324,129          |
| <b>INTEREST EXPENSE</b>   |                                       |                  |                            |                  |
| Customer accounts   | 22,016                                | 29,450           | 45,965                     | 62,184           |
| FHLB advances and other borrowings  | 27,963                                | 27,534           | 56,226                     | 55,656           |
|   | 49,979                                | 56,984           | 102,191                    | 117,840          |
| Net interest income   | 104,602                               | 101,555          | 208,316                    | 206,289          |
| Provision for loan losses   | 18,000                                | 30,750           | 29,209                     | 56,750           |
| Net interest income after provision for loan losses                                     | 86,602                                | 70,805           | 179,107                    | 149,539          |
| <b>OTHER INCOME</b>   |                                       |                  |                            |                  |
| Gain on sale of investments   | —                                     | 8,147            | —                          | 8,147            |
| Other   | 5,028                                 | 4,364            | 9,673                      | 8,790            |
|   | 5,028                                 | 12,511           | 9,673                      | 16,937           |
| <b>OTHER EXPENSE</b>  |                                       |                  |                            |                  |
| Compensation and benefits   | 20,185                                | 17,824           | 38,860                     | 35,547           |
| Occupancy   | 4,094                                 | 3,636            | 8,025                      | 7,151            |
| FDIC insurance premiums   | 4,350                                 | 5,100            | 8,543                      | 10,199           |
| Other   | 8,183                                 | 6,761            | 15,748                     | 14,703           |
|   | 36,812                                | 33,321           | 71,176                     | 67,600           |
| Loss on real estate acquired through foreclosure, net                                   | (1,582)                               | (9,645)          | (12,151)                   | (20,198)         |
| Income before income taxes  | 53,236                                | 40,350           | 105,453                    | 78,678           |
| Income tax provision  | 19,165                                | 14,526           | 37,964                     | 28,324           |
| <b>NET INCOME</b>   | <b>\$ 34,071</b>                      | <b>\$ 25,824</b> | <b>\$ 67,489</b>           | <b>\$ 50,354</b> |
| <b>PER SHARE DATA</b>   |                                       |                  |                            |                  |
| Basic earnings  | \$ 0.32                               | \$ 0.23          | \$ 0.63                    | \$ 0.45          |
| Diluted earnings  | 0.32                                  | 0.23             | 0.63                       | 0.45             |
| Cash dividends per share  | 0.08                                  | 0.06             | 0.16                       | 0.12             |
| Basic weighted average number of shares outstanding                                     | 107,198,829                           | 112,278,823      | 107,523,686                | 112,364,935      |
| Diluted weighted average number of shares outstanding, including dilutive stock options | 107,237,972                           | 112,411,414      | 107,549,396                | 112,447,927      |
| SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  |                                       |                  |                            |                  |

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(UNAUDITED)

|   | Quarter Ended March 31, |           | Six Months Ended March 31, |           |
|---|-------------------------|-----------|----------------------------|-----------|
|   | 2012                    | 2011      | 2012                       | 2011      |
|   | (In thousands)          |           |                            |           |
| Net income  | \$34,071                | \$25,824  | \$67,489                   | \$50,354  |
| Other comprehensive income net of tax:  |                         |           |                            |           |
| Net unrealized loss on available-for-sales securities,  |                         |           |                            |           |
| net of quarter-to-date tax of \$11,047 and \$9,055,   |                         |           |                            |           |
| and   |                         |           |                            |           |
| year-to-date tax of \$11,973 and \$18,652,  | (19,013                 | ) (20,738 | ) (20,606                  | ) (37,255 |
| respectively  |                         |           |                            |           |
| Reclassification adjustment of net gain from sale of available-for-sale securities included in net income | —                       | 5,153     | —                          | 5,153     |
| Other comprehensive income  | (19,013                 | ) (15,585 | ) (20,606                  | ) (32,102 |
| Comprehensive income  | \$15,058                | \$10,239  | \$46,883                   | \$18,252  |
| SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  |                         |           |                            |           |

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

|   | Six Months Ended |                |
|---|------------------|----------------|
|   | March 31, 2012   | March 31, 2011 |
|   | (In thousands)   |                |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                       |                  |                |
| Net income  | \$67,489         | \$50,354       |
| Adjustments to reconcile net income to net cash provided by operating activities: |                  |                |
| Amortization (accretion) of fees, discounts, premiums and intangible assets, net  | 20,703           | 15,792         |
| Cash received from (paid to) FDIC under loss share                                | (4,068           | ) 20,977       |
| Depreciation  | 3,750            | 3,300          |
| Stock option compensation expense   | 600              | 540            |
| Provision for loan losses   | 29,209           | 56,750         |
| Loss (gain) on real estate held for sale, net                                     | (1,285           | ) 12,051       |
| Increase in accrued interest receivable   | (1,536           | ) (2,835       |
| Increase in FDIC loss share receivable  | (2,052           | ) (1,183       |
| Increase in income taxes payable  | 6,031            | 18,072         |
| FHLB stock dividends  | 244              | (4             |
| Increase in intangible assets   | (1,061           | ) —            |
| Decrease in other assets  | 9,649            | 15,213         |
| Increase (decrease) in accrued expenses and other liabilities                     | 1,956            | (21,126        |
| Net cash provided by operating activities   | 129,629          | 167,901        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                       |                  |                |
| Net principal collections (loan originations)                                     | 342,513          | 361,916        |
| FHLB stock redemptions  | 1,512            | —              |
| Available-for-sale securities purchased   | (1,241,126       | ) (967,176     |
| Principal payments and maturities of available-for-sale securities                | 758,676          | 358,297        |
| Available-for-sale securities sold  | 3,500            | 131,361        |
| Principal payments and maturities of held-to-maturity securities                  | 8,394            | 28,146         |
| Net cash received from acquisition  | 50,451           | —              |
| Proceeds from sales of real estate held for sale                                  | 90,017           | 44,639         |
| Proceeds from sales of covered REO  | 22,959           | —              |
| Premises and equipment purchased  | (11,737          | ) (5,462       |
| Net cash provided (used) by investing activities                                  | 25,159           | (48,279        |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                       |                  |                |
| Net decrease in customer accounts   | (3,253           | ) (62,268      |
| Net decrease in borrowings  | (19,700          | ) (2,007       |
| Proceeds from exercise of common stock options                                    | 28               | 783            |
| Dividends paid on common stock  | (17,078          | ) (13,520      |
| Treasury stock purchased, net   | (30,307          | ) (10,604      |
| Decrease in advance payments by borrowers for taxes and insurance                 | (10,133          | ) (8,667       |
| Net cash used by financing activities   | (80,443          | ) (96,283      |
| Increase in cash and cash equivalents   | 74,345           | 23,339         |
| Cash and cash equivalents at beginning of period                                  | 816,002          | 888,622        |
| Cash and cash equivalents at end of period  | \$890,347        | \$911,961      |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS





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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)  
 (UNAUDITED)

|  | Six Months Ended |                |
|--|------------------|----------------|
|  | March 31, 2012   | March 31, 2011 |
|  | (In thousands)   |                |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>                 |                  |                |
| Non-cash investing activities  |                  |                |
| Non-covered real estate acquired through foreclosure                     | \$73,466         | \$53,398       |
| Covered real estate acquired through foreclosure                         | 6,304            | 33,075         |
| Cash paid during the period for  |                  |                |
| Interest   | 103,170          | 119,479        |
| Income taxes   | 31,947           | 10,252         |
| The following summarizes the non-cash activities related to acquisitions |                  |                |
| Fair value of assets acquired  | \$124,726        | \$—            |
| Fair value of liabilities assumed  | (154,500)        | ) —            |
| Net fair value of liabilities assumed                                    | (29,774)         | ) —            |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
QUARTERS AND SIX MONTHS ENDED MARCH 31, 2012 AND 2011  
(UNAUDITED)

NOTE A – Summary of Significant Accounting Policies

The consolidated unaudited interim financial statements included in this report have been prepared by Washington Federal, Inc. (“Company”). The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates and assumptions that affect amounts reported in the financial statements. Actual results could differ from these estimates. In the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation are reflected in the interim financial statements. The September 30, 2011 Consolidated Statement of Financial Condition was derived from audited financial statements.

The information included in this Form 10-Q should be read in conjunction with Company’s 2011 Annual Report on Form 10-K (“2011 Form 10-K”) as filed with the SEC. Interim results are not necessarily indicative of results for a full year.

Loans receivable – When a borrower defaults on a loan, the Company attempts to cure the deficiency by working with the borrower. In most cases, deficiencies are cured promptly, sometimes as a result of a negotiated modification of terms. If the delinquency is not promptly cured, and negotiations do not lead to a modification of terms, the Company may institute appropriate legal action to collect the loan, which may include foreclose of collateral. If foreclosed, the collateral will be liquidated in a reasonable time frame at prices available in the market place.

The Company will consider modifying the interest rates and terms of a loan if it determines that a modification is a better alternative to foreclosure.

Loans are placed on nonaccrual status when, in the judgment of management, the probability of collection of interest is deemed to be insufficient to warrant further accrual. When a loan is placed on nonaccrual status, previously accrued but unpaid interest is deducted from interest income. The Company does not accrue interest on loans 90 days past due or more. If payment is made on a loan so that the loan becomes less than 90 days past due, and the Company expects full collection of principal and interest, the loan is returned to full accrual status. Any interest ultimately collected is credited to income in the period of recovery. A loan is charged-off when the loss is estimable and it is confirmed that the borrower will not be able to meet its contractual obligations.

The Company maintains an allowance for loan losses to absorb losses inherent in the loan portfolio. The allowance is based on ongoing, quarterly assessments of the probable and estimable losses inherent in the loan portfolio. The Company’s methodology for assessing the appropriateness of the allowance consists of two components, which include the general allowance and specific allowances.

The general loan loss allowance is established by applying a loss percentage factor to the different loan types. Management believes loan types are the most relevant factor to group loans for the allowance calculation as the risk characteristics in these groups are similar. The loss percentage factor is made up of 2 parts – the historical loss factor (“HLF”) and the qualitative loss factor (“QLF”). The HLF takes into account historical charge-offs, while the QLF is determined by loan type and allows management to augment reserve levels to reflect the current environment and portfolio performance trends including recent charge-off trends. The allowances are provided based on Management’s continuing evaluation of the pertinent factors underlying the quality of the loan portfolio, including changes in the size and composition of the loan portfolio, actual loan loss experience, current economic conditions, collateral values, geographic concentrations, seasoning of the loan portfolio, specific industry conditions, and the duration of the current business cycle. The recovery of the carrying value of loans is susceptible to future market conditions beyond the Company’s control, which may result in losses or recoveries differing from those provided.

Specific allowances are established for loans which are individually evaluated, in cases where Management has identified significant conditions or circumstances related to a loan that Management believes indicate the probability that a loss has been incurred.

Impaired loans consist of loans receivable that are not expected to have their principal and interest repaid in accordance with their contractual terms. Collateral dependent impaired loans are measured using the fair value of the collateral, less selling costs. Non-collateral dependent loans are measured at the present value of expected future cash flows.

The Company receives fees for originating loans in addition to various fees and charges related to existing loans, which may include prepayment charges, late charges and assumption fees. Deferred loan fees and costs are recognized over the life of the loans using the effective interest method.

Off-Balance-Sheet Credit Exposures – The only material off-balance-sheet credit exposure is loans in process (“LIP”), which had a balance at March 31, 2012, excluding covered loans, of \$133,379,000. The Company estimates losses on LIP by including LIP

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
QUARTERS AND SIX MONTHS ENDED MARCH 31, 2012 AND 2011  
(UNAUDITED)

with the related principal balance outstanding and then applying its general reserve methodology to the gross amount. Certain reclassifications have been made to the financial statements to conform prior periods to current classifications.

NOTE B - Acquisitions

Western National Bank

Effective December 16, 2011, Washington Federal, acquired certain assets and liabilities, including most of the loans and deposits, of Western National Bank, headquartered in Phoenix, Arizona ("WNB") from the Federal Deposit Insurance Corporation ("FDIC") in an FDIC assisted transaction. Under the terms of the Purchase and Assumption Agreement, the Bank and the FDIC agreed to a discount of \$53 million on net assets and no loss sharing provision or premium on deposits.

WNB operated three full-service offices in Arizona. The Bank acquired certain assets with a book value of \$177 million, including \$143 million in loans and \$7 million in foreclosed real estate, and selected liabilities with a book value of \$153 million, including \$136 million in deposits. Pursuant to the purchase and assumption agreement with the FDIC, the Bank received a cash payment from the FDIC for \$30 million.

The acquisition was accounted for under the acquisition method of accounting. The purchased assets and assumed liabilities were recorded at their respective acquisition date estimated fair values. The purchase accounting for acquired assets and liabilities, mainly related to the valuation of the acquired loans, is subject to future adjustment based on the completion of valuations. The amounts currently recognized in the financial statements have been determined provisionally as we are completing a fair value analysis of those assets. Final purchase accounting adjustments are expected to be complete by fiscal year end. Loans that were classified as non-performing loans by WNB are no longer classified as non-performing because, at acquisition, the carrying value of these loans was adjusted to reflect fair value. Management believes that the new book value reflects an amount that will ultimately be collected.

South Valley Bancorp, Inc.

On April 4, 2012, the Company and South Valley Bancorp, Inc. ("South Valley") announced the signing of a definitive merger agreement. The merger agreement calls for the merger of South Valley with and into the Company, followed by the merger of South Valley's wholly owned subsidiary, South Valley Bank & Trust, into the Company's wholly owned subsidiary, Washington Federal. Under the terms of the definitive merger agreement, each outstanding share of South Valley common stock will be converted into the right to receive: (i) 0.2962 of a share of the Company's common stock, (ii) a contingent cash payment equal to the pro rata portion of an earn-out from the net proceeds collected from a pool of specified assets of South Valley with a value of approximately \$39 million as of March 31, 2012, and (iii) a contingent cash payment equal to the pro rata portion of the net proceeds, if any, received by South Valley from the sale of its trust business and/or wealth management business prior to the closing of the merger. Assuming a per share price of \$16.88 for the Company's common stock, the aggregate value of the stock portion of the merger consideration is approximately \$33.7 million. After consummation of the merger, the combined company will have 190 offices in eight western states with total assets of approximately \$14.4 billion and total deposits of approximately \$9.6 billion, based on financial results as of December 31, 2011. The merger is expected to close in the third calendar quarter of 2012, pending the receipt of all requisite regulatory approvals, the approval of South Valley's shareholders and the satisfaction of other customary closing conditions.

NOTE C – Dividends

On April 20, 2012, the Company paid its 117<sup>th</sup> consecutive quarterly cash dividend on common stock. Dividends per share were \$.08 and \$.06 for the quarters ended March 31, 2012 and 2011, respectively.

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 QUARTERS AND SIX MONTHS ENDED MARCH 31, 2012 AND 2011  
 (UNAUDITED)

## NOTE D – Loans Receivable (excluding Covered Loans)

|                                      | March 31, 2012<br>(In thousands) |      | September 30, 2011 |      |   |
|--------------------------------------|----------------------------------|------|--------------------|------|---|
| Non-acquired loans                   |                                  |      |                    |      |   |
| Single-family residential            | \$5,971,540                      | 74.4 | % \$6,218,878      | 74.7 | % |
| Construction - speculative           | 128,719                          | 1.6  | 140,459            | 1.9  |   |
| Construction - custom                | 235,566                          | 2.9  | 279,851            | 2.9  |   |
| Land - acquisition & development     | 151,967                          | 1.9  | 200,692            | 3.5  |   |
| Land - consumer lot loans            | 149,967                          | 1.9  | 163,146            | 2.1  |   |
| Multi-family                         | 686,467                          | 8.5  | 700,673            | 7.9  |   |
| Commercial real estate               | 293,234                          | 3.7  | 303,442            | 3.6  |   |
| Commercial & industrial              | 94,919                           | 1.2  | 109,332            | 1.0  |   |
| HELOC                                | 113,368                          | 1.4  | 115,092            | 1.3  |   |
| Consumer                             | 71,081                           | 0.9  | 67,509             | 1.1  |   |
| Total non-acquired loans             | 7,896,828                        | 98.4 | 8,299,074          | 100  |   |
| Credit-impaired acquired loans       |                                  |      |                    |      |   |
| Single-family residential            | 2,093                            | —    | —                  | —    |   |
| Construction - speculative           | 139                              | —    | —                  | —    |   |
| Construction - custom                | —                                | —    | —                  | —    |   |
| Land - acquisition & development     | 4,490                            | 0.1  | —                  | —    |   |
| Land - consumer lot loans            | —                                | —    | —                  | —    |   |
| Multi-family                         | 1,229                            | —    | —                  | —    |   |
| Commercial real estate               | 101,254                          | 1.2  | —                  | —    |   |
| Commercial & industrial              | 7,765                            | 0.1  | —                  | —    |   |
| HELOC                                | 17,215                           | 0.2  | —                  | —    |   |
| Consumer                             | 125                              | —    | —                  | —    |   |
| Total credit-impaired acquired loans | 134,310                          | 1.6  | —                  | —    |   |
| Total loans                          |                                  |      |                    |      |   |
| Single-family residential            | 5,973,633                        | 74.4 | 6,218,878          | 74.7 |   |
| Construction - speculative           | 128,858                          | 1.6  | 140,459            | 1.9  |   |
| Construction - custom                | 235,566                          | 2.9  | 279,851            | 2.9  |   |
| Land - acquisition & development     | 156,457                          | 2.0  | 200,692            | 3.5  |   |
| Land - consumer lot loans            | 149,967                          | 1.9  | 163,146            | 2.1  |   |
| Multi-family                         | 687,696                          | 8.5  | 700,673            | 7.9  |   |
| Commercial real estate               | 394,488                          | 4.9  | 303,442            | 3.6  |   |
| Commercial & industrial              | 102,684                          | 1.3  | 109,332            | 1.0  |   |
| HELOC                                | 130,583                          | 1.6  | 115,092            | 1.3  |   |
| Consumer                             | 71,206                           | 0.9  | 67,509             | 1.1  |   |
| Total loans                          | 8,031,138                        | 100  | % 8,299,074        | 100  | % |
| Less:                                |                                  |      |                    |      |   |
| Allowance for probable losses        | 143,819                          |      | 157,160            |      |   |
| Loans in process                     | 133,379                          |      | 170,229            |      |   |
| Discount on acquired loans           | 43,687                           |      | —                  |      |   |

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|                               |             |             |
|-------------------------------|-------------|-------------|
| Deferred net origination fees | 34,236      | 35,808      |
|                               | 355,121     | 363,197     |
|                               | \$7,676,017 | \$7,935,877 |

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The following table presents the changes in the accretable yield for credit impaired acquired loans as of March 31, 2012:

|                               | Credit impaired acquired loans |                          |
|-------------------------------|--------------------------------|--------------------------|
|                               | Accretable Yield               | Carrying Amount of Loans |
|                               | (In thousands)                 |                          |
| Balance as of October 1, 2011 | \$—                            | \$—                      |
| Additions                     | 21,606                         | 92,981                   |
| Accretion                     | (1,790                         | ) 1,790                  |
| Transfers to REO              | —                              | —                        |
| Payments received, net        | —                              | (4,148                   |
| Balance as of March 31, 2012  | \$19,816                       | \$90,623                 |

The following table sets forth information regarding non-accrual loans held by the Company as of the dates indicated:

|                                  | March 31, 2012 |      | September 30, 2011 |      |   |
|----------------------------------|----------------|------|--------------------|------|---|
|                                  | (In thousands) |      |                    |      |   |
| Non-accrual loans:               |                |      |                    |      |   |
| Single-family residential        | \$116,284      | 70.0 | % \$126,624        | 60.3 | % |
| Construction - speculative       | 8,190          | 4.9  | 15,383             | 7.3  |   |
| Construction - custom            | 539            | 0.3  | 635                | 0.3  |   |
| Land - acquisition & development | 25,036         | 15.1 | 37,339             | 17.7 |   |
| Land - consumer lot loans        | 5,641          | 3.4  | 8,843              | 4.2  |   |
| Multi-family                     | 4,530          | 2.7  | 7,664              | 3.6  |   |
| Commercial real estate           | 4,997          | 3.0  | 11,380             | 5.4  |   |
| Commercial & industrial          | 1              | —    | 1,679              | 0.8  |   |
| HELOC                            | 591            | 0.4  | 481                | 0.2  |   |
| Consumer                         | 344            | 0.2  | 437                | 0.2  |   |
| Total non-accrual loans          | \$166,153      | 100  | % \$210,465        | 100  | % |

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The following tables provide an analysis of the age of loans in past due status as of March 31, 2012 and September 30, 2011, respectively.

| March 31, 2012<br>Type of Loan       | Amount of Loans<br>Net of LIP & Chg.-Off<br>(In thousands) | Days Delinquent Based on \$ Amount of Loans |          |          |           |           | Total | % based<br>on \$ |
|--------------------------------------|--|---|----------|----------|-----------|-----------|-------|------------------|
|                                      |  | Current                                     | 30       | 60       | 90        |           |       |                  |
| Non-acquired loans                   |  |   |          |          |           |           |       |                  |
| Single-Family Residential            | \$5,969,973  | \$5,784,832                                 | \$45,826 | \$28,841 | \$110,474 | \$185,141 | 3.10  | %                |
| Construction - Speculative           | 102,654  | 97,455                                      | —        | 1,635    | 3,564     | 5,199     | 5.06  |                  |
| Construction - Custom                | 145,406  | 144,845                                     | —        | 22       | 539       | 561       | 0.39  |                  |
| Land - Acquisition & Development     | 146,228  | 125,100                                     | —        | 5,452    | 15,676    | 21,128    | 14.45 |                  |
| Land - Consumer Lot Loans            | 149,966  | 142,155                                     | 966      | 1,204    | 5,641     | 7,811     | 5.21  |                  |
| Multi-Family                         | 677,730  | 672,517                                     | —        | 683      | 4,530     | 5,213     | 0.77  |                  |
| Commercial Real Estate               | 292,143  | 286,778                                     | 672      | 1,950    | 2,743     | 5,365     | 1.84  |                  |
| Commercial & Industrial              | 94,901   | 94,895                                      | 5        | —        | 1         | 6         | 0.01  |                  |
| HELOC                                | 113,368  | 112,657                                     | 60       | 60       | 591       | 711       | 0.63  |                  |
| Consumer                             | 71,080   | 68,993                                      | 1,196    | 547      | 344       | 2,087     | 2.94  |                  |
| Total non-acquired loans             | 7,763,449  | 7,530,227                                   | 48,725   | 40,394   | 144,103   | 233,222   | 3.00  |                  |
| Credit-impaired acquired loans       |  |   |          |          |           |           |       |                  |
| Single-Family Residential            | 2,093  | 1,755                                       | 338      | —        | —         | 338       | 16.15 |                  |
| Construction - Speculative           | 139  | 139   | —        | —        | —         | —         | —     |                  |
| Construction - Custom                | —  | —   | —        | —        | —         | —         | —     |                  |
| Land - Acquisition & Development     | 4,490  | 3,937                                       | —        | —        | 553       | 553       | 12.32 |                  |
| Land - Consumer Lot Loans            | —  | —   | —        | —        | —         | —         | —     |                  |
| Multi-Family                         | 1,229  | 1,090                                       | 139      | —        | —         | 139       | 11.31 |                  |
| Commercial Real Estate               | 101,254  | 87,036                                      | 4,285    | 3,375    | 6,558     | 14,218    | 14.04 |                  |
| Commercial & Industrial              | 7,765  | 6,907                                       | 488      | 55       | 315       | 858       | 11.05 |                  |
| HELOC                                | 17,215   | 15,331                                      | —        | 1,084    | 800       | 1,884     | 10.94 |                  |
| Consumer                             | 125  | 89  | 36       | —        | —         | 36        | 28.80 |                  |
| Total credit-impaired acquired loans | 134,310  | 116,284                                     | 5,286    | 4,514    | 8,226     | 18,026    | 13.42 |                  |

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|             |             |             |          |          |           |           |      |
|-------------|-------------|-------------|----------|----------|-----------|-----------|------|
| Total loans | \$7,897,759 | \$7,646,511 | \$54,011 | \$44,908 | \$152,329 | \$251,248 | 3.18 |
|-------------|-------------|-------------|----------|----------|-----------|-----------|------|

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| September 30, 2011<br>Type of Loan | Amount of Loans<br>Net of LIP & Chg.-Off<br>(In thousands) | Days Delinquent Based on \$ Amount of Loans |          |          |           |           | Total | % based<br>on \$ |  |
|------------------------------------|--|---|----------|----------|-----------|-----------|-------|------------------|--|
|                                    |  | Current                                     | 30       | 60       | 90        |           |       |                  |  |
| Single-Family Residential          | \$6,217,670  | \$6,015,464                                 | \$54,140 | \$21,985 | \$126,082 | \$202,207 | 3.25  | %                |  |
| Construction - Speculative         | 115,409  | 106,843                                     | 330      | —        | 8,236     | 8,566     | 7.42  |                  |  |
| Construction - Custom              | 147,764  | 147,129                                     | —        | —        | 635       | 635       | 0.43  |                  |  |
| Land - Acquisition & Development   | 193,613  | 159,357                                     | 679      | —        | 33,577    | 34,256    | 17.69 |                  |  |
| Land - Consumer Lot Loans          | 163,146  | 151,849                                     | 1,163    | 1,291    | 8,843     | 11,297    | 6.92  |                  |  |
| Multi-Family                       | 699,340  | 690,765                                     | —        | 1,202    | 7,373     | 8,575     | 1.23  |                  |  |
| Commercial Real Estate             | 300,307  | 292,015                                     | 1,016    | —        | 7,276     | 8,292     | 2.76  |                  |  |
| Commercial & Industrial            | 108,995  | 106,708                                     | 55       | 553      | 1,679     | 2,287     | 2.10  |                  |  |
| HELOC                              | 115,092  | 114,059                                     | 452      | 100      | 481       | 1,033     | 0.90  |                  |  |
| Consumer                           | 67,509   | 65,434                                      | 1,191    | 446      | 437       | 2,074     | 3.07  |                  |  |
|                                    | \$8,128,845  | \$7,849,623                                 | \$59,026 | \$25,577 | \$194,619 | \$279,222 | 3.43  |                  |  |

Recently, most loans restructured in troubled debt restructurings ("TDRs") are accruing and performing loans where the borrower has proactively approached the Company about modification due to temporary financial difficulties. Each request is individually evaluated for merit and likelihood of success. The concession for these loans is typically a payment reduction through a rate reduction of between 100 to 200 basis points for a specific term, usually six to twelve months. Interest-only payments may also be approved during the modification period. Principal forgiveness is not an available option for restructured loans. As of March 31, 2012, single-family residential loans comprised 82.6% of TDRs.

The Company reserves for restructured loans within its allowance for loan loss methodology by taking into account the following performance indicators: 1) time since modification, 2) current payment status and 3) geographic area.

The following tables provide information related to loans that were restructured during the periods indicated:

|                                  | Quarter Ended March 31,<br>2012          |                                  | 2011                            |  |
|----------------------------------|--|----------------------------------|---------------------------------|--|
|                                  | Pre-Modification<br>Outstanding          | Post-Modification<br>Outstanding | Pre-Modification<br>Outstanding | Post-Modification<br>Outstanding         |
| Number<br>of<br>Contracts        | Recorded<br>Investment<br>(In thousands) | Recorded<br>Investment           | Number<br>of<br>Contracts       | Recorded<br>Investment<br>(In thousands) |
| Troubled Debt<br>Restructurings: |  |                                  |                                 |  |
| Single-Family Residential        | 312                                      | \$68,460                         | 26                              | \$7,019                                  |
|                                  |  | \$68,460                         |                                 | \$7,019                                  |

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|                                     |     |          |           |    |         |          |
|-------------------------------------|-----|----------|-----------|----|---------|----------|
| Construction -<br>Speculative       | 12  | 4,049    | 4,049     | —  | —       | —        |
| Construction - Custom               | —   | —        | —         | —  | —       | —        |
| Land - Acquisition &<br>Development | 4   | 1,823    | 1,823     | —  | —       | —        |
| Land - Consumer Lot<br>Loans        | 14  | 2,116    | 2,116     | 3  | 498     | 498      |
| Multi-Family                        | 2   | 1,871    | 1,871     | 2  | 951     | 951      |
| Commercial Real Estate              | —   | —        | —         | —  | —       | —        |
| Commercial & Industrial             | —   | —        | —         | —  | —       | —        |
| HELOC                               | —   | —        | —         | —  | —       | —        |
| Consumer                            | —   | —        | —         | —  | —       | —        |
|                                     | 344 | \$78,319 | \$ 78,319 | 31 | \$8,468 | \$ 8,468 |

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|  | Six Months Ended March 31,<br>2012 |  | 2011                             |                           | 2011                                     |                                  |
|--|------------------------------------|--|----------------------------------|---------------------------|--|----------------------------------|
|  | Number<br>of<br>Contracts          | Pre-Modification<br>Outstanding          | Post-Modification<br>Outstanding | Number<br>of<br>Contracts | Pre-Modification<br>Outstanding          | Post-Modification<br>Outstanding |
|  |                                    | Recorded<br>Investment<br>(In thousands) | Recorded<br>Investment           |                           | Recorded<br>Investment<br>(In thousands) | Recorded<br>Investment           |
| Troubled Debt Restructurings:                          |                                    |  |                                  |                           |  |                                  |
| Single-Family Residential                              | 491                                | \$ 121,145                               | \$ 121,145                       | 165                       | \$ 46,488                                | \$ 46,488                        |
| Construction - Speculative                             | 23                                 | 7,428                                    | 7,428                            | —                         | —  | —                                |
| Construction - Custom Land - Acquisition & Development | —                                  | —  | —                                | —                         | —  | —                                |
| Land - Consumer Lot Loans                              | 25                                 | 3,824                                    | 3,824                            | 13                        | 2,636                                    | 2,636                            |
| Multi-Family Commercial Real Estate                    | 2                                  | 1,871                                    | 1,871                            | 6                         | 8,182                                    | 8,182                            |
| Commercial & Industrial HELOC                          | 1                                  | 308                                      | 308                              | —                         | —  | —                                |
| Consumer   | 1                                  | 4  | 4                                | —                         | —  | —                                |
|  | —                                  | —  | —                                | —                         | —  | —                                |
|  | —                                  | —  | —                                | —                         | —  | —                                |
|  | 569                                | \$ 140,753                               | \$ 140,753                       | 184                       | \$ 57,306                                | \$ 57,306                        |

The following tables provide information on restructured loans for which a payment default occurred during the periods indicated and that had been modified as a TDR within 12 months or less of the payment default:

|   | Quarter Ended March 31,<br>2012 |  | 2011                   |  |
|---|---------------------------------|--|------------------------|--|
|   | Number of<br>Contracts          | Recorded<br>Investment<br>(In thousands) | Number of<br>Contracts | Recorded<br>Investment<br>(In thousands) |
| Troubled Debt Restructurings That Subsequently Defaulted: |                                 |  |                        |  |
| Single-Family Residential                                 | 108                             | \$ 20,419                                | 47                     | \$ 11,801                                |
| Construction - Speculative                                | —                               | —  | —                      | —  |
| Construction - Custom Land - Acquisition & Development    | —                               | —  | —                      | —  |
| Land - Consumer Lot Loans                                 | 5                               | 865                                      | 3                      | 710                                      |

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|                         |     |          |    |          |
|-------------------------|-----|----------|----|----------|
| Multi-Family            | —   | —        | 2  | 6,613    |
| Commercial Real Estate  | —   | —        | 1  | 222      |
| Commercial & Industrial | —   | —        | —  | —        |
| HELOC                   | —   | —        | —  | —        |
| Consumer                | —   | —        | —  | —        |
|                         | 113 | \$21,284 | 53 | \$19,346 |

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|   | Six Months Ended March 31, |                | 2011      |                |
|---|----------------------------|----------------|-----------|----------------|
|   | 2012                       | Recorded       | Number of | Recorded       |
|   | Number of                  | Investment     | Contracts | Investment     |
|   | Contracts                  | (In thousands) |           | (In thousands) |
| Troubled Debt Restructurings That Subsequently Defaulted: |                            |                |           |                |
| Single-Family Residential                                 | 125                        | \$24,783       | 87        | \$19,763       |
| Construction - Speculative                                | —                          | —              | —         | —              |
| Construction - Custom                                     | —                          | —              | —         | —              |
| Land - Acquisition & Development                          | —                          | —              | 1         | 4,505          |
| Land - Consumer Lot Loans                                 | 7                          | 1,312          | 4         | 831            |
| Multi-Family  | —                          | —              | 2         | 6,613          |
| Commercial Real Estate                                    | —                          | —              | 1         | 222            |
| Commercial & Industrial                                   | —                          | —              | —         | —              |
| HELOC   | —                          | —              | —         | —              |
| Consumer  | —                          | —              | —         | —              |
|   | 132                        | \$26,095       | 95        | \$31,934       |

## NOTE E – Allowance for Losses on Loans

The Company has an asset quality review function that analyzes its loan portfolios and reports the results of the review to the Board of Directors on a quarterly basis. The single-family residential, HELOC and consumer portfolios are evaluated based on their performance as a pool of loans, since no single loan is individually significant or judged by its risk rating, size or potential risk of loss. The construction, land, multi-family, commercial real estate and commercial and industrial loans are risk rated on a loan by loan basis to determine the relative risk inherent in specific borrowers or loans. Based on that risk rating, the loans are assigned a grade and classified as follows:

**Pass** – the credit does not meet one of the definitions below.

**Special mention** – A special mention credit is considered to be currently protected from loss but is potentially weak. No loss of principal or interest is foreseen; however, proper supervision and Management attention is required to deter further deterioration in the credit. Assets in this category constitute some undue and unwarranted credit risk but not to the point of justifying a risk rating of substandard. The credit risk may be relatively minor yet constitutes an unwarranted risk in light of the circumstances surrounding a specific asset.

**Substandard** – A substandard credit is an unacceptable credit. Additionally, repayment in the normal course is in jeopardy due to the existence of one or more well defined weaknesses. In these situations, loss of principal is likely if the weakness is not corrected. A substandard asset is inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. Assets so classified will have a well defined weakness or weaknesses that jeopardize the liquidation of the debt. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets risk rated substandard.

**Doubtful** – A credit classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weakness makes collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The probability of loss is high, but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and



refinancing plans.

Loss – Credits classified loss are considered uncollectible and of such little value that their continuance as a bankable asset is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this asset even though partial recovery may be affected in the future. Losses should be taken in the period in which they are identified as uncollectible. Partial charge-off versus full charge-off may be taken if the collateral offers some identifiable protection.

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The following table summarizes the activity in the allowance for loan losses for the quarter ended March 31, 2012 and fiscal year ended September 30, 2011:

| Quarter Ended March 31, 2012         | Beginning Allowance<br>(In thousands) | Charge-offs  | Recoveries | Provision & Transfers | Ending Allowance |
|--------------------------------------|---------------------------------------|--------------|------------|-----------------------|------------------|
| Single-family residential            | \$84,793                              | \$(15,086 )  | \$836      | \$13,332              | \$83,875         |
| Construction - speculative           | 14,640                                | (980 )       | —          | 2,283                 | 15,943           |
| Construction - custom                | 457                                   | —            | —          | (73 )                 | 384              |
| Land - acquisition & development     | 29,089                                | (11,738 )    | —          | 2,578                 | 19,929           |
| Land - consumer lot loans            | 8,283                                 | (687 )       | —          | 116                   | 7,712            |
| Multi-family                         | 6,543                                 | (106 )       | 9          | (1,609 )              | 4,837            |
| Commercial real estate               | 2,739                                 | (151 )       | 6          | 275                   | 2,869            |
| Commercial & industrial              | 4,421                                 | (111 )       | 53         | 64                    | 4,427            |
| HELOC                                | 972                                   | (76 )        | —          | 73                    | 969              |
| Consumer                             | 2,603                                 | (1,053 )     | 363        | 961                   | 2,874            |
|                                      | \$154,540                             | \$(29,988 )  | \$1,267    | \$18,000              | \$143,819        |
| Fiscal Year Ended September 30, 2011 | Beginning Allowance<br>(In thousands) | Charge-offs  | Recoveries | Provision & Transfers | Ending Allowance |
| Single-family residential            | \$47,160                              | \$(38,465 )  | \$3,072    | \$71,540              | \$83,307         |
| Construction - speculative           | 26,346                                | (13,197 )    | 2,143      | (1,464 )              | 13,828           |
| Construction - custom                | 770                                   | (237 )       | —          | 90                    | 623              |
| Land - acquisition & development     | 61,637                                | (39,797 )    | 2,271      | 8,608                 | 32,719           |
| Land - consumer lot loans            | 4,793                                 | (4,196 )     | —          | 4,923                 | 5,520            |
| Multi-family                         | 5,050                                 | (1,950 )     | 71         | 4,452                 | 7,623            |
| Commercial real estate               | 3,165                                 | (1,593 )     | 328        | 2,431                 | 4,331            |
| Commercial & industrial              | 6,193                                 | (4,733 )     | 1,925      | 1,714                 | 5,099            |
| HELOC                                | 586                                   | (939 )       | 185        | 1,307                 | 1,139            |
| Consumer                             | 7,394                                 | (4,602 )     | 1,429      | (1,250 )              | 2,971            |
|                                      | \$163,094                             | \$(109,709 ) | \$11,424   | \$92,351              | \$157,160        |

The Company recorded an \$18,000,000 provision for loan losses during the quarter ended March 31, 2012, while a \$30,750,000 provision was recorded for the same quarter one year ago. Non-performing assets (“NPAs”) amounted to \$286,248,000, or 2.11%, of total assets at March 31, 2012, compared to \$399,295,000, or 2.98%, of total assets one year ago. Acquired loans are not classified as non-performing loans because, at acquisition, the carrying value of these loan was adjusted to reflect fair value. Covered loans are not classified as non-performing loans because, at acquisition, the carrying value of these loans was adjusted to reflect fair value and are covered under FDIC loss sharing agreements. There was no additional provision for loan losses recorded on acquired or covered loans during the quarter ended March 31, 2012. Non-accrual loans decreased from \$221,736,000 at March 31, 2011, to \$166,153,000 at March 31, 2012, a 25.1% decrease. The Company had net charge-offs of \$28,721,000 for the quarter ended March 31, 2012, compared with \$26,421,000 of net charge-offs for the same quarter one year ago. A loan is charged-off when the loss is estimable and it is confirmed that the borrower will not be able to meet its contractual obligations. While the percentage of loans 30 days or more delinquent decreased from 3.37% at March 31, 2011, to

2.95% at March 31, 2012, delinquencies in the single-family residential portfolio, the largest portion of the loan portfolio, decreased from 3.33% at March 31, 2011, to 3.10% at March 31, 2012. While these asset quality trends are improving, real estate values remain under pressure in most of the Company's primary markets, thus the Company recorded a smaller provision for loan losses in the current quarter as compared to the same quarter one year ago. \$114,039,000 of the allowance was calculated under the formulas contained in our

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general allowance methodology and the remaining \$29,780,000 was made up of specific reserves on loans that were deemed to be impaired at March 31, 2012. For the period ending March 31, 2011, \$107,510,000 of the allowance was calculated under the formulas contained in our general allowance methodology and the remaining \$56,107,000 was made up of specific reserves on loans that were deemed to be impaired. The primary reasons for the shift in total allowance allocation from specific reserves to general reserves is due to the Company having already addressed many of the problem loans focused in the speculative construction and land A&D portfolios, combined with increased delinquencies and elevated charge-offs in the single-family residential portfolio.

The following tables shows a summary of loans collectively and individually evaluated for impairment and the related allocation of general and specific reserves as of March 31, 2012 and September 30, 2011:

| March 31, 2012                   | Loans Collectively Evaluated for Impairment |  |       | Loans Individually Evaluated for Impairment |   |       |   |
|----------------------------------|---|--|-------|---|---|-------|---|
|                                  | General Reserve Allocation                  | Gross Loans Subject to General Reserve (1) | Ratio | Specific Reserve Allocation                 | Gross Loans Subject to Specific Reserve (1) | Ratio |   |
|                                  | (In thousands)                              |  |       | (In thousands)                              |   |       |   |
| Single-family residential        | \$80,397                                    | \$ 5,920,650                               | 1.4   | % \$3,479                                   | \$ 50,890                                   | 6.8   | % |
| Construction - speculative       | 8,192                                       | 94,129                                     | 8.7   | 7,751                                       | 34,590                                      | 22.4  |   |
| Construction - custom            | 384   | 235,566                                    | 0.2   | —   | —   | —     |   |
| Land - acquisition & development | 6,339                                       | 44,765                                     | 14.2  | 13,589                                      | 107,202                                     | 12.7  |   |
| Land - consumer lot loans        | 6,672                                       | 147,703                                    | 4.5   | 1,040                                       | 2,264                                       | 45.9  |   |
| Multi-family                     | 2,727                                       | 671,367                                    | 0.4   | 2,110                                       | 15,100                                      | 14.0  |   |
| Commercial real estate           | 1,082                                       | 273,434                                    | 0.4   | 1,787                                       | 19,800                                      | 9.0   |   |
| Commercial & industrial          | 4,403                                       | 93,376                                     | 4.7   | 24  | 1,543                                       | 1.6   |   |
| HELOC                            | 969   | 113,368                                    | 0.9   | —   | —   | —     |   |
| Consumer                         | 2,874                                       | 71,080                                     | 4.0   | —   | —   | —     |   |
|                                  | \$114,039                                   | \$ 7,665,438                               | 1.4   | \$29,780                                    | \$ 231,389                                  | 12.9  |   |

(1) Excludes acquired and covered loans

| September 30, 2011               | Loans Collectively Evaluated for Impairment |  |       | Loans Individually Evaluated for Impairment |   |       |   |
|----------------------------------|---|--|-------|---|---|-------|---|
|                                  | General Reserve Allocation                  | Gross Loans Subject to General Reserve (1) | Ratio | Specific Reserve Allocation                 | Gross Loans Subject to Specific Reserve (1) | Ratio |   |
|                                  | (In thousands)                              |  |       | (In thousands)                              |   |       |   |
| Single-family residential        | \$77,441                                    | \$ 6,186,322                               | 1.3   | % \$5,866                                   | \$ 32,556                                   | 18.0  | % |
| Construction - speculative       | 6,969                                       | 89,986                                     | 7.7   | 6,859                                       | 50,473                                      | 13.6  |   |
| Construction - custom            | 623   | 279,851                                    | 0.2   | —   | —   | —     |   |
| Land - acquisition & development | 10,489                                      | 61,277                                     | 17.1  | 22,230                                      | 139,415                                     | 15.9  |   |
| Land - consumer lot loans        | 4,385                                       | 160,906                                    | 2.7   | 1,135                                       | 2,240                                       | 50.7  |   |
| Multi-family                     | 3,443                                       | 679,823                                    | 0.5   | 4,180                                       | 20,850                                      | 20.0  |   |
| Commercial real estate           | 2,730                                       | 268,906                                    | 1.0   | 1,601                                       | 34,536                                      | 4.6   |   |

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|                         |           |              |     |          |            |      |
|-------------------------|-----------|--------------|-----|----------|------------|------|
| Commercial & industrial | 5,058     | 106,406      | 4.8 | 41       | 2,926      | 1.4  |
| HELOC                   | 1,139     | 115,092      | 1.0 | —        | —          | —    |
| Consumer                | 2,971     | 67,509       | 4.4 | —        | —          | —    |
|                         | \$115,248 | \$ 8,016,078 | 1.4 | \$41,912 | \$ 282,996 | 14.8 |

(1) Excludes covered loans

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The following tables provide information on loans based on credit quality indicators (defined in Note A) as of March 31, 2012 and September 30, 2011:

Credit Risk Profile by Internally Assigned Grade (excludes covered loans):

| March 31, 2012                          | Internally Assigned Grade |                 |             |          |       | Total<br>Gross Loans |
|---|---------------------------|-----------------|-------------|----------|-------|----------------------|
|   | Pass<br>(In thousands)    | Special mention | Substandard | Doubtful | Loss  |                      |
| Non-acquired loans                      |                           |                 |             |          |       |                      |
| Single-family residential               | \$5,792,611               | \$300           | \$178,629   | \$—      | \$—   | \$5,971,540          |
| Construction - speculative              | 69,948                    | 8,885           | 49,886      | —        | —     | 128,719              |
| Construction - custom                   | 235,566                   | —               | —           | —        | —     | 235,566              |
| Land - acquisition & development        | 33,225                    | 19,801          | 98,941      | —        | —     | 151,967              |
| Land - consumer lot loans               | 149,243                   | 259             | 465         | —        | —     | 149,967              |
| Multi-family                            | 651,722                   | 6,735           | 28,010      | —        | —     | 686,467              |
| Commercial real estate                  | 255,328                   | 2,633           | 35,273      | —        | —     | 293,234              |
| Commercial & industrial                 | 91,621                    | 586             | 2,292       | —        | 420   | 94,919               |
| HELOC                                   | 113,368                   | —               | —           | —        | —     | 113,368              |
| Consumer                                | 70,123                    | 528             | 430         | —        | —     | 71,081               |
|   | 7,462,755                 | 39,727          | 393,926     | —        | 420   | 7,896,828            |
| Credit impaired acquired loans          |                           |                 |             |          |       |                      |
| Pool 1 - Construction and land A&D      | 2,567                     | —               | 2,062       | —        | —     | 4,629                |
| Pool 2 - Single-family residential      | —                         | —               | 2,093       | —        | —     | 2,093                |
| Pool 3 - Multi-family                   | 68                        | —               | 1,161       | —        | —     | 1,229                |
| Pool 4 - HELOC & other consumer         | 16,846                    | —               | —           | 494      | —     | 17,340               |
| Pool 5 - Commercial real estate         | 52,922                    | 11,040          | 36,189      | 987      | 116   | 101,254              |
| Pool 6 - Commercial & industrial        | 4,164                     | 993             | 2,189       | 419      | —     | 7,765                |
| Total credit impaired acquired loans    | 76,567                    | 12,033          | 43,694      | 1,900    | 116   | 134,310              |
| Total gross loans                       | \$7,539,322               | \$51,760        | \$437,620   | \$1,900  | \$536 | \$8,031,138          |
| Total grade as a % of total gross loans | 94.5                      | % 0.6           | % 4.9       | % —      | % —   | %                    |

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| September 30, 2011                      | Internally Assigned Grade |                 |             |          |       | Total<br>Gross Loans |
|---|---------------------------|-----------------|-------------|----------|-------|----------------------|
|   | Pass                      | Special mention | Substandard | Doubtful | Loss  |                      |
|   | (In thousands)            |                 |             |          |       |                      |
| Single-family residential               | \$6,047,279               | \$—             | \$171,599   | \$—      | \$—   | \$6,218,878          |
| Construction - speculative              | 56,485                    | 21,035          | 62,939      | —        | —     | 140,459              |
| Construction - custom                   | 279,851                   | —               | —           | —        | —     | 279,851              |
| Land - acquisition & development        | 44,888                    | 44,840          | 110,964     | —        | —     | 200,692              |
| Land - consumer lot loans               | 162,670                   | —               | 476         | —        | —     | 163,146              |
| Multi-family                            | 663,582                   | 4,629           | 32,462      | —        | —     | 700,673              |
| Commercial real estate                  | 264,083                   | 4,125           | 35,234      | —        | —     | 303,442              |
| Commercial & industrial                 | 104,171                   | 1,128           | 1,407       | 2,245    | 381   | 109,332              |
| HELOC                                   | 115,092                   | —               | —           | —        | —     | 115,092              |
| Consumer                                | 66,512                    | 528             | 469         | —        | —     | 67,509               |
|   | \$7,804,613               | \$76,285        | \$415,550   | \$2,245  | \$381 | \$8,299,074          |
| Total grade as a % of total gross loans | 94.1                      | % 0.9           | % 5.0       | % —      | % —   | %                    |

## Credit Risk Profile Based on Payment Activity (excludes acquired and covered loans):

| March 31, 2012                   | Performing Loans |                           | Non-Performing Loans |                           |   |
|----------------------------------|------------------|---------------------------|----------------------|---------------------------|---|
|                                  | Amount           | % of Total<br>Gross Loans | Amount               | % of Total<br>Gross Loans |   |
|                                  | (In thousands)   |                           |                      |                           |   |
| Single-family residential        | \$5,855,256      | 98.1                      | % \$116,284          | 1.9                       | % |
| Construction - speculative       | 120,529          | 93.6                      | 8,190                | 6.4                       |   |
| Construction - custom            | 235,027          | 99.8                      | 539                  | 0.2                       |   |
| Land - acquisition & development | 126,931          | 83.5                      | 25,036               | 16.5                      |   |
| Land - consumer lot loans        | 144,326          | 96.2                      | 5,641                | 3.8                       |   |
| Multi-family                     | 681,937          | 99.3                      | 4,530                | 0.7                       |   |
| Commercial real estate           | 288,237          | 98.3                      | 4,997                | 1.7                       |   |
| Commercial & industrial          | 94,918           | 100.0                     | 1                    | —                         |   |
| HELOC                            | 112,777          | 99.5                      | 591                  | 0.5                       |   |
| Consumer                         | 70,737           | 99.5                      | 344                  | 0.5                       |   |
|                                  | \$7,730,675      | 97.9                      | \$166,153            | 2.1                       |   |

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| September 30, 2011               | Performing Loans |                           | Non-Performing Loans |                           |   |
|----------------------------------|------------------|---------------------------|----------------------|---------------------------|---|
|                                  | Amount           | % of Total<br>Gross Loans | Amount               | % of Total<br>Gross Loans |   |
|                                  | (In thousands)   |                           |                      |                           |   |
| Single-family residential        | \$6,092,254      | 98.0                      | % \$126,624          | 2.0                       | % |
| Construction - speculative       | 125,076          | 89.0                      | 15,383               | 11.0                      |   |
| Construction - custom            | 279,216          | 99.8                      | 635                  | 0.2                       |   |
| Land - acquisition & development | 163,353          | 81.4                      | 37,339               | 18.6                      |   |
| Land - consumer lot loans        | 154,303          | 94.6                      | 8,843                | 5.4                       |   |
| Multi-family                     | 693,009          | 98.9                      | 7,664                | 1.1                       |   |
| Commercial real estate           | 292,062          | 96.2                      | 11,380               | 3.8                       |   |
| Commercial & industrial          | 107,653          | 98.5                      | 1,679                | 1.5                       |   |
| HELOC                            | 114,611          | 99.6                      | 481                  | 0.4                       |   |
| Consumer                         | 67,072           | 99.4                      | 437                  | 0.6                       |   |
|                                  | \$8,088,609      | 97.5                      | % \$210,465          | 2.5                       | % |



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The following table provides information on impaired loans based on loan types as of March 31, 2012 and September 30, 2011:

| March 31, 2012                      | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment  |                                 |
|-------------------------------------|---------------------|--------------------------|-------------------|------------------------------|---------------------------------|
|                                     |                     |                          |                   | Quarter Ended March 31, 2012 | Six Months Ended March 31, 2012 |
|                                     | (In thousands)      |                          |                   |                              |                                 |
| With no related allowance recorded: |                     |                          |                   |                              |                                 |
| Single-family residential           | \$51,677            | \$52,039                 | \$—               | \$26,012                     | \$17,652                        |
| Construction - speculative          | 8,127               | 10,341                   | —                 | 5,851                        | 5,963                           |
| Construction - custom               | —                   | —                        | —                 | —                            | —                               |
| Land - acquisition & development    | 27,521              | 59,792                   | —                 | 31,846                       | 32,913                          |
| Land - consumer lot loans           | 81                  | 81                       | —                 | 41                           | 27                              |
| Multi-family                        | 11,272              | 11,933                   | —                 | 8,721                        | 8,057                           |
| Commercial real estate              | 4,855               | 6,660                    | —                 | 3,203                        | 2,556                           |
| Commercial & industrial             | 201                 | 201                      | —                 | 103                          | 68                              |
| HELOC                               | 76                  | 76                       | —                 | 38                           | 25                              |
| Consumer                            | —                   | —                        | —                 | —                            | —                               |
|                                     | 103,810             | 141,123                  | —                 | 75,815                       | 67,261                          |
| With an allowance recorded:         |                     |                          |                   |                              |                                 |
| Single-family residential           | 332,053             | 332,053                  | 25,823            | 331,768                      | 336,505                         |
| Construction - speculative          | 27,751              | 27,751                   | 7,751             | 26,163                       | 25,511                          |
| Construction - custom               | —                   | —                        | —                 | —                            | —                               |
| Land - acquisition & development    | 30,521              | 31,397                   | 13,590            | 30,921                       | 31,138                          |
| Land - consumer lot loans           | 250                 | 250                      | 1,040             | 251                          | 251                             |
| Multi-family                        | 11,352              | 11,352                   | 2,110             | 11,370                       | 11,386                          |
| Commercial real estate              | 6,587               | 6,587                    | 1,787             | 6,413                        | 6,484                           |
| Commercial & industrial             | 24                  | 24                       | 24                | 29                           | 33                              |
| HELOC                               | —                   | —                        | —                 | —                            | —                               |
| Consumer                            | —                   | —                        | —                 | —                            | —                               |
|                                     | 408,538             | 409,414                  | 52,125            | (1) 406,915                  | 411,308                         |
| Total:                              |                     |                          |                   |                              |                                 |
| Single-family residential           | 383,730             | 384,092                  | 25,823            | 357,780                      | 354,157                         |
| Construction - speculative          | 35,878              | 38,092                   | 7,751             | 32,014                       | 31,474                          |
| Construction - custom               | —                   | —                        | —                 | —                            | —                               |
| Land - acquisition & development    | 58,042              | 91,189                   | 13,590            | 62,767                       | 64,051                          |
| Land - consumer lot loans           | 331                 | 331                      | 1,040             | 292                          | 278                             |
| Multi-family                        | 22,624              | 23,285                   | 2,110             | 20,091                       | 19,443                          |
| Commercial real estate              | 11,442              | 13,247                   | 1,787             | 9,616                        | 9,040                           |
| Commercial & industrial             | 225                 | \$225                    | 24                | 132                          | 101                             |
| HELOC                               | 76                  | 76                       | —                 | 38                           | 25                              |
| Consumer                            | —                   | —                        | —                 | —                            | —                               |
|                                     | \$512,348           | \$550,537                | \$52,125          | (1) \$482,730                | \$478,569                       |

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(1)Includes \$29,781,000 of specific reserves and \$22,344,000 included in the general reserves.

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| September 30, 2011                  | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance | Average<br>Recorded<br>Investment |
|-------------------------------------|------------------------|--------------------------------|----------------------|-----------------------------------|
|                                     | (In thousands)         |                                |                      |                                   |
| With no related allowance recorded: |                        |                                |                      |                                   |
| Single-family residential           | \$5,597                | \$9,575                        | \$—                  | \$5,935                           |
| Construction - speculative          | 8,286                  | 11,026                         | —                    | 7,374                             |
| Construction - custom               | —                      | —                              | —                    | —                                 |
| Land - acquisition & development    | 22,436                 | 50,970                         | —                    | 28,168                            |
| Land - consumer lot loans           | —                      | —                              | —                    | —                                 |
| Multi-family                        | 3,233                  | 4,508                          | —                    | 4,058                             |
| Commercial real estate              | 3,462                  | 3,963                          | —                    | 2,141                             |
| Commercial & industrial             | —                      | —                              | —                    | —                                 |
| HELOC                               | —                      | —                              | —                    | —                                 |
| Consumer                            | —                      | —                              | —                    | —                                 |
|                                     | 43,014                 | 80,042                         | —                    | 47,676                            |
| With an allowance recorded:         |                        |                                |                      |                                   |
| Single-family residential           | 331,546                | 331,546                        | 29,378               | 261,736                           |
| Construction - speculative          | 29,255                 | 29,255                         | 6,859                | 26,385                            |
| Construction - custom               | —                      | —                              | —                    | —                                 |
| Land - acquisition & development    | 49,036                 | 49,912                         | 22,230               | 41,006                            |
| Land - consumer lot loans           | 352                    | 352                            | 1,135                | 110                               |
| Multi-family                        | 17,149                 | 17,149                         | 4,180                | 12,380                            |
| Commercial real estate              | 6,429                  | 6,429                          | 1,601                | 3,351                             |
| Commercial & industrial             | 41                     | 41                             | 41                   | 31                                |
| HELOC                               | —                      | —                              | —                    | —                                 |
| Consumer                            | —                      | —                              | —                    | —                                 |
|                                     | 433,808                | 434,684                        | 65,424               | (1) 344,999                       |
| Total:                              |                        |                                |                      |                                   |
| Single-family residential           | 337,143                | 341,121                        | 29,378               | 267,671                           |
| Construction - speculative          | 37,541                 | 40,281                         | 6,859                | 33,759                            |
| Construction - custom               | —                      | —                              | —                    | —                                 |
| Land - acquisition & development    | 71,472                 | 100,882                        | 22,230               | 69,174                            |
| Land - consumer lot loans           | 352                    | 352                            | 1,135                | 110                               |
| Multi-family                        | 20,382                 | 21,657                         | 4,180                | 16,438                            |
| Commercial real estate              | 9,891                  | 10,392                         | 1,601                | 5,492                             |
| Commercial & industrial             | 41                     | 41                             | 41                   | 31                                |
| HELOC                               | —                      | —                              | —                    | —                                 |
| Consumer                            | —                      | —                              | —                    | —                                 |
|                                     | \$476,822              | \$514,726                      | \$65,424             | (1) \$392,675                     |

(1) Includes \$41,912,000 of specific reserves and \$23,512,000 included in the general reserves.



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NOTE F – New Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2011-11, Balance Sheet (Topic 210) – Disclosures about Offsetting Assets and Liabilities. The amendments in this ASU will enhance disclosures required by U.S. GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with current U.S. GAAP or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with current U.S. GAAP. The guidance in this ASU is effective for the first interim or annual period beginning on or after January 1, 2013 and should be applied retrospectively. This new guidance is not expected to have a material impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-12, Comprehensive Income (Topic 220) – Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. Under the amendments in ASU 2011-05, entities are required to present reclassification adjustments and the effect of those reclassification adjustments on the face of the financial statements where net income is presented, by component of net income, and on the face of the financial statements where other comprehensive income is presented, by component of other comprehensive income. In addition, the amendments in ASU 2011-05 require that reclassification adjustments be presented in interim financial periods. The amendments in ASU 2011-12 supersede and defer changes to those paragraphs in ASU 2011-05 that pertain to how, when and where reclassification adjustments are presented while the FASB redeliberates the presentation of reclassification adjustments. All other requirements of ASU 2011-05 are not affected by ASU 2011-12.

NOTE G – Fair Value Measurements

U.S. GAAP defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U.S. GAAP also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active exchange markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

We have established and documented the Company's process for determining the fair values of our assets and liabilities, where applicable. Fair value is based on quoted market prices, when available, for identical or similar assets or liabilities. In the absence of quoted market prices, fair value is determined using valuation models or third-party appraisals. The following is a description of the valuation methodologies used to measure and report the fair value of financial assets and liabilities on a recurring or nonrecurring basis:

Measured on a Recurring Basis

Securities

Securities available for sale are recorded at fair value on a recurring basis. Securities at fair value are priced using model pricing based on the securities' relationship to other benchmark quoted prices as provided by an independent

third party, and under the provisions of the Fair Value Measurements and Disclosures topic of the FASB Accounting Standards Codification are considered a Level 2 input method.

The following table presents the balance of assets measured at fair value on a recurring basis at March 31, 2012:

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|  | Fair Value at March 31, 2012 |             |         | Total       |
|--|------------------------------|-------------|---------|-------------|
|  | Level 1                      | Level 2     | Level 3 |             |
|  | (In thousands)               |             |         |             |
| Available-for-sale securities                    |                              |             |         |             |
| Equity securities                                | \$—                          | \$—         | \$—     | \$—         |
| Obligations of U.S. government                   | —                            | 14,142      | —       | 14,142      |
| Obligations of states and political subdivisions | —                            | 23,500      | —       | 23,500      |
| Obligations of foreign governments               | —                            | —           | —       | —           |
| Corporate debt securities                        | —                            | 277,586     | —       | 277,586     |
| Mortgage-backed securities                       |                              |             |         |             |
| Agency pass-through certificates                 | —                            | 3,372,397   | —       | 3,372,397   |
| Other debt securities                            | —                            | —           | —       | —           |
| Balance at end of period                         | \$—                          | \$3,687,625 | \$—     | \$3,687,625 |

There were no transfers between, into and/or out of Levels 1, 2 or 3 during the quarter ended March 31, 2012.

Measured on a Nonrecurring Basis

Impaired Loans & Real Estate Held for Sale

From time to time, and on a nonrecurring basis, fair value adjustments to collateral-dependent loans and real estate held for sale are recorded to reflect write-downs of principal balances based on the current appraised or estimated value of the collateral. When management determines that the fair value of the collateral or the real estate held for sale requires additional adjustments, either as a result of a non-current appraisal value or when there is no observable market price, the Company classifies the impaired loan or real estate held for sale as Level 3. Level 3 assets recorded at fair value on a nonrecurring basis at March 31, 2012 included loans for which a specific reserve allowance was established or a partial charge-off was recorded based on the fair value of collateral, as well as covered REO and real estate held for sale for which fair value of the properties was less than the cost basis.

Real estate held for sale consists principally of properties acquired through foreclosure.

The following table presents the aggregated balance of assets measured at estimated fair value on a nonrecurring basis through the quarter ended March 31, 2012, and the total losses resulting from those fair value adjustments for the quarter and six months ended March 31, 2012. The following estimated fair values are shown gross of estimated selling costs:

|                               | Through March 31, 2012 |         |           |           | Quarter Ended  | Six Months Ended |
|-------------------------------|------------------------|---------|-----------|-----------|----------------|------------------|
|                               | Level 1                | Level 2 | Level 3   | Total     | March 31, 2012 | March 31, 2012   |
|                               | (In thousands)         |         |           |           | Total Losses   |                  |
| Impaired loans (1)            | \$—                    | \$—     | \$81,219  | \$81,219  | \$21,831       | \$22,832         |
| Covered REO (2)               | —                      | —       | 24,915    | 24,915    | 500            | 1,201            |
| Real estate held for sale (2) | —                      | —       | 106,728   | 106,728   | 18,380         | 39,344           |
| Balance at end of period      | \$—                    | \$—     | \$212,862 | \$212,862 | \$40,711       | \$63,377         |

(1) The losses represents remeasurements of collateral-dependent loans.

(2) The losses represents aggregate writedowns and charge-offs on real estate held for sale.

There were no liabilities carried at fair value, measured on a recurring or nonrecurring basis, at March 31, 2012.

The following describes the process used to value Level 3 assets:

Impaired loans - The Company adjusts the carrying amount of impaired loans when there is evidence of probable loss and the expected fair value of the loan is less than its contractual amount. The amount of the impairment may be determined based on



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the estimated present value of future cash flows or the fair value of the underlying collateral. Impaired loans with a specific reserve allowance based on cash flow analysis or the value of the underlying collateral are classified as Level 3 assets.

The evaluations for impairment are prepared by the Problem Loan Review Committee, which is chaired by the Chief Credit Officer and includes the Loan Review manager and Special Credits manager, as well as senior credit officers, division managers and group executives, as applicable. These evaluations are performed in conjunction with the quarterly allowance for loan loss ("ALLL") process.

Applicable loans are evaluated for impairment on a quarterly basis. Loans included in the previous quarter's review are reevaluated and if their values are materially different from the prior quarter evaluation, the underlying information (loan balance and collateral value) are compared. Material differences are evaluated for reasonableness and discussions are held between the relationship manager and their division manager to understand the difference and determine if any adjustment is necessary. The inputs are developed and substantiated on a quarterly basis, based on current borrower developments, market conditions and collateral values. The following method is used to value impaired loans:

The fair value of the collateral, which may take the form of real estate or personal property, is based on internal estimates, field observations, assessments provided by third-party appraisers and other valuation models. The Company performs or reaffirms valuations of collateral-dependent impaired loans at least annually. Adjustments are made if management believes that more recent information is available and relevant with respect to the fair value of the collateral.

Real estate held for sale ("OREO") - These assets are valued based on inputs such as appraisals and third-party price opinions, less estimated selling costs. Assets that are acquired through foreclosure are recorded initially at the lower of the loan balance or fair value at the date of foreclosure. After foreclosure, valuations are updated periodically, and current market conditions may require the assets to be written down further to a new cost basis. The following method is used to value real estate held for sale:

When a loan is reclassified from loan status to real estate held for sale due to the Company taking possession of the collateral, a Special Credits officer, along with the Special Credits manager, obtains a valuation, which may include a third-party appraisal, which is used to establish the fair value of the underlying collateral. The determined fair value, to the extent it does not exceed the carrying value of the loan, becomes the carrying value of the OREO asset. In addition to the valuations from independent third-party sources, the carrying balance of OREO assets are written down once a bona fide offer is contractually accepted, through execution of a Purchase and Sale Agreement, where the accepted price is lower than the current balance of the particular OREO asset. The fair value of OREO assets is re-evaluated quarterly and the OREO asset is adjusted to reflect the lower of cost or fair value as necessary.

**Fair Values of Financial Instruments**

U. S. GAAP requires disclosure of fair value information about financial instruments, whether or not recognized on the statement of financial condition, for which it is practicable to estimate those values. Certain financial instruments and all non-financial instruments are excluded from the disclosure requirements. Accordingly, the aggregate fair value estimates presented do not reflect the underlying fair value of the Company. Although management is not aware of any factors that would materially affect the estimated fair value amounts presented below, such amounts have not been comprehensively revalued for purposes of these financial statements since the dates shown, and therefore, estimates of fair value subsequent to those dates may differ significantly from the amounts presented below.

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|  | Level in Fair Value Hierarchy | March 31, 2012  |                      | September 30, 2011 |                      |
|--|-------------------------------|-----------------|----------------------|--------------------|----------------------|
|  |                               | Carrying Amount | Estimated Fair Value | Carrying Amount    | Estimated Fair Value |
| (In thousands)                                   |                               |                 |                      |                    |                      |
| Financial assets                                 |                               |                 |                      |                    |                      |
| Cash and cash equivalents                        | 1                             | \$890,347       | \$890,347            | \$816,002          | \$816,002            |
| Available-for-sale securities                    | 2                             |                 |                      |                    |                      |
| Equity securities                                |                               | —               | —                    | —                  | —                    |
| Obligations of U.S. government                   |                               | 14,142          | 14,142               | 190,527            | 190,527              |
| Obligations of states and political subdivisions |                               | 23,500          | 23,500               | 23,568             | 23,568               |
| Obligations of foreign governments               |                               | —               | —                    | —                  | —                    |
| Corporate debt securities                        |                               | 277,586         | 277,586              | 29,959             | 29,959               |
| Mortgage-backed securities                       |                               |                 |                      |                    |                      |
| Agency pass-through certificates                 |                               | 3,372,397       | 3,372,397            | 3,011,090          | 3,011,090            |
| Other debt securities                            |                               | —               | —                    | —                  | —                    |
| Total available-for-sale securities              |                               | 3,687,625       | 3,687,625            | 3,255,144          | 3,255,144            |
| Held-to-maturity securities                      | 2                             |                 |                      |                    |                      |
| Equity securities                                |                               | —               | —                    | —                  | —                    |
| Obligations of U.S. government                   |                               | —               | —                    | —                  | —                    |
| Obligations of states and political subdivisions |                               | 795             | 823                  | 1,950              | 2,023                |
| Obligations of foreign governments               |                               | —               | —                    | —                  | —                    |
| Corporate debt securities                        |                               | —               | —                    | —                  | —                    |
| Mortgage-backed securities                       |                               |                 |                      |                    |                      |
| Agency pass-through certificates                 |                               | 37,912          | 40,967               | 45,086             | 48,593               |
| Other debt securities                            |                               | —               | —                    | —                  | —                    |
| Total held-to-maturity securities                |                               | 38,707          | 41,790               | 47,036             | 50,616               |
| Loans receivable                                 | 3                             | 7,717,088       | 8,342,403            | 7,935,877          | 8,479,307            |
| Covered loans                                    | 3                             | 321,634         | 315,179              | 382,183            | 375,027              |
| FDIC indemnification asset                       | 3                             | 100,875         | 98,495               | 98,871             | 101,751              |
| FHLB stock                                       | 2                             | 151,747         | 151,747              | 151,755            | 151,755              |
| Financial liabilities                            |                               |                 |                      |                    |                      |
| Customer accounts                                | 2                             | 8,798,440       | 8,513,457            | 8,665,903          | 8,557,357            |
| FHLB advances and other borrowings               | 2                             | 2,760,041       | 3,113,854            | 2,762,066          | 3,038,127            |

The following methods and assumptions were used to estimate the fair value of financial instruments:

Cash and cash equivalents – The carrying amount of these items is a reasonable estimate of their fair value.

Available-for-sale securities and held-to-maturity securities – Securities at fair value are priced using model pricing based on the securities' relationship to other benchmark quoted prices as provided by an independent third party, and under the provisions of the Fair Value Measurements and Disclosures topic of the FASB Accounting Standards Codification are considered a Level 2

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input method.

Loans receivable and covered loans – For certain homogeneous categories of loans, such as fixed- and variable-rate residential mortgages, fair value is estimated for securities backed by similar loans, adjusted for differences in loan characteristics, using the same methodology described above for AFS and HTM securities. The fair value of other loan types is estimated by discounting the future cash flows and estimated prepayments using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining term. Some loan types were valued at carrying value because of their floating rate or expected maturity characteristics. Net deferred loan fees are not included in the fair value calculation but are included in the carrying amount.

FDIC indemnification asset – The fair value of the indemnification asset is estimated by discounting the expected future cash flows using the current rates.

FHLB stock – The fair value is based upon the par value of the stock which equates to its carrying value.

Customer accounts – The fair value of demand deposits, savings accounts, and money market accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated by discounting the estimated future cash flows using the rates currently offered for deposits with similar remaining maturities.

FHLB advances and other borrowings – The fair value of FHLB advances and other borrowings is estimated by discounting the estimated future cash flows using rates currently available to the Company for debt with similar remaining maturities.

The following is a reconciliation of amortized cost to fair value of available-for-sale and held-to-maturity securities:

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|  | March 31, 2012                      |                |                      |               |       |   |
|--|-------------------------------------|----------------|----------------------|---------------|-------|---|
|  | Amortized<br>Cost<br>(In thousands) | Gross<br>Gains | Unrealized<br>Losses | Fair<br>Value | Yield |   |
| Available-for-sale securities                |                                     |                |                      |               |       |   |
| U.S. government and agency securities<br>due |                                     |                |                      |               |       |   |
| Within 1 year                                | \$500                               | \$32           | \$—                  | \$532         | 4.00  | % |
| 1 to 5 years                                 | —                                   | —              | —                    | —             | —     |   |
| 5 to 10 years                                | 9,300                               | 4,310          | —                    | 13,610        | 10.38 |   |
| Over 10 years                                | —                                   | —              | —                    | —             | —     |   |
| Corporate bonds due                          |                                     |                |                      |               |       |   |
| 1 to 5 years                                 | 250,000                             | —              | (1,448               | ) 248,552     | 0.89  |   |
| 5 to 10 years                                | 30,000                              | 234            | (1,200               | ) 29,034      | 4.00  |   |
| Municipal bonds due                          |                                     |                |                      |               |       |   |
| Over 10 years                                | 20,451                              | 3,049          | —                    | 23,500        | 6.45  |   |
| Mortgage-backed securities                   |                                     |                |                      |               |       |   |
| Agency pass-through certificates             | 3,274,318                           | 100,861        | (2,782               | ) 3,372,397   | 4.54  |   |
|  | 3,584,569                           | 108,486        | (5,430               | ) 3,687,625   | 4.31  |   |
| Held-to-maturity securities                  |                                     |                |                      |               |       |   |
| Tax-exempt municipal bonds due               |                                     |                |                      |               |       |   |
| 1 to 5 years                                 | —                                   | —              | —                    | —             | —     |   |
| 5 to 10 years                                | 795                                 | 28             | —                    | 823           | 5.65  |   |
| Over 10 years                                | —                                   | —              | —                    | —             | —     |   |
| U.S. government and agency securities<br>due |                                     |                |                      |               |       |   |
| 1 to 5 years                                 | —                                   | —              | —                    | —             | —     |   |
| Mortgage-backed securities                   |                                     |                |                      |               |       |   |
| Agency pass-through certificates             | 37,912                              | 3,055          | —                    | 40,967        | 5.31  |   |
|  | 38,707                              | 3,083          | —                    | 41,790        | 5.32  |   |
|  | \$3,623,276                         | \$111,569      | \$(5,430             | ) \$3,729,415 | 4.32  | % |

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|   | September 30, 2011               |             |                   | Fair Value  | Yield |   |
|---|----------------------------------|-------------|-------------------|-------------|-------|---|
|   | Amortized Cost<br>(In thousands) | Gross Gains | Unrealized Losses |             |       |   |
| Available-for-sale securities             |                                  |             |                   |             |       |   |
| U.S. government and agency securities due |                                  |             |                   |             |       |   |
| Within 1 year                             | \$500                            | \$34        | \$—               | \$534       | 4.00  | % |
| 1 to 5 years                              | —                                | —           | —                 | —           | —     |   |
| 5 to 10 years                             | 9,300                            | 4,547       | —                 | 13,847      | 10.38 |   |
| Over 10 years                             | 175,515                          | 631         | —                 | 176,146     | 2.57  |   |
| Corporate bonds due                       |                                  |             |                   |             |       |   |
| 5 to 10 years                             | 30,000                           | 284         | (325)             | 29,959      | 4.00  |   |
| Municipal bonds due                       |                                  |             |                   |             |       |   |
| Over 10 years                             | 20,461                           | 3,107       | —                 | 23,568      | 6.45  |   |
| Mortgage-backed securities                |                                  |             |                   |             |       |   |
| Agency pass-through certificates          | 2,883,734                        | 127,356     | —                 | 3,011,090   | 4.72  |   |
|   | 3,119,510                        | 135,959     | (325)             | 3,255,144   | 4.62  |   |
| Held-to-maturity securities               |                                  |             |                   |             |       |   |
| Tax-exempt municipal bonds due            |                                  |             |                   |             |       |   |
| 1 to 5 years                              | 405                              | 5           | —                 | 410         | 6.52  |   |
| 5 to 10 years                             | 1,545                            | 68          | —                 | 1,613       | 5.60  |   |
| Over 10 years                             | —                                | —           | —                 | —           | —     |   |
| U.S. government and agency securities due |                                  |             |                   |             |       |   |
| 1 to 5 years                              | —                                | —           | —                 | —           | —     |   |
| Mortgage-backed securities                |                                  |             |                   |             |       |   |
| Agency pass-through certificates          | 45,086                           | 3,507       | —                 | 48,593      | 5.31  |   |
|   | 47,036                           | 3,580       | —                 | 50,616      | 5.33  |   |
|   | \$3,166,546                      | \$139,539   | \$(325)           | \$3,305,760 | 4.63  | % |

During the period ending March 31, 2012, \$3,500,000 of available-for-sale securities were sold, resulting in a gain of \$0. \$131,361,000 of available-for-sale securities were sold during the period ending March 31, 2011, resulting in a gain of \$8,147,000.

Substantially all mortgage-backed securities have contractual due dates that exceed 10 years.

The following table shows the unrealized gross losses and fair value of securities at March 31, 2012, by length of time that individual securities in each category have been in a continuous loss position. Management believes that the declines in fair value of these investments are not an other than temporary impairment.

|                     | Less than 12 months     |             | 12 months or more       |            | Total                   |             |
|---------------------|-------------------------|-------------|-------------------------|------------|-------------------------|-------------|
|                     | Unrealized Gross Losses | Fair Value  | Unrealized Gross Losses | Fair Value | Unrealized Gross Losses | Fair Value  |
| Corporate bonds due | \$(2,648)               | ) \$257,353 | \$—                     | \$—        | \$(2,648)               | ) \$257,353 |

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|                                  |        |   |           |        |   |          |        |   |           |
|----------------------------------|--------|---|-----------|--------|---|----------|--------|---|-----------|
| Agency pass-through certificates | (2,653 | ) | 396,343   | (129   | ) | 41,945   | (2,782 | ) | 438,288   |
|                                  | (5,301 | ) | \$653,696 | \$(129 | ) | \$41,945 | (5,430 | ) | \$695,641 |

NOTE H – Covered Assets

Covered assets represent loans and real estate held for sale acquired from the FDIC that are subject to loss sharing agreements

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and were \$357,443,000 as of March 31, 2012, versus \$438,566,000 as of September 30, 2011.

Changes in the carrying amount and accretible yield for acquired impaired and non-impaired loans were as follows:

| March 31, 2012                                   | Acquired Impaired |                          | Acquired Non-impaired |                          |
|--|-------------------|--------------------------|-----------------------|--------------------------|
|  | Accretible Yield  | Carrying Amount of Loans | Accretible Yield      | Carrying Amount of Loans |
|  | (In thousands)    |                          |                       |                          |
| Balance at beginning of period                   | \$37,072          | \$116,061                | \$30,370              | \$269,888                |
| Accretion  | (10,404           | ) 10,404                 | (3,965                | ) 3,965                  |
| Transfers to REO                                 | —                 | (11,775                  | ) —                   | —                        |
| Payments received, net                           | —                 | (29,141                  | ) —                   | (37,768                  |
| Balance at end of period                         | \$26,668          | \$85,549                 | \$26,405              | \$236,085                |
|  |                   |                          |                       | )                        |
| September 30, 2011                               | Acquired Impaired |                          | Acquired Non-impaired |                          |
|  | Accretible Yield  | Carrying Amount of Loans | Accretible Yield      | Carrying Amount of Loans |
|  | (In thousands)    |                          |                       |                          |
| Balance at beginning of period                   | \$27,019          | \$190,530                | \$39,813              | \$343,944                |
| Reclassification from nonaccretable balance, net | 24,025            | —                        | —                     | —                        |
| Accretion  | (13,972           | ) 13,972                 | (9,443                | ) 9,443                  |
| Transfers to REO                                 | —                 | (54,638                  | ) —                   | —                        |
| Payments received, net                           | —                 | (33,803                  | ) —                   | (83,499                  |
| Balance at end of period                         | \$37,072          | \$116,061                | \$30,370              | \$269,888                |
|  |                   |                          |                       | )                        |

At March 31, 2012, none of the acquired impaired or non-impaired loans were classified as non-performing assets. Therefore, interest income, through accretion of the difference between the carrying amount of the loans and the expected cash flows, was recognized on all acquired loans. The allowance for credit losses related to the acquired loans resulted from decreased expectations of future cash flows due to increased credit losses for certain acquired loan pools.

The outstanding principal balance of acquired loans was \$422,647,000 and \$495,358,000 as of March 31, 2012 and September 30, 2011, respectively. The discount balance related to the acquired loans was \$97,247,000 and \$109,409,000 as of March 31, 2012 and September 30, 2011, respectively.

The following table shows the year to date activity for the FDIC indemnification asset:

|                                | March 31, 2012 | September 30, 2011 |
|--------------------------------|----------------|--------------------|
|                                | (In thousands) |                    |
| Balance at beginning of period | \$101,634      | \$131,128          |
| Additions                      | 2,052          | 10,470             |
| Payments made (received)       | 4,068          | (32,828            |
| Amortization                   | (7,869         | ) (10,239          |
|                                |                | )                  |

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|                          |           |           |
|--------------------------|-----------|-----------|
| Accretion                | 990       | 3,103     |
| Balance at end of period | \$100,875 | \$101,634 |

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The following tables provide information on covered loans based on credit quality indicators (defined in Note A) as of March 31, 2012 and September 30, 2011:

Credit Risk Profile by Internally Assigned Grade:

| March 31, 2012                        | Internally Assigned Grade |                 |             |          |      | Total<br>Net Loans           |
|---------------------------------------|---------------------------|-----------------|-------------|----------|------|------------------------------|
|                                       | Pass                      | Special mention | Substandard | Doubtful | Loss |                              |
|                                       | (In thousands)            |                 |             |          |      |                              |
| Purchased non credit-impaired loans:  |                           |                 |             |          |      |                              |
| Single-family residential             | \$37,588                  | \$—             | \$3,196     | \$—      | \$—  | \$40,784                     |
| Construction - speculative            | 734                       | —               | —           | —        | —    | 734                          |
| Construction - custom                 | —                         | —               | —           | —        | —    | —                            |
| Land - acquisition & development      | 7,632                     | 5,398           | 1,031       | —        | —    | 14,061                       |
| Land - consumer lot loans             | 507                       | —               | —           | —        | —    | 507                          |
| Multi-family                          | 29,828                    | —               | 2,760       | —        | —    | 32,588                       |
| Commercial real estate                | 99,296                    | 1,115           | 28,787      | —        | —    | 129,198                      |
| Commercial & industrial               | 7,462                     | 1,156           | 6,923       | —        | —    | 15,541                       |
| HELOC                                 | 19,705                    | —               | —           | —        | —    | 19,705                       |
| Consumer                              | 1,019                     | —               | —           | —        | —    | 1,019                        |
|                                       | 203,771                   | 7,669           | 42,697      | —        | —    | 254,137                      |
| Total grade as a % of total net loans | 80.2                      | % 3.0           | % 16.8      | % —      | % —  | %                            |
| Purchased credit-impaired loans:      |                           |                 |             |          |      |                              |
| Pool 1 - Construction and land A&D    | 10,415                    | 5,872           | 42,297      | —        | —    | 58,584                       |
| Pool 2 - Single-family residential    | 2,038                     | —               | 4,044       | —        | —    | 6,082                        |
| Pool 3 - Multi-family                 | —                         | 3,043           | —           | —        | —    | 3,043                        |
| Pool 4 - HELOC & other consumer       | 1,997                     | —               | 4,574       | —        | —    | 6,571                        |
| Pool 5 - Commercial real estate       | 411                       | 30,259          | 41,912      | —        | —    | 72,582                       |
| Pool 6 - Commercial & industrial      | 4,983                     | 1,556           | 15,109      | —        | —    | 21,648                       |
|                                       | \$19,844                  | \$40,730        | \$107,936   | \$—      | \$—  | 168,510                      |
|                                       |                           |                 |             |          |      | Total covered loans 422,647  |
|                                       |                           |                 |             |          |      | Discount (97,247 )           |
|                                       |                           |                 |             |          |      | Allowance (3,766 )           |
|                                       |                           |                 |             |          |      | Covered loans, net \$321,634 |

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| September 30, 2011                    | Internally Assigned Grade |                 |             |          |      | Total<br>Net Loans           |
|---------------------------------------|---------------------------|-----------------|-------------|----------|------|------------------------------|
|                                       | Pass                      | Special mention | Substandard | Doubtful | Loss |                              |
|                                       | (In thousands)            |                 |             |          |      |                              |
| Purchased non credit-impaired loans:  |                           |                 |             |          |      |                              |
| Single-family residential             | \$45,619                  | \$—             | \$595       | \$—      | \$—  | \$46,214                     |
| Construction - speculative            | 1,315                     | —               | —           | —        | —    | 1,315                        |
| Construction - custom                 | —                         | —               | —           | —        | —    | —                            |
| Land - acquisition & development      | 8,383                     | 6,315           | 360         | —        | —    | 15,058                       |
| Land - consumer lot loans             | 543                       | —               | 111         | —        | —    | 654                          |
| Multi-family                          | 32,448                    | —               | 2,458       | —        | —    | 34,906                       |
| Commercial real estate                | 118,124                   | 1,361           | 28,979      | —        | —    | 148,464                      |
| Commercial & industrial               | 13,717                    | 4,481           | 4,239       | 444      | —    | 22,881                       |
| HELOC                                 | 21,730                    | —               | —           | —        | —    | 21,730                       |
| Consumer                              | 1,199                     | —               | —           | —        | —    | 1,199                        |
|                                       | 243,078                   | 12,157          | 36,742      | 444      | —    | 292,421                      |
| Total grade as a % of total net loans | 83.1                      | % 4.2           | % 12.6      | % 0.2    | % —  | %                            |
| Purchased credit-impaired loans:      |                           |                 |             |          |      |                              |
| Pool 1 - Construction and land A&D    | 9,982                     | 2,980           | 54,682      | —        | —    | 67,644                       |
| Pool 2 - Single-family residential    | 3,667                     | —               | 8,263       | —        | —    | 11,930                       |
| Pool 3 - Multi-family                 | —                         | —               | 3,324       | —        | —    | 3,324                        |
| Pool 4 - HELOC & other consumer       | 3,544                     | —               | 5,411       | —        | —    | 8,955                        |
| Pool 5 - Commercial real estate       | 418                       | 30,579          | 48,069      | —        | —    | 79,066                       |
| Pool 6 - Commercial & industrial      | 2,859                     | 2,725           | 25,662      | 772      | —    | 32,018                       |
|                                       | \$20,470                  | \$36,284        | \$145,411   | \$772    | \$—  | 202,937                      |
|                                       |                           |                 |             |          |      | Total covered loans 495,358  |
|                                       |                           |                 |             |          |      | Discount (109,409 )          |
|                                       |                           |                 |             |          |      | Allowance (3,766 )           |
|                                       |                           |                 |             |          |      | Covered loans, net \$382,183 |



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The following tables provide an analysis of the age of purchased non credit-impaired loans in past due status for the periods ended March 31, 2012 and September 30, 2011:

| March 31, 2012<br>Type of Loans  | Amount of Loans<br>Net of LIP & Chg.-Off | Days Delinquent Based on \$ Amount of Loans |         |       |         |          | % based<br>on \$ |   |
|----------------------------------|--|---|---------|-------|---------|----------|------------------|---|
|                                  |  | Current                                     | 30      | 60    | 90      | Total    |                  |   |
| Single-Family Residential        | \$ 40,784                                | \$38,794                                    | \$—     | \$—   | \$1,990 | \$1,990  | 4.88             | % |
| Construction - Speculative       | 734                                      | 734   | —       | —     | —       | —        | NM               |   |
| Construction - Custom            | —  | —   | —       | —     | —       | —        | NM               |   |
| Land - Acquisition & Development | 14,061                                   | 13,077                                      | —       | —     | 984     | 984      | 7.00             |   |
| Land - Consumer Lot Loans        | 507                                      | 276   | 133     | —     | 98      | 231      | 45.56            |   |
| Multi-Family                     | 32,588                                   | 31,080                                      | —       | —     | 1,508   | 1,508    | 4.63             |   |
| Commercial Real Estate           | 129,198                                  | 124,777                                     | 1,742   | 79    | 2,600   | 4,421    | 3.42             |   |
| Commercial & Industrial          | 15,541                                   | 15,016                                      | —       | 434   | 91      | 525      | 3.38             |   |
| HELOC                            | 19,705                                   | 18,456                                      | 906     | 5     | 338     | 1,249    | 6.34             |   |
| Consumer                         | 1,019                                    | 1,018                                       | 1       | —     | —       | 1        | 0.10             |   |
|                                  | \$ 254,137                               | \$243,228                                   | \$2,782 | \$518 | \$7,609 | \$10,909 | 4.29             | % |

| September 30, 2011<br>Type of Loans | Amount of Loans<br>Net of LIP & Chg.-Off | Days Delinquent Based on \$ Amount of Loans |         |         |          |          | % based<br>on \$ |   |
|-------------------------------------|--|---|---------|---------|----------|----------|------------------|---|
|                                     |  | Current                                     | 30      | 60      | 90       | Total    |                  |   |
| Single-Family Residential           | \$ 46,214                                | \$43,445                                    | \$1,034 | \$30    | \$1,705  | \$2,769  | 5.99             | % |
| Construction - Speculative          | 1,315                                    | 1,315                                       | —       | —       | —        | —        | NM               |   |
| Construction - Custom               | —  | —   | —       | —       | —        | —        | NM               |   |
| Land - Acquisition & Development    | 15,058                                   | 13,344                                      | 487     | —       | 1,227    | 1,714    | 11.38            |   |
| Land - Consumer Lot Loans           | 654                                      | 527   | 16      | —       | 111      | 127      | 19.42            |   |
| Multi-Family                        | 34,906                                   | 33,398                                      | —       | —       | 1,508    | 1,508    | 4.32             |   |
| Commercial Real Estate              | 148,464                                  | 142,060                                     | 1,527   | —       | 4,877    | 6,404    | 4.31             |   |
| Commercial & Industrial             | 22,881                                   | 18,049                                      | 3,606   | 703     | 523      | 4,832    | 21.12            |   |
| HELOC                               | 21,730                                   | 20,339                                      | 731     | 391     | 269      | 1,391    | 6.40             |   |
| Consumer                            | 1,199                                    | 1,123                                       | 31      | 8       | 37       | 76       | 6.34             |   |
|                                     | \$ 292,421                               | \$273,600                                   | \$7,432 | \$1,132 | \$10,257 | \$18,821 | 6.44             | % |

NM - not meaningful

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**FORWARD LOOKING STATEMENTS**

In addition to historical information, this Quarterly Report on Form 10-Q includes certain “forward-looking statements,” as defined in the Securities Act of 1933 and the Securities Exchange Act of 1934, based on current management expectations. Actual results could differ materially from those management expectations. Such forward-looking statements include statements regarding the Company’s intentions, beliefs or current expectations as well as the assumptions on which such statements are based. Stockholders and potential stockholders are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those contemplated by such forward-looking statements. Factors that could cause future results to vary from current management expectations include, but are not limited to: general economic conditions; legislative and regulatory changes, including without limitation the potential effect of the Dodd-Frank Wall Street Reform and Consumer Protection Act and regulations to be promulgated thereunder; monetary fiscal policies of the federal government; changes in tax policies; rates and regulations of federal, state and local tax authorities; changes in interest rates; deposit flows; cost of funds; demand for loan products; demand for financial services; competition; changes in the quality or composition of the Company’s loan and investment portfolios; changes in accounting principles; policies or guidelines and other economic, competitive, governmental and technological factors affecting the Company’s operations, markets, products, services and fees, including without limitation the Bank’s ability to comply in a timely and satisfactory manner with the requirements of the memorandum of understanding entered into with the Office of Thrift Supervision. The Company undertakes no obligation to update or revise any forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time.

**GENERAL**

Washington Federal, Inc. (“Company”) is a savings and loan holding company. The Company’s primary operating subsidiary is Washington Federal.

**INTEREST RATE RISK**

The Company accepts a higher level of interest rate volatility as a result of its significant holdings of fixed-rate single-family home loans that are longer in term than the characteristics of its primary liabilities of customer accounts and borrowings. As a result, assets do not respond as quickly to changes in interest rates as liabilities and net interest income typically declines when interest rates rise and expands when interest rates fall as compared to a portfolio of matched maturities of assets and liabilities.

At March 31, 2012, the Company had approximately \$1.95 billion more liabilities subject to repricing in the next year than assets, which amounted to a negative one-year maturity gap of 14.5% of total assets. This was a decrease from the 16.5% negative gap as of September 30, 2011.

The potential impact of rising interest rates on net income for one year has also been estimated using a model that is based on the granular level of detail for loans and deposits. In the event of an immediate and parallel increase of 200 basis points in interest rates, we would expect net interest income to decrease by 3.3%. In the event of a gradual increase from current rates by 200 basis points over a twelve-month period, we would expect a decrease in net interest income of .5%.

This analysis assumes zero balance sheet growth and constant percentage composition of assets and liabilities. It also assumes that loan and deposit prices respond in full to the increase in market rates. Actual results will differ from the assumptions used in this model, as Management monitors and adjusts loan and deposit pricing and the size and composition of the balance sheet to respond to changing interest rates.

The net portfolio value (“NPV”) is the difference between the present value of interest-bearing assets and the present value of expected cash flows from interest-earning liabilities and off-balance-sheet contracts. The sensitivity of the NPV to changes in interest rates is another measure of interest rate risk. This approach provides a longer term view of

interest rate risk as it incorporates all future expected cash flows. In the event of an immediate and parallel increase of 200 basis points in interest rates, the NPV is estimated to decline by \$485 million and the NPV to total assets ratio to decline to 13.04%. As of September 30, 2011 the estimated decrease in NPV in the event of a 200 basis point increase in rates was estimated to decline by \$619 million and the NPV to total assets ratio to decline to 11.04%.

The interest rate spread decreased to 3.01% at March 31, 2012 from 3.13% at September 30, 2011. The spread decreased due to a decline in the average rate on earning assets. As of March 31, 2012, the weighted average rate on earning assets decreased by 25 basis points compared to September 30, 2011, while the weighted average rates on customer deposit accounts and borrowings

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decreased by 13 basis points over the same period.

As of March 31, 2012, the Company had increased total assets by \$123,359,000 from \$13,440,749,000 at September 30, 2011. For the quarter ended March 31, 2012, compared to September 30, 2011, loans (both non-covered and covered) decreased \$320,406,000, or 3.9%. To help offset the reduced income from loans, investment securities increased \$424,144,000, or 12.3%. Cash and cash equivalents of \$890,347,000 and stockholders’ equity of \$1,908,057,000 provides management with flexibility in managing interest rate risk going forward.

## LIQUIDITY AND CAPITAL RESOURCES

The Company’s net worth at March 31, 2012 was \$1,908,057,000, or 14.07%, of total assets. This was an increase of \$1,524,000 from September 30, 2011 when net worth was \$1,906,533,000, or 14.18%, of total assets. The Company’s net worth was impacted in the six months ended March 31, 2012 by net income of \$67,489,000, the payment of \$17,078,000 in cash dividends, treasury stock purchases that totaled \$30,307,000, as well as a decrease in other comprehensive income of \$20,606,000.

Management believes this strong net worth position will help the Company manage its interest rate risk and provide the capital support needed for controlled growth in a regulated environment. To be categorized as well capitalized, Washington Federal must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following table.

|  | Actual                    |       | Capital Adequacy Guidelines |       | Categorized as Well Capitalized Under Prompt Corrective Action Provisions |       |         |       |
|--|---------------------------|-------|-----------------------------|-------|---|-------|---------|-------|
|  | Capital<br>(In thousands) | Ratio | Capital                     | Ratio | Capital   | Ratio | Capital | Ratio |
| March 31, 2012                           |                           |       |                             |       |   |       |         |       |
| Total capital to risk-weighted assets    | \$ 1,638,750              | 25.59 | % \$ 512,353                | 8.00  | % \$ 640,442  | 10.00 | %       |       |
| Tier I capital to risk-weighted assets   | 1,557,847                 | 24.32 | % N/A                       | N/A   | 384,265   | 6.00  | %       |       |
| Core capital to adjusted tangible assets | 1,557,847                 | 11.70 | % N/A                       | N/A   | 665,492   | 5.00  | %       |       |
| Core capital to total assets             | 1,557,847                 | 11.70 | % 532,393                   | 4.00  | % N/A   | N/A   |         |       |
| Tangible capital to tangible assets      | 1,557,847                 | 11.70 | % 532,393                   | 4.00  | % N/A   | N/A   |         |       |
| September 30, 2011                       |                           |       |                             |       |   |       |         |       |
| Total capital to risk-weighted assets    | 1,624,817                 | 24.68 | % 526,765                   | 8.00  | % 658,456   | 10.00 | %       |       |
| Tier I capital to risk-weighted assets   | 1,543,438                 | 23.44 | % N/A                       | N/A   | 395,074   | 6.00  | %       |       |
| Core capital to adjusted tangible assets | 1,543,438                 | 11.82 | % N/A                       | N/A   | 652,672   | 5.00  | %       |       |
| Core capital to total assets             | 1,543,438                 | 11.82 | % 391,603                   | 3.00  | % N/A   | N/A   |         |       |
| Tangible capital to tangible assets      | 1,543,438                 | 11.82 | % 195,802                   | 1.50  | % N/A   | N/A   |         |       |

## CHANGES IN FINANCIAL CONDITION

Available-for-sale and held-to-maturity securities: Available-for-sale securities increased \$432,481,000, or 13.3%, during the six months ended March 31, 2012, which included the purchase of \$1,241,126,000 of available-for-sale securities. There were \$3,500,000 of available-for-sale securities sold during the six months ended March 31, 2012, resulting in no gain or loss. During the same period, there were no purchases or sales of held-to-maturity securities. As of March 31, 2012, the Company had net unrealized gains on available-for-sale securities of \$65,183,000, net of tax,

which were recorded as part of stockholders' equity. The Company increased its available-for-sale investment portfolio to partially replace some of the lost interest income on maturing and prepaying loans and mortgage-backed securities. Loans receivable: During the six months ended March 31, 2012, the balance of loans receivable decreased 3.3% to \$7,676,017,000 compared to \$7,935,877,000 at September 30, 2011. This decrease is consistent with management's strategy to reduce the



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Company’s exposure to land and construction loans and not aggressively compete for 30 year fixed-rate mortgages at current market rates. Additionally, during the year to date period, \$73,466,000 of loans were transferred to REO. If the current low rates on 30 year fixed-rate mortgages persist, management will consider continuing to shrink the Company's loan portfolio. The following table shows the loan portfolio by category for the last three quarters.

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| Loan Portfolio by Category *         | September 30, 2011 |      | December 31, 2011 |      | March 31, 2012 |      |   |
|--------------------------------------|--------------------|------|-------------------|------|----------------|------|---|
|                                      | (In thousands)     |      |                   |      |                |      |   |
| Non-Acquired loans                   |                    |      |                   |      |                |      |   |
| Single-family residential            | \$6,218,878        | 74.9 | % \$6,079,712     | 74.0 | % \$5,971,540  | 74.4 | % |
| Construction - speculative           | 140,459            | 1.7  | 129,766           | 1.6  | 128,719        | 1.6  |   |
| Construction - custom                | 279,851            | 3.4  | 271,227           | 3.3  | 235,566        | 2.9  |   |
| Land - acquisition & development     | 200,692            | 2.4  | 171,678           | 2.1  | 151,967        | 1.9  |   |
| Land - consumer lot loans            | 163,146            | 2.0  | 154,874           | 1.9  | 149,967        | 1.9  |   |
| Multi-family                         | 700,673            | 8.4  | 687,367           | 8.4  | 686,467        | 8.5  |   |
| Commercial real estate               | 303,442            | 3.7  | 308,529           | 3.8  | 293,234        | 3.7  |   |
| Commercial & industrial              | 109,332            | 1.3  | 85,463            | 1.0  | 94,919         | 1.2  |   |
| HELOC                                | 115,092            | 1.4  | 113,781           | 1.4  | 113,368        | 1.4  |   |
| Consumer                             | 67,509             | 0.8  | 63,106            | 0.8  | 71,081         | 0.9  |   |
| Total non-acquired loans             | 8,299,074          | 100  | 8,065,503         | 98.3 | 7,896,828      | 98.4 |   |
| Credit-impaired acquired loans       |                    |      |                   |      |                |      |   |
| Single-family residential            | —                  | —    | 2,778             | —    | 2,093          | —    |   |
| Construction - speculative           | —                  | —    | 354               | —    | 139            | —    |   |
| Land - acquisition & development     | —                  | —    | 4,287             | 0.1  | 4,490          | 0.1  |   |
| Multi-family                         | —                  | —    | 1,782             | —    | 1,229          | —    |   |
| Commercial real estate               | —                  | —    | 106,345           | 1.3  | 101,254        | 1.2  |   |
| Commercial & industrial              | —                  | —    | 8,849             | 0.1  | 7,765          | 0.1  |   |
| HELOC                                | —                  | —    | 18,308            | 0.2  | 17,215         | 0.2  |   |
| Consumer                             | —                  | —    | 137               | —    | 125            | —    |   |
| Total credit-impaired acquired loans | —                  | —    | 142,840           | 1.7  | 134,310        | 1.6  |   |
| Total loans                          |                    |      |                   |      |                |      |   |
| Single-family residential            | 6,218,878          | 74.7 | 6,082,490         | 74.0 | 5,973,633      | 74.4 |   |
| Construction - speculative           | 140,459            | 1.9  | 130,120           | 1.6  | 128,858        | 1.6  |   |
| Construction - custom                | 279,851            | 2.9  | 271,227           | 3.3  | 235,566        | 2.9  |   |
| Land - acquisition & development     | 200,692            | 3.5  | 175,965           | 2.2  | 156,457        | 2.0  |   |
| Land - consumer lot loans            | 163,146            | 2.1  | 154,874           | 1.9  | 149,967        | 1.9  |   |
| Multi-family                         | 700,673            | 7.9  | 689,149           | 8.4  | 687,696        | 8.5  |   |
| Commercial real estate               | 303,442            | 3.6  | 414,874           | 5.1  | 394,488        | 4.9  |   |
| Commercial & industrial              | 109,332            | 1.0  | 94,312            | 1.1  | 102,684        | 1.3  |   |
| HELOC                                | 115,092            | 1.3  | 132,089           | 1.6  | 130,583        | 1.6  |   |
| Consumer                             | 67,509             | 1.1  | 63,243            | 0.8  | 71,206         | 0.9  |   |
| Total loans                          | 8,299,074          | 100  | % 8,208,343       | 100  | % 8,031,138    | 100  | % |
| Less:                                |                    |      |                   |      |                |      |   |
| Allowance for probable losses        | 157,160            |      | 154,540           |      | 143,819        |      |   |
| Loans in process                     | 170,229            |      | 159,437           |      | 133,379        |      |   |
| Discount on acquired loans           | —                  |      | 48,929            |      | 43,687         |      |   |
| Deferred net origination fees        | 35,808             |      | 35,362            |      | 34,236         |      |   |

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|             |             |             |
|-------------|-------------|-------------|
| 363,197     | 398,268     | 355,121     |
| \$7,935,877 | \$7,810,075 | \$7,676,017 |

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\* Excludes covered loans

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Covered loans: As of March 31, 2012, covered loans had decreased 15.8%, or \$60,549,000, to \$321,634,000, compared to September 30, 2011, due to continued paydowns and transfers of the properties into covered real estate owned.

Non-performing assets: Non-performing assets, which excludes covered assets acquired in FDIC-assisted transactions, decreased during the quarter ended March 31, 2012 to \$286,248,000 from \$370,294,000 at September 30, 2011, a 22.7% decrease. The continued elevated level of NPAs is a result of the significant decline in housing values in the western United States and the national recession over the last three years. Non-performing assets as a percentage of total assets was 2.11% at March 31, 2012 compared to 2.76% at September 30, 2011. This level of NPAs remains significantly higher than the 0.91% average in the Company’s 28+ year history as a public company. The Company anticipates NPAs will continue to be elevated in the future until the residential real estate market stabilizes and values recover.

The following table sets forth information regarding restructured and non-accrual loans and REO held by the Company at the dates indicated.

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|   | March 31,<br>2012<br>(In thousands) |      | September 30,<br>2011 |      |   |
|---|-------------------------------------|------|-----------------------|------|---|
| Restructured loans:   |                                     |      |                       |      |   |
| Single-family residential   | \$352,622                           | 82.6 | % \$309,372           | 82.0 | % |
| Construction - speculative  | 20,485                              | 4.8  | 15,481                | 4.1  |   |
| Construction - custom   | —                                   | —    | —                     | —    |   |
| Land - acquisition & development  | 20,443                              | 4.8  | 18,033                | 4.8  |   |
| Land - consumer lot loans   | 14,389                              | 3.4  | 13,124                | 3.5  |   |
| Multi - family  | 16,955                              | 4.0  | 19,046                | 5.0  |   |
| Commercial real estate  | 1,714                               | 0.4  | 1,435                 | 0.4  |   |
| Commercial & industrial   | 4                                   | —    | 828                   | 0.2  |   |
| HELOC   | 177                                 | —    | 177                   | —    |   |
| Consumer  | —                                   | —    | —                     | —    |   |
| Total restructured loans (1)  | 426,789                             | 100  | % 377,496             | 100  | % |
| Non-accrual loans:  |                                     |      |                       |      |   |
| Single-family residential   | 116,284                             | 70.0 | % 126,624             | 60.3 | % |
| Construction - speculative  | 8,190                               | 4.9  | 15,383                | 7.3  |   |
| Construction - custom   | 539                                 | 0.3  | 635                   | 0.3  |   |
| Land - acquisition & development  | 25,036                              | 15.1 | 37,339                | 17.7 |   |
| Land - consumer lot loans   | 5,641                               | 3.4  | 8,843                 | 4.2  |   |
| Multi-family  | 4,530                               | 2.7  | 7,664                 | 3.6  |   |
| Commercial real estate  | 4,997                               | 3.0  | 11,380                | 5.4  |   |
| Commercial & industrial   | 1                                   | —    | 1,679                 | 0.8  |   |
| HELOC   | 591                                 | 0.4  | 481                   | 0.2  |   |
| Consumer  | 344                                 | 0.2  | 437                   | 0.2  |   |
| Total non-accrual loans (2)   | 166,153                             | 100  | % 210,465             | 100  | % |
| Total REO (3)   | 99,826                              |      | 129,175               |      |   |
| Total REHI (3)  | 20,269                              |      | 30,654                |      |   |
| Total non-performing assets   | \$286,248                           |      | \$370,294             |      |   |
| Total non-performing assets and performing restructured loans as a percentage of total assets | 4.96                                | %    | 5.14                  | %    |   |
| (1) Restructured loans were as follows:   |                                     |      |                       |      |   |
| Performing  | \$387,010                           | 90.7 | % \$320,018           | 84.8 | % |
| Non-accrual *   | 39,779                              | 9.3  | 57,478                | 15.2 |   |
|   | \$426,789                           | 100  | % \$377,496           | 100  | % |

\*Included in "Total non-accrual loans" above

The Company recognized interest income on nonaccrual loans of approximately \$1,430,000 in the six months (2) ended March 31, 2012. Had these loans performed according to their original contract terms, the Company would have recognized interest income of approximately \$5,297,000 for the six months ended March 31, 2012.

In addition to the nonaccrual loans reflected in the above table, at March 31, 2012, the Company had \$188,475,000 of loans that were less than 90 days delinquent but which it had classified as substandard for one or more reasons. If

these loans were deemed non-performing, the Company's ratio of total NPAs and performing restructured loans as a percent of total assets would have increased to 6.65% at March 31, 2012.

Total REO and REHI (included in real estate held for sale on the Statement of Financial Condition) includes real (3)estate held for sale acquired in settlement of loans or acquired from purchased institutions in settlement of loans. Excludes covered REO.

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Restructured single-family residential loans are reserved for under the Company’s general reserve methodology. If any individual loan is significant in balance, the Company may establish a specific reserve as warranted.

Most restructured loans are accruing and performing loans where the borrower has proactively approached the Company about modifications due to temporary financial difficulties. Each request is individually evaluated for merit and likelihood of success. Single-family residential loans comprised 82.6% of restructured loans as of March 31, 2012. The concession for these loans is typically a payment reduction through a rate reduction of from 100 to 200 bps for a specific term, usually six to twelve months. Interest-only payments may also be approved during the modification period.

For commercial loans, six consecutive payments on newly restructured loan terms are required prior to returning the loan to accrual status. In some instances after the required six consecutive payments are made, a management assessment will conclude that collection of the entire principal balance is still in doubt. In those instances, the loan will remain on non-accrual. Homogeneous loans may or may not be on accrual status at the time of restructuring, but all are placed on accrual status upon the restructuring of the loan. Homogeneous loans are restructured only if the borrower can demonstrate the ability to meet the restructured payment terms; otherwise, collection is pursued and the loan remains on non-accrual status until liquidated. If the homogeneous restructured loan does not perform it will be placed in non-accrual status when it is 90 days delinquent.

A loan that defaults and is subsequently modified would impact the Company’s delinquency trend, which is part of the qualitative risk factors component of the general reserve calculation. Any modified loan that re-defaults and is charged-off would impact the historical loss factors component of our general reserve calculation.

Allocation of the allowance for loan losses: The following table shows the allocation of the Company’s allowance for loan losses at the dates indicated.

|                                  | March 31, 2012              |                             |                       | September 30, 2011          |                             |                       |
|----------------------------------|-----------------------------|-----------------------------|-----------------------|-----------------------------|-----------------------------|-----------------------|
|                                  | Amount<br>(In<br>thousands) | Loans to<br>Total Loans (1) | Coverage<br>Ratio (2) | Amount<br>(In<br>thousands) | Loans to<br>Total Loans (1) | Coverage<br>Ratio (2) |
| Single-family residential        | \$83,875                    | 75.7                        | % 1.4                 | % \$83,307                  | 74.9                        | % 1.3                 |
| Construction - speculative       | 15,943                      | 1.6                         | 12.4                  | 13,828                      | 1.7                         | 9.8                   |
| Construction - custom            | 384                         | 3.0                         | 0.2                   | 623                         | 3.4                         | 0.2                   |
| Land - acquisition & development | 19,929                      | 1.9                         | 13.1                  | 32,719                      | 2.4                         | 16.3                  |
| Land - consumer lot loans        | 7,712                       | 1.9                         | 5.1                   | 5,520                       | 2.0                         | 40.0                  |
| Multi-family                     | 4,837                       | 8.7                         | 0.7                   | 7,623                       | 8.4                         | 1.1                   |
| Commercial real estate           | 2,869                       | 3.7                         | 1.0                   | 4,331                       | 3.7                         | 1.4                   |
| Commercial & industrial          | 4,427                       | 1.2                         | 4.7                   | 5,099                       | 1.3                         | 4.7                   |
| HELOC                            | 969                         | 1.4                         | 0.9                   | 1,139                       | 1.4                         | 1.0                   |
| Consumer                         | 2,874                       | 0.9                         | 4.0                   | 2,971                       | 0.8                         | 4.4                   |
|                                  | \$143,819                   | 100                         | %                     | \$157,160                   | 100                         | %                     |

(1) Represents the total amount of the loan category as a % of total gross non-acquired and non-covered loans outstanding.

(2) Represents the allocated allowance of the loan category as a % of total gross non-acquired and non-covered loans outstanding for the same loan category.

Customer accounts: Customer accounts increased \$132,537,000, or 1.53%, to \$8,798,440,000 at March 31, 2012 compared with \$8,665,903,000 at September 30, 2011. The following table shows the composition of the Company's customer accounts as of the dates shown:

Deposits by Type



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|                         | March 31, 2012 |      |           |   | September 30, 2011 |      |        |   |
|-------------------------|----------------|------|-----------|---|--------------------|------|--------|---|
|                         | (In thousands) |      |           |   |                    |      |        |   |
|                         |                |      | Wtd. Avg. |   | Wtd. Avg.          |      |        |   |
|                         |                |      | Rate      |   |                    |      | Rate   |   |
| Checking (non-interest) | \$267,031      | 3.0  | % —       | % | \$235,146          | 2.7  | % —    | % |
| NOW (interest)          | 594,879        | 6.8  | 0.14      | % | 543,907            | 6.3  | 0.13   | % |
| Savings (passbook/stmt) | 291,958        | 3.3  | 0.20      | % | 255,396            | 2.9  | 0.20   | % |
| Money Market            | 1,710,756      | 19.5 | 0.26      | % | 1,627,739          | 18.8 | 0.26   | % |
| CD’s                    | 5,933,816      | 67.4 | 1.36      | % | 6,003,715          | 69.3 | 1.55   | % |
| Total                   | \$8,798,440    | 100  | % 0.98    | % | \$8,665,903        | 100  | % 1.14 | % |

FHLB advances and other borrowings: Total borrowings decreased slightly to \$2,760,041,000 at March 31, 2012, compared with \$2,762,066,000 at September 30, 2011. The Company has a credit line with the FHLB Seattle equal to 50% of total assets, providing a substantial source of liquidity if needed. FHLB advances are collateralized as provided for in the Advances, Pledge and Security Agreement by all FHLB stock owned by the Company, deposits with the FHLB and certain mortgages or deeds of trust securing such properties as provided in the agreements with the FHLB.

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

## RESULTS OF OPERATIONS

Net Income: The quarter ended March 31, 2012, produced net income of \$34,071,000 compared to \$25,824,000 for the same quarter one year ago. For the six months ended March 31, 2012, net income totaled \$67,489,000 compared to \$50,354,000 for the six months ended March 31, 2011. The net income for the quarter and six months ended March 31, 2012 benefited from overall lower credit costs, which included the provision for loan losses and real estate owned expenses. The provision for loan losses amounted to \$18,000,000 and \$29,209,000 for the quarter and six months ended March 31, 2012, as compared to \$30,750,000 and \$56,750,000 for the three and six month period one year ago. See related discussion in “Provision for Loan Losses” section below for reasons for the decrease in the provision for loan losses. In addition, losses recognized on real estate acquired through foreclosure was \$1,582,000 and \$12,151,000 for the quarter and six months ended March 31, 2012 as compared to \$9,645,000 and \$20,198,000 for the three and six month periods one year ago.

Net Interest Income: The largest component of the Company’s earnings is net interest income, which is the difference between the interest and dividends earned on loans and other investments and the interest paid on customer deposits and borrowings. Net interest income is impacted primarily by two factors; first, the volume of earning assets and liabilities and second, the rate earned on those assets or the rate paid on those liabilities.

The following table sets forth certain information explaining changes in interest income and interest expense for the periods indicated compared to the same periods one year ago. For each category of interest-earning asset and interest-bearing liability, information is provided on changes attributable to (1) changes in volume (changes in volume multiplied by old rate) and (2) changes in rate (changes in rate multiplied by old volume). The change in interest income and interest expense attributable to changes in both volume and rate has been allocated proportionately to the change due to volume and the change due to rate.

## Rate / Volume Analysis:

|                                    | Comparison of Quarters Ended<br>3/31/12 and 3/31/11 |          |            | Comparison of Six Months Ended<br>3/31/12 and 3/31/11 |           |            |
|------------------------------------|---|----------|------------|---|-----------|------------|
|                                    | Volume  | Rate     | Total      | Volume  | Rate      | Total      |
|                                    | (In thousands)                                      |          |            |   |           |            |
| Interest income:                   |   |          |            |   |           |            |
| Loans and covered loans            | \$(6,864 )  | \$2,002  | \$(4,862 ) | \$(17,806 )   | \$2,507   | \$(15,299) |
| Mortgaged-backed securities        | 9,249   | (6,730 ) | 2,519      | 17,820  | (12,699 ) | 5,121      |
| Investments (1)                    | (601 )  | (1,014 ) | (1,615 )   | (1,044 )  | (2,400 )  | (3,444 )   |
| All interest-earning assets        | 1,784   | (5,742 ) | (3,958 )   | (1,030 )  | (12,592 ) | (13,622 )  |
| Interest expense:                  |   |          |            |   |           |            |
| Customer accounts                  | (29 )   | (7,405 ) | (7,434 )   | (579 )  | (15,640 ) | (16,219 )  |
| FHLB advances and other borrowings | 1,133   | (704 )   | 429        | 2,106   | (1,536 )  | 570        |
| All interest-bearing liabilities   | 1,104   | (8,109 ) | (7,005 )   | 1,527   | (17,176 ) | (15,649 )  |
| Change in net interest income      | \$680   | \$2,367  | \$3,047    | \$(2,557 )  | \$4,584   | \$2,027    |

(1) Includes interest on cash equivalents and dividends on FHLB stock

Provision for Loan Losses: The Company recorded an \$18,000,000 provision for loan losses during the quarter ended March 31, 2012, while a \$30,750,000 provision was recorded for the same quarter one year ago. Non-performing assets amounted to \$286,248,000, or 2.11% , of total assets at March 31, 2012, compared to \$399,295,000, or 2.98%, of total assets one year ago. Non-accrual loans decreased from \$221,736,000 at March 31, 2011, to \$166,153,000 at March 31, 2012, a 25.1% decrease. The Company had net charge-offs of \$28,721,000 for the quarter ended March 31,

2012, compared with \$26,421,000 of net charge-offs for the same quarter one year ago. The decrease in the provision for loan losses is in response to four primary factors: first, the amount of NPA's improved; second, non-accrual loans as a percentage of net loans decreased from 2.77% at March 31, 2011, to 2.16% at March 31, 2012; third, the percentage of loans 30 days or more delinquent decreased from from 3.37% at March 31, 2011, to 2.95% at March 31, 2012; and finally, the Company's exposure in the land A&D and speculative construction portfolios, the source of the majority of losses during this period of the cycle, has decreased from a combined 4.6% of the gross loan portfolio at March 31, 2011, to 3.5% at March 31, 2012. Management expects the provision to remain at elevated levels until housing

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

PART I – Financial Information

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

values stabilize. Management believes the allowance for loan losses, totaling \$143,819,000, is sufficient to absorb estimated losses inherent in the portfolio.

See Note F for further discussion and analysis of the allowance for loan losses for the quarter ended March 31, 2012.

Other Income: The quarter ended March 31, 2012 produced total other income of \$5,028,000 compared to \$12,511,000 for the same quarter one year ago, a decrease of \$7,483,000. The quarter ended March 31, 2011 included an \$8,147,000 gain on sale of investments compared to no gain during the current quarter ended March 31, 2012.

Other Expense: The quarter ended March 31, 2012, produced total other expense of \$36,812,000 compared to \$33,321,000 for the same quarter one year ago, a 10.5% increase. The increase in total other expense over the same comparable period one year ago was primarily due to the increase of \$2,361,000 in compensation and benefits, which, for the quarter ended March 31, 2012 included the addition of the employees from the Charter Bank acquisition October 2011 and the Western National Bank transaction with the FDIC in December 2011. Also impacted by these acquisitions were the increases in occupancy expense and other expense of \$458,000 and \$1,422,000 respectively, for the quarter ended March 31, 2012 as compared to the prior year. Total other expense for the quarters ended March 31, 2012 and 2011 equaled 1.08% and 0.99%, respectively, of average assets. The number of staff, including part-time employees on a full-time equivalent basis, was 1,248 and 1,226 at March 31, 2012 and 2011, respectively.

Taxes: Income taxes increased to \$19,165,000 for the quarter ended March 31, 2012, as compared to \$14,526,000 for the same period one year ago. The effective tax rate for the quarters ended March 31, 2012 and 2010, was 36.00%.

The Company expects an effective tax rate of 36.00% going forward.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Management believes that there have been no material changes in the Company’s quantitative and qualitative information about market risk since September 30, 2011. For a complete discussion of the Company’s quantitative and qualitative market risk, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in the Company’s 2011 Form 10-K.

(a) Evaluation of Disclosure Controls and Procedures. The Company maintains a set of disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) that are designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Company’s President and Chief Executive Officer along with the Company’s Executive Vice President and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Management has evaluated, with the participation of the Company’s President and Chief Executive Officer, along with the Company’s Executive Vice President and Chief Financial Officer, the effectiveness of the Company’s disclosure controls and procedures as of the end of the period covered by this quarterly report (the "Evaluation Date"). Based on the evaluation, the Company’s President and Chief Executive Officer along with the Company’s Executive Vice President and Chief Financial Officer have concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures are effective.

(b) Changes in Internal Control over Financial Reporting. During the period to which this report relates, there have not been any changes in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or that are reasonably likely to materially affect, such controls.



WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

PART II – Other Information

Item 1. Legal Proceedings

From time to time the Company or its subsidiaries are engaged in legal proceedings in the ordinary course of business, none of which are considered to have a material impact on the Company's financial position or results of operations.

Item 1A. Risk Factors

In addition to the other information contained in this Quarterly Report on Form 10-Q, the following risk factors represent material updates and additions to the risk factors previously disclosed in the Company's Annual Report on Form 10-K. Additional risks not presently known to us, or that we currently deem immaterial, may also adversely affect our business, financial condition or results of operations.

Financial reform legislation has, among other things, eliminated the Office of Thrift Supervision ("OTS"), tightened capital standards, created a new Consumer Financial Protection Bureau and resulted in new laws and regulations that may increase our costs of operations.

On July 21, 2010, the President signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act"). This new law significantly changed the current bank regulatory structure and affected the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. It requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impact of the Act may not be known for many months or years.

One change that was particularly significant to the Company and the Bank was the abolition of the OTS, the Bank's historical federal financial institution regulator. After the OTS was abolished, supervision and regulation of the Company moved to the Board of Governors of the Federal Reserve System ("Federal Reserve") and supervision and regulation of the Bank moved to the Office of the Comptroller of the Currency ("OCC"). Except as described below, however, the laws and regulations applicable to the Company and the Bank will not generally change – the Home Owners Loan Act and the regulations issued under the Act will generally still apply (although these laws and regulations will be interpreted by the Federal Reserve and the OCC, respectively).

In addition, the Company for the first time is subject to consolidated capital requirements and is required to serve as a source of strength to the Bank. The Bank is subject to the same lending limits as national banks. At this time, we do not anticipate that being subject to any of these provisions will have a material effect on the Company or the Bank.

The Act also broadened the base for Federal Deposit Insurance Corporation insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution. This could result in an increase in deposit insurance assessments to be paid by the Bank. The Act also permanently increased the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per depositor, retroactive to January 1, 2008, and non-interest bearing transaction accounts will have unlimited deposit insurance from March 31, 2011 through December 31, 2012. The Federal Reserve also adopted a rule addressing interchange fees applicable to debit card transactions that lowers fee income generated from this source. At this time, we do not anticipate that being subject to any of these provisions will have a material effect on the Company or the Bank.

The Act requires publicly traded companies to give stockholders a non-binding vote on executive compensation and so-called "golden parachute" payments, and authorizes the Securities and Exchange Commission to promulgate rules that would allow stockholders to nominate their own candidates for election as directors using a company's proxy materials. The legislation also directs the federal financial institution regulatory agencies to promulgate rules prohibiting excessive compensation being paid to financial institution executives.

The Act created a new Consumer Financial Protection Bureau to take over responsibility for the principal federal consumer protection laws, such as the Truth in Lending Act, the Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act and the Truth in Saving Act, among others, with broad rule-making, supervisory and examination authority in this area over institutions that have assets of \$10 billion or more, such as the Bank. The Act

also narrowed the scope of federal preemption of state laws related to federally chartered institutions. Many of the provisions of the Act did not become effective until a year or more after its enactment and some provisions require the adoption and implementation of new or revised regulations. In addition, the scope and impact of many of the Act's provisions

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## WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

## PART II – Other Information

will be determined through the rulemaking process. As a result, we cannot predict the ultimate impact of the Act on the Company or the Bank at this time, including the extent to which it could increase costs or limit our ability to pursue business opportunities in an efficient manner, or otherwise adversely affect our business, financial condition and results of operations. Nor can we predict the impact or substance of other future legislation or regulation. However, it is expected that at a minimum they will increase our operating and compliance costs.

The Bank has entered into a memorandum of understanding with the OTS that will entail compliance costs. Failure to comply with the memorandum could result in formal enforcement action or regulatory constraints on the Bank.

As previously disclosed, the Bank entered into a memorandum of understanding (“MOU”) with the OTS on July 28, 2010. The MOU and our compliance with it is being monitored by the OCC since the OTS was abolished in July 2011. The MOU does not affect dividend policy or require additional capital, but a finding by the OCC that the Bank failed to comply with the MOU could result in additional regulatory scrutiny, constraints on the Bank's business, or formal enforcement action. Any of those events could have a material adverse effect on the Bank's future operations, financial condition, growth or other aspects of our business.

The MOU will remain in effect until the OCC, as the successor to the OTS, decides to modify, suspend or terminate it.

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

The following table provides information with respect to purchases made by or on behalf of the Company of the Company's common stock during the three months ended March 31, 2012.

| Period                                | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plan (1) | Maximum Number of Shares That May Yet Be Purchased Under the Plan at the End of the Period |
|---------------------------------------|----------------------------------|------------------------------|---|--|
| January 1, 2012 to January 31, 2012—  |                                  | \$—                          | —   | 7,533,514  |
| February 1, 2012 to February 29, 2012 | 625,200                          | 15.99                        | 625,200   | 6,908,314  |
| March 1, 2012 to March 31, 2012       | —                                | —                            | —   | 6,908,314  |
| Total                                 | 625,200                          | \$15.99                      | 625,200   | 6,908,314  |

The Company's only stock repurchase program was publicly announced by the Board of Directors on February 3, (1) 1995 and has no expiration date. Under this ongoing program, a total of 31,956,264 shares have been authorized for repurchase.

## Item 3. Defaults Upon Senior Securities

Not applicable



Item 5. Other Information

In June 2011, the FASB issued guidance on the presentation of comprehensive income in financial statements. Entities are required to present total comprehensive income either in a single, continuous statement of comprehensive income or in two separate, but consecutive, statements. We adopted this standard as of October 1, 2011 and present net income and other comprehensive income in two separate, but consecutive, statements. The table below reflects the retrospective application of this guidance for each of the three years ended September 30. The retrospective application did not have a material impact on our financial condition or results of operations.

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|  | Fiscal Years Ended September 30, |            |            |
|--|----------------------------------|------------|------------|
|  | 2011                             | 2010       | 2009       |
|  | (In thousands)                   |            |            |
| Net income   | \$ 111,141                       | \$ 118,653 | \$ 48,172  |
| Other comprehensive income net of tax:   |                                  |            |            |
| Net unrealized gains (losses) on available-for-sales securities,<br>net of taxes of \$16,981 for 2011  | 30,852                           | (19,203    | ) 51,273   |
| Reclassification adjustment of net gains from sale<br>of available-for-sale securities included in net income,<br>net of taxes of \$2,892 for 2011 | 5,255                            | 14,454     | 686        |
| Other comprehensive income   | 36,107                           | (4,749     | ) 51,959   |
| Comprehensive income   | \$ 147,248                       | \$ 113,904 | \$ 100,131 |

## Item 6. Exhibits

## (a) Exhibits

31.1 Section 302 Certification by the Chief Executive Officer

31.2 Section 302 Certification by the Chief Financial Officer

32 Section 906 Certification by the Chief Executive Officer and the Chief Financial Officer

101 Financial Statements from the Company's Quarterly Report on Form 10-Q for the fiscal quarter and six months ended March 31, 2012 formatted in XBRL

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

SIGNATURES

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

May 7, 2012

/S/ ROY M. WHITEHEAD  
ROY M. WHITEHEAD  
Chairman, President and Chief Executive Officer

May 7, 2012

/S/ BRENT J. BEARDALL  
BRENT J. BEARDALL  
Executive Vice President and Chief  
Financial Officer