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TIMBERLAND BANCORP INC  
Form 10-Q  
August 08, 2007

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended June 30, 2007

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 0-23333

TIMBERLAND BANCORP, INC.  
(Exact name of registrant as specified in its charter)

Washington 91-1863696  
(State of Incorporation) (IRS Employer Identification No.)

624 Simpson Avenue, Hoquiam, Washington 98550  
(Address of principal executive office) (Zip Code)

(360) 533-4747  
(Registrant's telephone number, including area code)

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. Check one:

Large accelerated filer  Accelerated Filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (in Rule 12b-2 of the Exchange Act).

Yes  No

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

| CLASS                         | SHARES OUTSTANDING AT July 31, 2007 |
|-------------------------------|-------------------------------------|
| Common stock, \$.01 par value | 6,965,360                           |

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## INDEX

|   | Page  |
|---|-------|
|   | ----  |
| PART I. FINANCIAL INFORMATION   |       |
| Item 1. Financial Statements (unaudited)  |       |
| Condensed Consolidated Balance Sheets   | 3     |
| Condensed Consolidated Statements of Income   | 4     |
| Condensed Consolidated Statements of Shareholders' Equity                                     | 5     |
| Condensed Consolidated Statements of Cash Flows   | 6-7   |
| Condensed Consolidated Statements of Comprehensive Income                                     | 8     |
| Notes to Condensed Consolidated Financial Statements  | 9-15  |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations | 15-28 |
| Item 3. Quantitative and Qualitative Disclosures about Market Risk                            | 29    |
| Item 4. Controls and Procedures   | 29    |
| PART II. OTHER INFORMATION  |       |
| Item 1. Legal Proceedings   | 29    |
| Item 1A - Risk Factors  | 29    |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds                           | 30    |
| Item 3. Defaults Upon Senior Securities   | 30    |
| Item 4. Submission of Matters to a Vote of Security Holders                                   | 30    |
| Item 5. Other Information   | 30    |
| Item 6. Exhibits  | 31    |
| SIGNATURES  | 32    |

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### Item 1. Financial Statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 June 30, 2007 and September 30, 2006  
 Dollars in thousands, except share amounts

|  | June 30,<br>2007 | September 30,<br>2006 |
|--|------------------|-----------------------|
|  | -----            |                       |
| Assets   | (Unaudited)      |                       |
| Cash equivalents:  |                  |                       |
| Non-interest bearing   | \$ 11,798        | \$ 14,870             |
| Interest bearing deposits in banks   | 1,188            | 2,519                 |
| Federal funds sold   | 205              | 5,400                 |
|  | -----            |                       |
|  | 13,191           | 22,789                |
|  | -----            |                       |
| Certificates of deposit ("CDs") held for investment                        | - -              | 100                   |
| Investments and mortgage-backed securities: held to maturity               | 72               | 75                    |
| Investments and mortgage-backed securities: available for sale             | 64,911           | 81,408                |
| Federal Home Loan Bank ("FHLB") stock                                      | 5,705            | 5,705                 |
| Loans receivable   | 500,694          | 426,318               |
| Loans held for sale  | 1,165            | 2,449                 |
| Less: Allowance for loan losses  | (4,529)          | (4,122)               |
|  | -----            |                       |
| Net loans receivable   | 497,330          | 424,645               |
|  | -----            |                       |
| Accrued interest receivable  | 3,177            | 2,806                 |
| Premises and equipment   | 16,557           | 16,730                |
| Other real estate owned ("OREO") and other repossessed items               | 68               | 15                    |
| Bank owned life insurance ("BOLI")   | 12,294           | 11,951                |
| Goodwill   | 5,650            | 5,650                 |
| Core deposit intangible  | 1,292            | 1,506                 |
| Mortgage servicing rights  | 1,018            | 932                   |
| Other assets   | 2,881            | 2,775                 |
|  | -----            |                       |
| Total assets   | \$624,146        | \$577,087             |
|  | =====            |                       |
| Liabilities and shareholders' equity                                       |                  |                       |
| Deposits   | \$433,514        | \$431,061             |
| FHLB advances  | 112,463          | 62,761                |
| Other borrowings: repurchase agreements                                    | 775              | 947                   |
| Other liabilities and accrued expenses                                     | 3,402            | 2,953                 |
|  | -----            |                       |
| Total liabilities  | 550,154          | 497,722               |
|  | -----            |                       |
| Commitments and contingencies  | --               | --                    |
| Shareholders' equity   |                  |                       |
| Preferred stock, \$.01 par value; 1,000,000 shares authorized; none issued |                  |                       |
| Common stock, \$.01 par value; 50,000,000 shares authorized;               |                  |                       |
| June 30, 2007 - 7,025,360 shares issued and                                |                  |                       |

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|  |           |           |
|--|-----------|-----------|
| outstanding  |           |           |
| September 30, 2006 - 3,757,676 shares issued                           |           |           |
| and outstanding on a pre-split basis                                   | 70        | 38        |
| Additional paid in capital   | 11,425    | 20,888    |
| Unearned shares - Employee Stock Ownership Plan ("ESOP")               | (3,106)   | (3,305)   |
| Unearned shares - Management Recognition and Development Plan ("MRDP") | (415)     | (188)     |
| Retained earnings  | 66,915    | 62,933    |
| Accumulated other comprehensive loss                                   | (897)     | (1,001)   |
|  | -----     | -----     |
| Total shareholders' equity   | 73,992    | 79,365    |
|  | -----     | -----     |
| Total liabilities and shareholders' equity                             | \$624,146 | \$577,087 |
|  | =====     | =====     |

See notes to unaudited condensed consolidated financial statements

3

TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
For the three and nine months ended June 30, 2007 and 2006  
Dollars in thousands, except per share amounts  
(unaudited)

|   | Three Months<br>Ended June 30, |          | Nine Months<br>Ended June 30, |          |
|---|--------------------------------|----------|-------------------------------|----------|
|   | 2007                           | 2006     | 2007                          | 2006     |
|   | -----                          | -----    | -----                         | -----    |
| Interest and dividend income                        |                                |          |                               |          |
| Loans receivable                                    | \$ 9,981                       | \$ 8,036 | \$28,050                      | \$23,144 |
| Investments and mortgage-backed securities          | 350                            | 529      | 1,185                         | 1,642    |
| Dividends from investments                          | 426                            | 370      | 1,259                         | 1,036    |
| Federal funds sold                                  | 49                             | 121      | 192                           | 292      |
| Interest bearing deposits in banks                  | 8                              | 18       | 61                            | 54       |
|   | -----                          | -----    | -----                         | -----    |
| Total interest and dividend income                  | 10,814                         | 9,074    | 30,747                        | 26,168   |
|   | -----                          | -----    | -----                         | -----    |
| Interest expense                                    |                                |          |                               |          |
| Deposits  | 2,866                          | 2,058    | 8,113                         | 5,554    |
| FHLB advances - short term                          | 651                            | - -      | 1,298                         | 13       |
| FHLB advances - long term                           | 627                            | 718      | 1,875                         | 2,188    |
| Other borrowings                                    | 12                             | 10       | 39                            | 36       |
|   | -----                          | -----    | -----                         | -----    |
| Total interest expense                              | 4,156                          | 2,786    | 11,325                        | 7,791    |
|   | -----                          | -----    | -----                         | -----    |
| Net interest income                                 | 6,658                          | 6,288    | 19,422                        | 18,377   |
| Provision for loan losses                           | 260                            | - -      | 416                           | --       |
|   | -----                          | -----    | -----                         | -----    |
| Net interest income after provision for loan losses | 6,398                          | 6,288    | 19,006                        | 18,377   |
|   | -----                          | -----    | -----                         | -----    |
| Non-interest income                                 |                                |          |                               |          |
| Service charges on deposits                         | 692                            | 769      | 2,061                         | 2,226    |
| Gain on sale of loans, net                          | 79                             | 60       | 250                           | 264      |
| BOLI net earnings                                   | 116                            | 112      | 343                           | 333      |
| Escrow fees   | 22                             | 32       | 77                            | 87       |

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|   |           |           |           |           |
|---|-----------|-----------|-----------|-----------|
| Servicing income on loans sold                | 127       | 80        | 373       | 266       |
| ATM transaction fees                          | 295       | 266       | 830       | 742       |
| Other   | 170       | 209       | 471       | 674       |
|   | -----     |           |           |           |
| Total non-interest income                     | 1,501     | 1,528     | 4,405     | 4,592     |
|   | -----     |           |           |           |
| Non-interest expense                          |           |           |           |           |
| Salaries and employee benefits                | 2,752     | 2,727     | 8,303     | 8,095     |
| Premises and equipment                        | 557       | 583       | 1,827     | 1,814     |
| Advertising                                   | 190       | 185       | 569       | 501       |
| Loss (gain) from other real estate operations | 1         | 5         | (14)      | (79)      |
| ATM expenses                                  | 128       | 105       | 354       | 299       |
| Postage and courier                           | 113       | 123       | 347       | 370       |
| Amortization of core deposit intangible       | 71        | 82        | 214       | 246       |
| State and local taxes                         | 148       | 138       | 420       | 427       |
| Professional fees                             | 175       | 222       | 524       | 611       |
| Other   | 626       | 621       | 2,052     | 1,863     |
|   | -----     |           |           |           |
| Total non-interest expense                    | 4,761     | 4,791     | 14,596    | 14,147    |
|   | -----     |           |           |           |
| Income before federal income taxes            | 3,138     | 3,025     | 8,815     | 8,822     |
| Federal income taxes                          | 1,000     | 964       | 2,806     | 2,809     |
|   | -----     |           |           |           |
| Net income                                    | \$ 2,138  | \$ 2,061  | \$ 6,009  | \$ 6,013  |
|   | =====     |           |           |           |
| Earnings per common share:                    |           |           |           |           |
| Basic   | \$ 0.32   | \$ 0.29   | \$ 0.88   | \$ 0.85   |
| Diluted                                       | \$ 0.31   | \$ 0.28   | \$ 0.85   | \$ 0.82   |
| Weighted average shares outstanding:          |           |           |           |           |
| Basic   | 6,713,777 | 7,141,700 | 6,863,253 | 7,058,116 |
| Diluted                                       | 6,910,165 | 7,382,876 | 7,080,530 | 7,305,004 |
| Dividends paid per share:                     | \$ 0.09   | \$ 0.08   | \$ 0.27   | \$ 0.24   |

See notes to unaudited condensed consolidated financial statements

4

TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
 For the year ended September 30, 2006 and the nine months ended June 30, 2007  
 Dollars in thousands, except per share amounts and common stock shares

|                         | Common<br>Stock Shares<br>Outstanding | Common<br>Stock<br>Amount | Additional<br>Paid-In<br>Capital | Unearned<br>Shares<br>Issued to<br>ESOP | Unearned<br>Shares<br>Issued<br>to MRP | Retained<br>Earnings | Accumu-<br>lated<br>Other<br>Compre-<br>hensive<br>Loss |
|-------------------------|---------------------------------------|---------------------------|----------------------------------|---|--|----------------------|---|
|                         | -----                                 | -----                     | -----                            | -----                                   | -----                                  | -----                | -----   |
| Balance, Sept. 30, 2005 | 7,519,874                             | \$ 38                     | \$22,040                         | (\$3,833)                               | \$ - -                                 | \$57,268             | (\$871)   |

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|   |           |       |          |           |         |          |           |
|---|-----------|-------|----------|-----------|---------|----------|-----------|
| Net income  | -         | -     | -        | -         | -       | 8,157    | -         |
| Issuance of MRDP shares   | 12,000    | -     | 195      | -         | (195)   | -        | -         |
| Repurchase of<br>common stock   | (217,200) | (1)   | (3,700)  | -         | -       | -        | -         |
| Exercise of stock options   | 200,678   | 1     | 1,827    | -         | -       | -        | -         |
| Cash dividends<br>(\$ .33 per share)                                    | -         | -     | -        | -         | -       | (2,492)  | -         |
| Earned ESOP shares  | -         | -     | 480      | 528       | -       | -        | -         |
| Earned MRDP shares  | -         | -     | (4)      | -         | 7       | -        | -         |
| Stock option compensation<br>exp.                                       | -         | -     | 50       | -         | -       | -        | -         |
| Change in fair value of<br>securities available<br>for sale, net of tax | -         | -     | -        | -         | -       | -        | (130)     |
| Balance, Sept. 30, 2006   | 7,515,352 | \$ 38 | \$20,888 | (\$3,305) | (\$188) | \$62,933 | (\$1,001) |
| (Unaudited)   |           |       |          |           |         |          |           |
| Net income  | -         | -     | -        | -         | -       | 6,009    | -         |
| Stock split   | -         | 36    | -        | -         | -       | (36)     | -         |
| Issuance of MRDP shares   | 15,080    | -     | 263      | -         | (263)   | -        | -         |
| Repurchase of<br>common stock   | (615,542) | (4)   | (11,232) | -         | -       | -        | -         |
| Exercise of stock<br>options  | 110,470   | -     | 1,207    | -         | -       | -        | -         |
| Cash dividends<br>(\$ .27 per share)                                    | -         | -     | -        | -         | -       | (1,991)  | -         |
| Earned ESOP shares  | -         | -     | 280      | 199       | -       | -        | -         |
| Earned MRDP shares  | -         | -     | -        | -         | 36      | -        | -         |
| Stock option<br>compensation exp.                                       | -         | -     | 19       | -         | -       | -        | -         |
| Change in fair value of<br>securities available<br>for sale, net of tax | -         | -     | -        | -         | -       | -        | 104       |
| Balance, June 30, 2007  | 7,025,360 | \$ 70 | \$11,425 | (\$3,106) | (\$415) | \$66,915 | (\$897)   |

See notes to unaudited condensed consolidated financial statements

5

TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
For the nine months ended June 30, 2007 and 2006  
In thousands  
(unaudited)

| Cash flow from operating activities                                  | Nine Months Ended<br>June 30, |          |
|--|-------------------------------|----------|
|  | 2007                          | 2006     |
| Net income   | \$ 6,009                      | \$ 6,013 |
| Non-cash revenues, expenses, gains and losses<br>included in income: |                               |          |
| Provision for loan losses  | 416                           | -        |
| Depreciation   | 760                           | 755      |
| Deferred federal income taxes  | (178)                         | -        |
| Amortization of core deposit intangible                              | 214                           | 246      |
| Earned ESOP shares   | 199                           | 396      |

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|  |           |           |
|--|-----------|-----------|
| Earned MRDP shares   | 36        | - -       |
| Stock option compensation expense                            | 19        | 38        |
| Stock option tax effect less excess tax benefit              | 110       | 92        |
| Gain on sale of OREO, net                                    | (19)      | (49)      |
| Gain on sale of premises and equipment                       | (64)      | (38)      |
| BOLI cash surrender value increase                           | (343)     | (333)     |
| Gain on sale of loans  | (250)     | (264)     |
| Increase (decrease) in deferred loan origination fees        | 123       | (322)     |
| Loans originated for sale                                    | (20,102)  | (16,000)  |
| Proceeds from sale of loans                                  | 21,636    | 17,595    |
| Increase in other assets, net                                | (412)     | (203)     |
| Increase in other liabilities and accrued expenses, net      | 449       | 85        |
|  | -----     | -----     |
| Net cash provided by operating activities                    | 8,603     | 8,011     |
| <br>Cash flow from investing activities                      |           |           |
| Decrease in certificates of deposit held for investment      | 100       | - -       |
| Proceeds from maturities of securities available<br>for sale | 16,630    | 4,011     |
| Proceeds from maturities of securities held to maturity      | 2         | 17        |
| Increase in loans receivable, net                            | (74,580)  | (10,868)  |
| Additions to premises and equipment                          | (847)     | (1,271)   |
| Proceeds from the disposition of premises and equipment      | 324       | - -       |
| Proceeds from sale of OREO                                   | 37        | 473       |
|  | -----     | -----     |
| Net cash used in investing activities                        | (58,334)  | (7,638)   |
| <br>Cash flow from financing activities                      |           |           |
| Increase in deposits, net                                    | 2,453     | 7,719     |
| Increase (decrease) in FHLB advances - long term             | 5,952     | (577)     |
| Increase (decrease) in FHLB advances - short term            | 43,750    | (8,000)   |
| Increase (decrease) in repurchase agreements                 | (172)     | 371       |
| Proceeds from exercise of stock options                      | 744       | 1,011     |
| ESOP tax effect  | 280       | 299       |
| Stock option excess tax benefit                              | 353       | 376       |
| Purchase and retirement of common stock                      | (11,236)  | (1,745)   |
| Payment of dividends   | (1,991)   | (1,810)   |
|  | -----     | -----     |
| Net cash provided (used in) by financing activities          | 40,133    | (2,356)   |
| <br>Net decrease in cash equivalents                         | (9,598)   | (1,983)   |
| Cash equivalents   |           |           |
| Beginning of period  | 22,789    | 28,718    |
|  | -----     | -----     |
| End of period  | \$ 13,191 | \$ 26,735 |
|  | -----     | -----     |

See notes to unaudited condensed consolidated financial statements  
(continued)

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|  | Nine Months Ended<br>June 30, |          |
|--|-------------------------------|----------|
|  | 2007                          | 2006     |
|  | -----                         |          |
| Supplemental disclosure of cash flow information                   |                               |          |
| Income taxes paid  | \$ 2,674                      | \$ 2,625 |
| Interest paid  | 11,222                        | 7,544    |
| Supplemental disclosure of non-cash investing activities           |                               |          |
| Market value adjustment of securities held for<br>sale, net of tax | 104                           | (489)    |
| Loans transferred to OREO and other repossessed<br>assets          | 71                            | 27       |
| Supplemental disclosure of non-cash financing activities           |                               |          |
| Shares issued to MRDP  | 263                           | - -      |

See notes to unaudited condensed consolidated financial statements

7

TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
For the three and nine months ended June 30, 2007 and 2006  
In thousands  
(unaudited)

|  | Three Months Ended<br>June 30, |         | Nine Months Ended<br>June 30, |         |
|--|--------------------------------|---------|-------------------------------|---------|
|  | 2007                           | 2006    | 2007                          | 2006    |
|  | -----                          |         | -----                         |         |
| Comprehensive income:  |                                |         |                               |         |
| Net income   | \$2,138                        | \$2,061 | \$6,009                       | \$6,013 |
| Increase (decrease) in fair<br>value of securities available<br>for sale, net of tax | (162)                          | (197)   | 104                           | (489)   |
|  | -----                          |         | -----                         |         |
| Total comprehensive income   | \$1,976                        | \$1,864 | \$6,113                       | \$5,524 |
|  | =====                          |         | =====                         |         |



See notes to unaudited condensed consolidated financial statements

8

Timberland Bancorp, Inc. and Subsidiaries  
Notes to Condensed Consolidated Financial Statements (unaudited)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Presentation: The accompanying unaudited condensed consolidated financial statements for Timberland Bancorp, Inc. ("Company") were prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions for Form 10-Q and therefore, do not include all disclosures necessary for a complete presentation of financial condition, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. However, all adjustments which are in the opinion of management, necessary for a fair presentation of the interim condensed consolidated financial statements have been included. All such adjustments are of a normal recurring nature. The unaudited condensed consolidated financial statements should be read in conjunction with the audited financial statements included in the Company's Annual Report on Form 10-K for the year ended September 30, 2006 ("2006 Form 10-K"). The results of operations for the nine months ended June 30, 2007 are not necessarily indicative of the results that may be expected for the entire fiscal year.

(b) Stock Split: On June 5, 2007 the Company's common stock was split two-for-one in the form of a 100% stock dividend. Each shareholder of record as of May 22, 2007 received one additional share for every share owned. All share and per share amounts (including stock options) in the condensed consolidated financial statements and accompanying notes were restated to reflect the split, except as otherwise noted.

(c) Principles of Consolidation: The interim condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Timberland Bank ("Bank"), and the Bank's wholly-owned subsidiary, Timberland Service Corp. All significant inter-company balances have been eliminated in consolidation.

(d) Operating Segment: The Company provides a broad range of financial services to individuals and companies located primarily in Western Washington. These services include demand, time and savings deposits; real estate, business and consumer lending; escrow services; and investment advisory services. While the Company's chief decision maker monitors the revenue streams from the various products and services, operations are managed and financial performance is evaluated on a Company-wide basis. Accordingly, all of our operations are considered by management to be aggregated in one reportable operating segment.

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

(f) Certain prior period amounts have been reclassified to conform to the June 30, 2007 presentation with no change to net income or shareholders' equity previously reported.

### (2) EARNINGS PER SHARE

Basic earnings per share ("EPS") is computed by dividing net income by the weighted average number of common shares outstanding during the period, without considering any dilutive items. Diluted EPS is computed by dividing net income by the weighted average number of common shares and common stock equivalents for items that are dilutive, net of shares assumed to be repurchased using the treasury stock method at the average share price for the Company's common stock during the period. Common stock equivalents arise from assumed conversion of outstanding stock options and awarded but not released MRDP shares. In accordance with Statement of Position ("SOP") 93-6, Employers' Accounting for Employee Stock Ownership Plans, issued by

9

the American Institute of Certified Public Accountants, shares owned by the Bank's ESOP that have not been allocated are not considered to be outstanding for the purpose of computing earnings per share. At June 30, 2007 and 2006, there were 440,830 and 511,364 ESOP shares, respectively, that had not been allocated.

|  | Three Months Ended<br>June 30, |             | Nine Months Ended<br>June 30, |             |
|--|--------------------------------|-------------|-------------------------------|-------------|
|  | 2007                           | 2006        | 2007                          | 2006        |
| Basic EPS computation  |                                |             |                               |             |
| Numerator - net income   | \$2,138,000                    | \$2,061,000 | \$6,009,000                   | \$6,013,000 |
| Denominator - weighted<br>average common shares<br>outstanding | 6,713,777                      | 7,141,700   | 6,863,253                     | 7,058,116   |
| Basic EPS  | \$ 0.32                        | \$ 0.29     | \$ 0.88                       | \$ 0.85     |
| Diluted EPS computation  |                                |             |                               |             |
| Numerator - net income   | \$2,138,000                    | \$2,061,000 | \$6,009,000                   | \$6,013,000 |
| Denominator - weighted<br>average common shares<br>outstanding | 6,713,777                      | 7,141,700   | 6,863,253                     | 7,058,116   |
| Effect of dilutive stock<br>options                            | 193,827                        | 241,176     | 215,232                       | 246,888     |
| Effect of dilutive MRDP<br>shares                              | 2,561                          | -           | 2,045                         | -           |
| Weighted average common shares<br>and common stock equivalents | 6,910,165                      | 7,382,876   | 7,080,530                     | 7,305,004   |



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|  | Shares    | Price  | Value  |
|--|-----------|--------|--------|
|  | -----     | -----  | -----  |
| Options outstanding, beginning of period | 524,144   | \$7.26 | \$1.85 |
| Exercised                                | (110,470) | 6.73   | 1.76   |
| Forfeited                                | (1,000)   | 7.61   | 1.99   |
| Granted                                  | --        | --     | --     |
|  | -----     |        |        |
| Options outstanding, end of period       | 412,674   | \$7.39 | \$1.87 |
| Options exercisable, end of period       | 391,670   | \$7.30 | \$1.85 |

Nine Months Ended  
June 30, 2006  
Total Options Outstanding

|  | Shares    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Grant Date<br>Fair<br>Value |
|--|-----------|--|--|
|  | -----     | -----                                    | -----  |
| Options outstanding, beginning of period | 724,822   | \$6.93                                   | \$1.79   |
| Exercised                                | (167,678) | 6.04                                     | 1.64   |
| Granted                                  | --        | --                                       | --   |
|  | -----     |  |  |
| Options outstanding, end of period       | 557,144   | \$7.20                                   | \$1.84   |
| Options exercisable, end of period       | 510,136   | \$7.06                                   | \$1.81   |

The aggregate intrinsic value of all options outstanding at June 30, 2007 was \$3.43 million. The aggregate intrinsic value of all options that were exercisable at June 30, 2007 was \$3.29 million. The aggregate intrinsic value of all options outstanding at June 30, 2006 was \$4.69 million. The aggregate intrinsic value of all options that were exercisable at June 30, 2006 was \$4.36 million.

11

Nine Months Ended June 30,  
Total Unvested Options

|                                       | 2007     |   | 2006     |   |
|---------------------------------------|----------|---|----------|---|
|                                       | Shares   | Weighted<br>Average<br>Grant<br>Date<br>Fair<br>Value | Shares   | Weighted<br>Average<br>Grant<br>Date<br>Fair<br>Value |
|                                       | -----    | -----   | -----    | -----   |
| Unvested options, beginning of period | 45,008   | \$2.15  | 77,680   | \$2.09  |
| Vested                                | (23,004) | 2.07  | (30,672) | 2.00  |
| Forfeited                             | (1,000)  | 1.99  | --       | --  |
| Granted                               | --       | --  | --       | --  |
|                                       | -----    |   | -----    |   |
| Unvested options, end of period       | 21,004   | \$2.23  | 47,008   | \$2.14  |

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The total fair value of options vested during the nine months ended June 30, 2007 was \$48,000. The total fair value of options vested during the nine months ended June 30, 2006 was \$61,000.

Proceeds, related tax benefits realized from options exercised and intrinsic value of options exercised were as follows:

|                                      | Nine Months Ended<br>June 30, |         |
|--------------------------------------|-------------------------------|---------|
|                                      | (In Thousands)                |         |
|                                      | 2007                          | 2006    |
| Proceeds from options exercised      | \$744                         | \$1,012 |
| Related tax benefit recognized       | 463                           | 468     |
| Intrinsic value of options exercised | 1,231                         | 1,377   |

Options outstanding at June 30, 2007 were as follows:

| Outstanding                 |         |  |   | Exercisable |  |   |
|-----------------------------|---------|--|---|-------------|--|---|
| Range<br>Exercise<br>Prices | Shares  | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (Years) | Shares      | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (Years) |
| \$ 6.00-6.19                | 233,810 | \$ 6.00                                  | 1.7   | 233,810     | \$ 6.00                                  | 1.7   |
| 6.80-7.45                   | 66,638  | 7.35                                     | 3.9   | 66,638      | 7.35                                     | 3.9   |
| 7.60-7.98                   | 6,000   | 7.91                                     | 4.9   | 2,000       | 7.85                                     | 4.8   |
| 9.53                        | 56,680  | 9.52                                     | 5.7   | 39,676      | 9.52                                     | 5.7   |
| 11.46-11.63                 | 49,546  | 11.51                                    | 6.5   | 49,546      | 11.51                                    | 6.5   |
|                             | 412,674 | \$ 7.39                                  | 3.2   | 391,670     | \$ 7.30                                  | 3.1   |

12

Options outstanding at June 30, 2006 were as follows:

| Outstanding                 |         |  |   | Exercisable |  |   |
|-----------------------------|---------|--|---|-------------|--|---|
| Range<br>Exercise<br>Prices | Shares  | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (Years) | Shares      | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (Years) |
| \$ 6.00-6.19                | 351,110 | \$ 6.01                                  | 2.6   | 350,110     | \$ 6.01                                  | 2.6   |
| 6.80-7.45                   | 66,678  | 7.35                                     | 5.1   | 60,010      | 7.35                                     | 5.1   |
| 7.60-7.98                   | 21,000  | 7.76                                     | 5.7   | 10,000      | 7.68                                     | 5.6   |
| 9.53                        | 56,680  | 9.53                                     | 6.7   | 28,340      | 9.53                                     | 6.7   |
| 11.46-11.63                 | 61,676  | 11.53                                    | 7.6   | 61,676      | 11.53                                    | 7.6   |
|                             | 557,144 | \$ 7.20                                  | 4.0   | 510,136     | \$ 7.06                                  | 3.8   |

There were no options granted during the nine months ended June 30, 2007 and June 30, 2006.

### Stock Grant Plans

The Company adopted the MRDP in 1998, which was subsequently approved by shareholders in 1999 for the benefit of employees, officers and directors of

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the Company. The objective of the MRDP is to retain and attract personnel of experience and ability in key positions by providing them with a proprietary interest in the Company.

The MRDP allows for the issuance to participants of up to 529,000 shares of the Company's common stock. Shares may be purchased in the open market or may be issued from authorized and unissued shares. Awards under the MRDP are made in the form of restricted shares of common stock that are subject to restrictions on the transfer of ownership. Compensation expense in the amount of the fair value of the common stock at the date of the grant to the plan participants is recognized over a five-year vesting period, with 20% vesting on each of the five anniversaries from the date of the grant. During the nine months ended June 30, 2007 the Company awarded 15,080 MRDP shares to officers and directors. These shares had a weighted average grant date fair value of \$17.44 per share. There were no MRDP shares granted during the nine months ended June 30, 2006.

At June 30, 2007 there were a total of 27,080 unvested MRDP shares with a weighted average grant date fair value of \$16.90. There were no MRDP shares that vested during the nine months ended June 30, 2007 and 2006. At June 30, 2007, there were 92,066 shares available for future award under the MRDP.

### Expenses for Stock Compensation Plans

Compensation expenses for all stock-based plans were as follows:

|   | Nine Months Ended June 30, |                 |                  |                 |
|---|----------------------------|-----------------|------------------|-----------------|
|   | 2007                       |                 |                  | 2006            |
|   | (In thousands)             |                 |                  |                 |
|   | Stock<br>Options           | Stock<br>Grants | Stock<br>Options | Stock<br>Grants |
| Compensation expense recognized in income | \$ 19                      | \$ 40           | \$ 38            | \$ - -          |
| Related tax benefit recognized            | 7                          | 14              | 13               | - -             |

13

The compensation expense yet to be recognized for stock based awards that have been awarded but not vested for the years ending September 30 is as follows (in thousands):

|                   | Stock<br>Options | Stock<br>Grants | Total<br>Awards |
|-------------------|------------------|-----------------|-----------------|
| Remainder of 2007 | \$ 6             | \$ 23           | \$ 29           |
| 2008              | 5                | 92              | 97              |
| 2009              | 2                | 92              | 94              |
| 2010              | 1                | 91              | 92              |
| 2011              | --               | 85              | 85              |
| 2012              | --               | 32              | 32              |
|                   | ----             | ----            | ----            |
| Total             | \$14             | \$415           | \$429           |

### (5) DIVIDEND / SUBSEQUENT EVENT

On July 12, 2007, the Company announced a quarterly cash dividend of \$0.10 per common share, payable August 23, 2007, to shareholders of record as of the

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close of business on August 9, 2007.

### (6) RECENT ACCOUNTING PRONOUNCEMENTS

In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value under Generally Accepted Accounting Principles ("GAAP"), and expands disclosures about fair value measurements. This Statement expands other accounting pronouncements that require or permit fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Management is assessing the impact of adoption of SFAS 157 on the Company's consolidated financial statements.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109 ("FIN 48"). The interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The new interpretation is effective for fiscal years beginning after December 15, 2006. The Company will adopt the provisions of FIN 48 on October 1, 2007 and is currently evaluating FIN 48 to determine the effect the guidance will have on the Company's consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets. SFAS No. 156 amends Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, to require all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable. SFAS No. 156 also permits servicers to subsequently measure each separate class of servicing assets and liabilities at fair value rather than at the lower of cost or market. For those companies that elect to measure their servicing assets and liabilities at fair value, SFAS No. 156 requires the difference between the recorded value and fair value at the date of adoption to be recognized as a cumulative effect adjustment to retained earnings as of the beginning of the fiscal year in which the election is made. The Company adopted SFAS No. 156 on October 1, 2006 and will continue to measure servicing assets at the lower of cost or market.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with

14

the FASB's long-term measurement objectives for accounting for financial instruments. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The adoption of this Statement is not expected to have a material impact on the Company's consolidated financial statements.

Item 2. Management's Discussion and Analysis of Financial Condition and

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Results of Operations  
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The following analysis discusses the material changes in the financial condition and results of operations of the Company at and for the three and nine months ended June 30, 2007. This analysis as well as other sections of this report contains certain "forward-looking statements." The Company desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 and is including this statement for the express purpose of availing itself of the protection of such safe harbor with forward looking statements. These forward looking statements may describe future plans or strategies and include the Company's expectations of future financial results. The words "believe," "expect," "anticipate," "estimate," "project," and similar expressions identify forward-looking statements. The Company's ability to predict results or the effect of future plans or strategies is inherently uncertain. The Company's actual results, performance, or achievements may differ materially from those suggested, expressed, or implied by forward looking statements as a result of a wide variety or range of factors including, but not limited to: interest rate fluctuations; economic conditions in the Company's primary market areas; deposit flows; demand for residential, commercial real estate, consumer, and other types of loans; real estate values; success of new products and services; technological factors affecting operations; and other risks detailed in the Company's reports filed with the SEC, including its 2006 Form 10-K. Accordingly, these factors should be considered in evaluating forward-looking statements, and undue reliance should not be placed on such statements. The Company undertakes no responsibility to update or revise any forward-looking statements.

### Overview

Timberland Bancorp, Inc., a Washington corporation, was organized on September 8, 1997 for the purpose of becoming the holding company for Timberland Savings Bank, SSB upon the Bank's conversion from a Washington-chartered mutual savings bank to a Washington-chartered stock savings bank ("Conversion"). The Conversion was completed on January 12, 1998 through the sale and issuance of 13,225,000 shares of common stock by the Company. At June 30, 2007, the Company had total assets of \$624.15 million and total shareholders' equity of \$73.99 million. The Company's business activities generally are limited to passive investment activities and oversight of its investment in the Bank. Accordingly, the information set forth in this report relates primarily to the Bank.

The Bank was established in 1915 as "Southwest Washington Savings and Loan Association." In 1935, the Bank converted from a state-chartered mutual savings and loan association to a federally-chartered mutual savings and loan association, and in 1972 changed its name to "Timberland Federal Savings and Loan Association." In 1990, the Bank converted to a federally chartered mutual savings bank under the name "Timberland Savings Bank, FSB." In 1991, the Bank converted to a Washington-chartered mutual savings bank and changed its name to "Timberland Savings Bank, SSB." In 2000, the Bank changed its name to "Timberland Bank." The Bank's deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") up to applicable legal limits. The Bank has been a member of the Federal Home Loan Bank System since 1937. The Bank is regulated by the Washington State Department of Financial Institutions, Division of Banks and the FDIC.

The Bank is a community-oriented bank which offers a variety of deposit and loan products to its customers. The Bank operates 21 branches (including its main office in Hoquiam) and a loan production office in the following market areas:



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- \* Grays Harbor County
- \* Thurston County
- \* Pierce County
- \* King County
- \* Kitsap County
- \* Lewis County

### Critical Accounting Policies and Estimates

The Company has identified two accounting policies that as a result of judgments, estimates and assumptions inherent in those policies, are critical to an understanding of the Company's Consolidated Financial Statements.

**Allowance for Loan Losses.** The allowance for loan losses is maintained at a level sufficient to provide for probable loan losses based on evaluating known and inherent risks in the portfolio. The allowance is based upon management's comprehensive analysis of the pertinent factors underlying the quality of the loan portfolio. These factors include changes in the amount and composition of the loan portfolio, actual loss experience, current economic conditions, and detailed analysis of individual loans for which the full collectibility may not be assured. The appropriate allowance for loan loss level is estimated based upon factors and trends identified by management at the time consolidated financial statements are prepared.

**Mortgage Servicing Rights.** Mortgage servicing rights ("MSRs") are capitalized when acquired through the origination of loans that are subsequently sold with servicing rights retained and are amortized to servicing income on loans sold in proportion to and over the period of estimated net servicing income. The value of MSRs at the date of the sale of loans is determined based on the discounted present value of expected future cash flows using key assumptions for servicing income and costs and prepayment rates on the underlying loans. The estimated fair value is periodically evaluated for impairment by comparing actual cash flows and estimated cash flows from the servicing assets to those estimated at the time servicing assets were originated. The effect of changes in market interest rates on estimated rates of loan prepayments represents the predominant risk characteristic underlying the MSR portfolio. The Company's methodology for estimating the fair value of MSRs is highly sensitive to changes in assumptions. For example, the determination of fair value uses anticipated prepayment speeds. Actual prepayment experience may differ and any difference may have a material effect on the fair value. Thus, any measurement of MSRs' fair value is limited by the conditions existing and assumptions as of the date made. Those assumptions may not be appropriate if they are applied at different times.

### Comparison of Financial Condition at June 30, 2007 and September 30, 2006

The Company's total assets increased by \$47.06 million, or 8.2%, to \$624.15 million at June 30, 2007 from \$577.09 million at September 30, 2006, primarily attributable to a \$72.68 million, or 17.1%, increase in net loans receivable. This increase was partially offset by a \$16.50 million decrease in investment and mortgage-backed securities and a \$9.60 million decrease in cash equivalents.

Total deposits increased by \$2.45 million to \$433.51 million at June 30, 2007 from \$431.06 million at September 30, 2006 primarily attributable to an increase in certificate of deposit accounts and money market accounts. These increases were partially offset by decreases in non-interest bearing accounts and N.O.W. checking accounts.

Shareholders' equity decreased by \$5.38 million to \$73.99 million at June 30,

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2007 from \$79.37 million at September 30, 2006. The decrease in shareholders equity was primarily a result of share repurchases and dividends paid to shareholders.

16

A more detailed explanation of the changes in significant balance sheet categories follows:

**Cash Equivalents:** Cash equivalents decreased by \$9.60 million or 42.1% to \$13.19 million at June 30, 2007 from \$22.79 million at September 30, 2006. The decrease was primarily a result of federal funds sold decreasing by \$5.20 million, non-interest bearing accounts decreasing by \$3.07 million, and interest bearing deposits in banks decreasing by \$1.33 million. These liquid funds decreased primarily to fund loan portfolio growth.

**Investment Securities and Mortgage-backed Securities:** Investment and mortgage-backed securities decreased by \$16.50 million or 20.3% to \$64.98 million at June 30, 2007 from \$81.48 million at September 30, 2006, as a result of regular amortization and prepayments on mortgage-backed securities and the maturity or call of U.S. agency securities. At June 30, 2007, the Company's securities' portfolio was comprised of mutual funds of \$31.86 million, U.S. agency securities of \$18.90 million, and mortgage-backed securities of \$14.22 million. The mutual funds invest primarily in mortgage-backed products and U.S. agency securities. For additional information, see the "Investment Securities" table included herein.

**Loans:** Net loans receivable increased by \$72.68 million or 17.1% to \$497.33 million at June 30, 2007 from \$424.65 million at September 30, 2006. The increase in the portfolio was primarily a result of a \$26.96 million increase in construction loans (net of undisbursed portion of construction loans in process), a \$24.20 million increase in land loans, a \$14.03 million increase in multi-family loans, a \$7.52 million increase in consumer loans, a \$5.17 million increase in one- to four-family loans and a \$4.82 million increase in commercial business loans. These increases were partially offset by a \$9.49 million decrease in commercial real estate loans. The majority of the increase in multi-family loan category was a result of several loans being switched to the multi-family category from the commercial real estate category.

Loan demand remained strong as loan originations totaled \$233.37 million for the nine months ended June 30, 2007 compared to \$169.82 million for nine months ended June 30, 2006. The Bank also continued to sell longer-term fixed rate loans for asset liability management purposes. The Bank sold fixed rate one- to four-family mortgage loans totaling \$21.64 million for nine months ended June 30, 2007 compared to \$17.60 million for the nine months ended June 30, 2006.

For additional information, see the sections entitled "Loan Portfolio Composition" and "Construction and Land Development Loan Portfolio Composition" included herein.

**Other Real Estate Owned and Other Repossessed Items:** OREO and other repossessed items increased to \$68,000 at June 30, 2007 from \$15,000 at September 30, 2006 as one manufactured home was repossessed. At June 30, 2007, OREO and other repossessed items consisted of one manufactured home. For additional information, see the section entitled "Non-performing Assets" included herein.

**Premises and Equipment:** Premises and equipment decreased to \$16.56 million at June 30, 2007 from \$16.73 million at September 30, 2006. The decrease was

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primarily a result of selling a land parcel in Grays Harbor County.

**Goodwill and Core Deposit Intangible:** The value of goodwill remained unchanged. The amortized value of core deposit intangible decreased to \$1.29 million at June 30, 2007 from \$1.51 million at September 30, 2006. The decrease is attributable to scheduled amortization of the core deposit intangible.

**Deposits:** Deposits increased by \$2.45 million, or 0.6%, to \$433.51 million at June 30, 2007 from \$431.06 million at September 30, 2006. The deposit increase was primarily a result of a \$15.61 million increase in certificate of deposit accounts and a \$4.07 million increase in money market accounts. These increases were

17

partially offset by a decrease of \$9.22 million in N.O.W. checking accounts, a \$7.33 million decrease in non-interest bearing accounts, and a \$677,000 decrease in savings accounts. For additional information, see the section entitled "Deposit Breakdown" included herein.

**FHLB Advances and Other Borrowings:** FHLB advances and other borrowings increased by \$49.53 million to \$113.24 million at June 30, 2007 from \$63.71 million at September 30, 2006 as the Bank used additional advances to fund loan portfolio growth. For additional information, see "FHLB Advance Maturity Schedule" included herein.

**Shareholders' Equity:** Total shareholders' equity decreased by \$5.38 million to \$73.99 million at June 30, 2007 from \$79.37 million at September 30, 2006, primarily as a result of share repurchases of \$11.24 million and dividends to shareholders of \$1.99 million. These decreases to shareholders' equity were partially offset by net income of \$6.01 million, an increase of \$1.72 million from the exercise of stock options and vesting associated with the Company's benefit plans, and a \$104,000 net increase in the fair value of securities available for sale.

During the nine months ended June 30, 2007 the Company repurchased 615,542 shares of its common stock for \$11.24 million at an average price of \$18.25 per share. Cumulatively, the Company has repurchased 7,566,984 shares (57.2%) of the 13,225,000 shares that were issued in its 1998 initial public offering, at an average price of \$8.82 per share. For additional information, see Item 2 of Part II of this Form 10-Q.

**Non-performing Assets:** Non-performing assets to total assets were 0.17% at June 30, 2007 compared to 0.02% at September 30, 2006, as total non-performing assets increased to \$1.05 million at June 30, 2007 from \$95,000 at September 30, 2006.

Total non-performing assets of \$1.05 million at June 30, 2007 consisted of a \$347,000 commercial real estate loan, four single-family mortgage loans totaling \$351,000, a \$250,000 single-family construction loan, a \$34,000 land loan and other repossessed items totaling \$68,000. The Company had a net charge-off of \$9,000 during the nine months ended June 30, 2007. For additional information, see the section entitled "Non-performing Assets" and "Activity in the Allowance for Loan Losses" included herein.

### Investment Securities

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The following table sets forth the composition of the Company's investment securities portfolio.

At June 30,  
2007

At September 30,  
2006

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|                                    | Amount   | Percent | Amount   | Percent |
|------------------------------------|----------|---------|----------|---------|
|                                    | -----    | -----   | -----    | -----   |
| (Dollars in thousands)             |          |         |          |         |
| Held-to-maturity:                  |          |         |          |         |
| Mortgage-backed securities         | \$ 72    | 0.1%    | \$ 75    | 0.1%    |
| Available-for-sale (at fair value) |          |         |          |         |
| U.S. agency securities             | 18,904   | 29.1    | 31,718   | 38.9    |
| Mortgage-backed securities         | 14,145   | 21.8    | 17,603   | 21.6    |
| Mutual funds                       | 31,862   | 49.0    | 32,087   | 39.4    |
|                                    | -----    | -----   | -----    | -----   |
| Total portfolio                    | \$64,983 | 100.0%  | \$81,483 | 100.0%  |
|                                    | =====    | =====   | =====    | =====   |

18

Loan Portfolio Composition

The following table sets forth the composition of the Company's loan portfolio.

|   | At June 30,<br>2007 |         | At September 30,<br>2006 |         |
|---|---------------------|---------|--------------------------|---------|
|   | Amount              | Percent | Amount                   | Percent |
|   | -----               | -----   | -----                    | -----   |
| (Dollars in thousands)                                  |                     |         |                          |         |
| Mortgage loans:   |                     |         |                          |         |
| One- to four-family (1)                                 | \$103,883           | 18.2%   | \$98,709                 | 20.1%   |
| Multi-family  | 31,719              | 5.6     | 17,689                   | 3.6     |
| Commercial  | 128,118             | 22.4    | 137,609                  | 28.1    |
| Construction and<br>land development                    | 181,157             | 31.7    | 146,855                  | 29.9    |
| Land  | 53,794              | 9.4     | 29,598                   | 6.0     |
|   | -----               | -----   | -----                    | -----   |
| Total mortgage loans                                    | 498,671             | 87.3    | 430,460                  | 87.7    |
| Consumer loans:   |                     |         |                          |         |
| Home equity and second mortgage                         | 44,347              | 7.8     | 37,435                   | 7.6     |
| Other   | 11,735              | 2.0     | 11,127                   | 2.3     |
|   | -----               | -----   | -----                    | -----   |
|   | 56,082              | 9.8     | 48,562                   | 9.9     |
| Commercial business loans                               | 16,625              | 2.9     | 11,803                   | 2.4     |
|   | -----               | -----   | -----                    | -----   |
| Total loans   | 571,378             | 100.0%  | 490,825                  | 100.0%  |
|   | =====               | =====   | =====                    | =====   |
| Less:   |                     |         |                          |         |
| Undisbursed portion of<br>construction loans in process | (66,598)            |         | (59,260)                 |         |
| Deferred loan origination fees                          | (2,921)             |         | (2,798)                  |         |
| Allowance for loan losses                               | (4,529)             |         | (4,122)                  |         |
|   | -----               |         | -----                    |         |
| Total loans receivable, net                             | \$497,330           |         | \$424,645                |         |
|   | =====               |         | =====                    |         |

(1) Includes loans held-for-sale.

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### Construction and Land Development Loan Portfolio Composition

The following table sets forth the composition of the Company's construction and land development loan portfolio.

|                                 | At June 30,<br>2007 |         | At September 30,<br>2006 |         |
|---------------------------------|---------------------|---------|--------------------------|---------|
|                                 | Amount              | Percent | Amount                   | Percent |
| (Dollars in thousands)          |                     |         |                          |         |
| Custom and owner/builder const. | \$ 48,894           | 27.0%   | \$ 46,346                | 31.6%   |
| Speculative construction        | 43,655              | 24.1    | 34,363                   | 23.4    |
| Commercial real estate          | 50,729              | 28.0    | 42,398                   | 28.9    |
| Multi-family                    | 19,801              | 10.9    | 7,662                    | 5.2     |
| Land development                | 18,078              | 10.0    | 16,086                   | 10.9    |
|                                 | -----               | -----   | -----                    | -----   |
| Total construction loans        | \$181,157           | 100.0%  | \$146,855                | 100.0%  |
|                                 | =====               | =====   | =====                    | =====   |

19

### Activity in the Allowance for Loan Losses

The following table sets forth information regarding activity in the allowance for loan losses.

|  | Three Months Ended<br>June 30, |         |
|--|--------------------------------|---------|
|  | 2007                           | 2006    |
| (In thousands)                             |                                |         |
| Balance at beginning of period             | \$4,272                        | \$4,119 |
| Provision for loan losses                  | 260                            | -       |
| Loans charged off                          | (3)                            | (2)     |
| Recoveries on loans previously charged off | --                             | 3       |
|  | -----                          | -----   |
| Net recovery (charge-off)                  | (3)                            | 1       |
|  | -----                          | -----   |
| Balance at end of period                   | \$4,529                        | \$4,120 |
|  | =====                          | =====   |

|  | Nine Months Ended<br>June 30, |         |
|--|-------------------------------|---------|
|  | 2007                          | 2006    |
| (In thousands)                             |                               |         |
| Balance at beginning of period             | \$4,122                       | \$4,099 |
| Provision for loan losses                  | 416                           | -       |
| Loans charged off                          | (10)                          | (2)     |
| Recoveries on loans previously charged off | 1                             | 23      |
|  | -----                         | -----   |
| Net recovery (charge-off)                  | (9)                           | 21      |
|  | -----                         | -----   |
| Balance at end of period                   | \$4,529                       | \$4,120 |
|  | =====                         | =====   |

### Non-performing Assets

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The following table sets forth information with respect to the Company's non-performing assets.

|   | At<br>June 30,<br>2007 | At<br>September 30,<br>2006 |
|---|------------------------|-----------------------------|
| -----<br>(Dollars in thousands)                                     |                        |                             |
| Loans accounted for on a non-accrual basis:                         |                        |                             |
| Mortgage loans:   |                        |                             |
| One- to four-family   | \$ 351                 | \$ 80                       |
| Commercial real estate  | 347                    | - -                         |
| Construction and land development                                   | 250                    | - -                         |
| Land  | 34                     | - -                         |
|   | -----                  | -----                       |
| Total   | 982                    | 80                          |
|   |                        |                             |
| Accruing loans which are contractually<br>past due 90 days or more: |                        |                             |
|   | - -                    | - -                         |
|   | -----                  | -----                       |
| Total   | - -                    | - -                         |
|   |                        |                             |
| Total of non-accrual and<br>90 days past due loans                  |                        |                             |
|   | 982                    | 80                          |
|   |                        |                             |
| Other real estate owned and other<br>repossessed items              |                        |                             |
|   | 68                     | 15                          |
|   | -----                  | -----                       |
| Total non-performing assets   | \$1,050                | \$ 95                       |
|   | =====                  | =====                       |

20

|  |           |           |
|--|-----------|-----------|
| Restructured loans   | - -       | - -       |
|  |           |           |
| Non-accrual and 90 days or more past<br>due loans as a percentage of loans<br>receivable (1) | 0.20%     | 0.02%     |
|  |           |           |
| Non-accrual and 90 days or more past<br>due loans as a percentage of total assets            | 0.16%     | 0.01%     |
|  |           |           |
| Non-performing assets as a percentage<br>of total assets                                     | 0.17%     | 0.02%     |
|  |           |           |
| Loans receivable (1)   | \$501,859 | \$428,767 |
|  | =====     | =====     |
|  |           |           |
| Total assets   | \$624,146 | \$577,087 |
|  | =====     | =====     |

(1) Includes loans held-for-sale and is before the allowance for loan losses.

### Deposit Breakdown

-----

The following table sets forth the composition of the Company's deposit balances.

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|  | At<br>June 30, 2007 | At<br>September 30, 2006 |
|--|---------------------|--------------------------|
| -----<br>(In thousands)                    |                     |                          |
| Non-interest bearing                       | \$ 50,580           | \$ 57,905                |
| N.O.W. checking                            | 80,290              | 89,509                   |
| Savings                                    | 59,558              | 60,235                   |
| Money market accounts                      | 46,446              | 42,378                   |
| Certificates of deposit under \$100,000    | 131,803             | 128,183                  |
| Certificates of deposit \$100,000 and over | 64,837              | 52,851                   |
|  | -----               | -----                    |
| Total Deposits                             | \$433,514           | \$431,061                |
|  | =====               | =====                    |

FHLB Advance Maturity Schedule

-----  
The Bank has short- and long-term borrowing lines with the FHLB of Seattle with total credit on the lines equal to 30% of the Bank's total assets, limited by available collateral. Borrowings are considered short-term when the original maturity is less than one year. FHLB advances consisted of the following:

|                                 | At June 30,<br>2007 |         | At September 30,<br>2006 |         |
|---------------------------------|---------------------|---------|--------------------------|---------|
|                                 | Amount              | Percent | Amount                   | Percent |
| -----<br>(Dollars in thousands) |                     |         |                          |         |
| Short-term                      | \$ 72,750           | 64.7%   | \$29,000                 | 46.2%   |
| Long-term                       | 39,713              | 35.3    | 33,761                   | 53.8    |
|                                 | -----               | -----   | -----                    | -----   |
| Total FHLB advances             | \$112,463           | 100.0%  | \$62,761                 | 100.0%  |
|                                 | =====               | =====   | =====                    | =====   |

21

The Bank's FHLB borrowings mature at various dates through December 2016 and bear interest at rates ranging from 4.10% to 6.18%. Principal reduction amounts due for future years ending September 30 are as follows (in thousands):

|            |           |
|------------|-----------|
| 2007       | \$ 72,767 |
| 2008       | 15,069    |
| 2009       | 4,627     |
| 2010       | - -       |
| 2011       | - -       |
| Thereafter | 20,000    |
|            | -----     |
| Total      | \$112,463 |
|            | =====     |

A portion of these advances have a puttable feature and may be called by the FHLB earlier than the above schedule indicates.

Comparison of Operating Results for the Three and Nine Months Ended June 30,

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2007 and 2006

The Company's net income increased by \$77,000 or 3.7% to \$2.14 million for the quarter ended June 30, 2007 from \$2.06 million for the quarter ended June 30, 2006. Diluted earnings per share increased 10.7% to \$0.31 for the quarter ended June 30, 2007 from \$0.28 for the quarter ended June 30, 2006.

Net income decreased slightly by \$4,000 but remained at \$6.01 million for the nine months ended June 30, 2007 and for the comparable period in 2006. Diluted earnings per share increased to \$0.85 for the nine months ended June 30, 2007 from \$0.82 for the nine months ended June 30, 2006.

The increase in diluted earnings per share was primarily a result of increased net interest income and a decrease in the weighted average number of shares outstanding due to share repurchases. Net interest income increased during the current periods as a result of a larger interest earning asset base, however, margin compression resulting from higher funding costs mitigated the impact of this growth. Following the industry trend and a flat yield curve environment, the net interest margin compressed to 4.67% and 4.72% for the three and nine months ended June 30, 2007 from 5.00% and 4.90% for the three and nine months ended June 30, 2006.

A more detailed explanation of the income statement categories is presented below.

**Net Income:** Net income for the quarter ended June 30, 2007 increased by \$77,000 to \$2.14 million from \$2.06 million for the quarter ended June 30, 2006. Earnings per diluted share for the quarter ended June 30, 2007 increased to \$0.31 from \$0.28 for the quarter ended June 30, 2006. The \$0.03 increase in diluted earnings per share for the quarter ended June 30, 2007 was primarily a result of a \$370,000 (\$244,000 net of income tax - \$0.04 per diluted share) increase in net interest income and a decrease in the number of weighted average shares outstanding (\$0.02 per diluted share) primarily due to share repurchases. These increases to earnings per share were partially offset by a \$260,000 (\$172,000 net of income tax - \$0.03 per diluted share) increase in the provision for loan losses.

Net income for the nine months ended June 30, 2007 decreased by \$4,000 to \$6.01 million, or \$0.85 per diluted share from \$6.01 million, or \$0.82 per diluted share for the nine months ended June 30, 2006. The \$0.03 increase in diluted earnings per share for the nine months ended June 30, 2007 was primarily the result of a \$1.04 million (\$690,000 net of income tax - \$0.10 per diluted share) increase in net interest income, and a decrease in the number of weighted average shares outstanding (\$0.03 per diluted share) primarily due to share

22

repurchases. These increases were partially offset by a \$449,000 (\$296,000 net of income tax - \$0.04 per diluted share) increase in non-interest expense, a \$416,000 (\$275,000 net of income tax - \$0.04 per diluted share) increase in the provision for loan losses and a \$187,000 (\$123,000 net of income tax - \$0.02 per diluted share) decrease in non-interest income.

**Net Interest Income:** Net interest income increased by \$370,000, or 5.9%, to \$6.66 million for the quarter ended June 30, 2007 from \$6.29 million for the quarter ended June 30, 2006, primarily as a result of a larger interest earning asset base. Total interest income increased by \$1.74 million to \$10.81 million for the quarter ended June 30, 2007 from \$9.07 million for the quarter ended June 30, 2006 as average total interest earning assets increased



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by \$67.79 million. The yield on interest earning assets increased to 7.58% for the quarter ended June 30, 2007 from 7.22% for the quarter ended June 30, 2006. Total interest expense increased by \$1.37 million to \$4.16 million for the quarter ended June 30, 2007 from \$2.79 million for the quarter ended June 30, 2006 as the average rate paid on interest bearing liabilities increased to 3.42% for the quarter ended June 30, 2007 from 2.65% for the quarter ended June 30, 2006. The net interest margin decreased to 4.67% for the quarter ended June 30, 2007 from 5.00% for the quarter ended June 30, 2006.

Net interest income increased by \$1.04 million to \$19.42 million for the nine months ended June 30, 2007 from \$18.38 million for the nine months ended June 30, 2006, primarily as a result of a larger interest earning asset base. Total interest income increased by \$4.58 million to \$30.75 million for the nine months ended June 30, 2007 from \$26.17 million for the nine months ended June 30, 2006 as average total interest earning assets increased by \$49.32 million. The yield on interest earning assets increased to 7.47% for the nine months ended June 30, 2007 from 6.98% for the nine months ended June 30, 2006. Total interest expense increased by \$3.54 million to \$11.33 million for the nine months ended June 30, 2007 from \$7.79 million for the nine months ended June 30, 2006 as the average rate paid on interest bearing liabilities increased to 3.26% for the nine months ended June 30, 2007 from 2.47% for the nine months ended June 30, 2006. The net interest margin decreased to 4.72% for the nine months ended June 30, 2007 from 4.90% for the nine months ended June 30, 2006.

The margin compression was primarily attributable to increased funding costs which were greater than the increased yield on interest earning assets. Increased funding costs resulted from an increase in interest rates on deposits and an increased reliance on FHLB advances to fund loan growth. For additional information, see the section entitled "Rate Volume Analysis" included herein.

### Rate Volume Analysis

The following table sets forth the effects of changing rates and volumes on the net interest income on the Company. Information is provided with respect to the (i) effects on interest income attributable to change in volume (changes in volume multiplied by prior rate), and (ii) effects on interest income attributable to changes in rate (changes in rate multiplied by prior volume), and (iii) the net change (sum of the prior columns). Changes in rate/volume have been allocated to rate and volume variances based on the absolute values of each.

|                                  | Three months ended<br>June 30, 2007<br>compared to three months<br>ended June 30, 2006<br>increase (decrease)<br>due to |         |               | Nine months ended<br>June 30, 2007<br>compared to nine months<br>ended June 30, 2006<br>increase (decrease)<br>due to |         |               |
|----------------------------------|---|---------|---------------|---|---------|---------------|
|                                  | Rate  | Volume  | Net<br>Change | Rate  | Volume  | Net<br>Change |
|                                  | ----  | -----   | -----         | ----  | -----   | -----         |
|                                  | (In thousands)  |         |               |   |         |               |
| Interest-earning assets:         |   |         |               |   |         |               |
| Loans receivable (1)             | \$ 39   | \$1,904 | \$1,943       | \$ 728  | \$4,179 | \$4,907       |
| Investments and                  |   |         |               |   |         |               |
| mortgage-backed securities       |   | 23      |               |   |         |               |
| FHLB stock and equity securities | 27  | (206)   | (179)         | (14)  | (443)   | (457)         |
| equity securities                | 49  | 7       | 56            | 211   | 12      | 223           |

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|   |         |        |        |         |         |         |
|---|---------|--------|--------|---------|---------|---------|
| Federal funds sold  | 7       | (77)   | (70)   | (4)     | (97)    | (101)   |
| Interest-bearing deposits                                     | 2       | (12)   | (10)   | 7       | - -     | 7       |
|   | -----   | -----  | -----  | -----   | -----   | -----   |
| Total net increase in income on interest-earning assets       | 124     | 1,616  | 1,740  | 928     | 3,651   | 4,579   |
| Interest-bearing liabilities:                                 |         |        |        |         |         |         |
| Savings accounts  | 1       | (4)    | (3)    | - -     | (11)    | (11)    |
| NOW accounts  | (5)     | (24)   | (29)   | 7       | (24)    | (17)    |
| Money market Accounts   | 135     | 30     | 165    | 331     | 15      | 346     |
| Certificate accounts  | 415     | 260    | 675    | 1,461   | 779     | 2,240   |
| Short-term borrowings   | 4       | 649    | 653    | 41      | 1,247   | 1,288   |
| Long-term borrowings  | (23)    | (68)   | (91)   | (59)    | (253)   | (312)   |
|   | -----   | -----  | -----  | -----   | -----   | -----   |
| Total net increase in expense on interest bearing liabilities | 527     | 843    | 1,370  | 1,781   | 1,753   | 3,534   |
| Net increase (decrease) in net interest income                | (\$403) | \$ 773 | \$ 370 | (\$853) | \$1,898 | \$1,045 |

(1) Includes loans originated for sale.

Provision for Loan Losses: A provision for loan losses of \$260,000 was made during the quarter ended June 30, 2007 compared to no provision made during quarter ended June 30, 2006. For the nine months ended June 30, 2007 a provision for loan losses of \$416,000 was made compared to no provision for the nine months ended June 30, 2006. The provisions were made primarily in connection with strong loan portfolio growth and changes in the composition of the loan portfolio. At June 30, 2007, the Company's non-performing assets to total assets were 0.17%.

The Bank has established a comprehensive methodology for determining the provision for loan losses. On a quarterly basis the Bank performs an analysis that considers pertinent factors underlying the quality of the loan portfolio. The factors include changes in the amount and composition of the loan portfolio, historic loss experience for various loan segments, changes in economic conditions, delinquency rates, a detailed analysis of loans on non-accrual status, and other factors to determine an appropriate level of allowance for loan losses. Based on its comprehensive analysis, management deemed the allowance for loan losses of \$4.53 million at June 30, 2007 (0.90% of loans receivable and 461% of non-performing loans) adequate to provide for probable losses based on an evaluation of known and inherent risks in the loan portfolio at that date. The allowance for loan losses was \$4.12 million (1.03% of loans receivable and 213% of non-performing loans) at June 30, 2006. The Company had a net charge-off of \$3,000 for the quarter June 30, 2007 and net recovery of \$1,000 for the quarter ended June 30, 2006. The Company had a net charge-off of \$9,000 for nine months ended June 30,

2007 and a net recovery of \$21,000 for the nine months ended June 30, 2006.

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For additional information, see the section entitled "Activity in the Allowance for Loan Losses" included herein.

Non-interest Income: Total non-interest income decreased by \$27,000 to \$1.50 million for the quarter ended June 30, 2007 from \$1.53 million for the quarter ended June 30, 2006, primarily as a result of a decrease in service charges on deposits and a decrease in fee income from the sale of non-deposit investment products. These decreases were partially offset by increased servicing income on loans sold, increased gains on sale of loans, and increased ATM transaction fees.

Total non-interest income decreased by \$187,000 to \$4.41 million for the nine months ended June 30, 2007 from \$4.59 million for the nine months ended June 30, 2006, primarily as a result of a decrease in services charges on deposits and a decrease in fee income from the sale of non-deposit investment products. The decrease in service charges on deposits was primarily a result of fewer overdrafts on checking accounts. The reduction in non-deposit investment sale fee income was a result of decreased sales volume. These decreases were partially offset by increased servicing income on loans sold and increased ATM transaction fees.

Non-interest Expense: Total non-interest expense decreased by \$30,000 to \$4.76 million for the quarter ended June 30, 2007 from \$4.79 million for the quarter ended June 30, 2006. The decrease was primarily attributable to a \$59,000 gain on the sale of a land parcel that was recorded in the premises and equipment expense category. The Company's efficiency ratio improved to 58.35% for the quarter ended June 30, 2007 from 61.30% for the quarter ended June 30, 2006.

Total non-interest expense increased by \$449,000 or 3.2% to \$14.60 million for the nine months ended June 30, 2007 from \$14.15 million for the nine months ended June 30, 2006. The increase was primarily a result of a \$208,000 increase in salary expense, a \$68,000 increase in advertising expense, a \$55,000 increase in ATM expense and smaller increases in several other categories. The Company's efficiency ratio improved to 61.26% for the nine months ended June 30, 2007 from 61.59% for the nine months ended June 30, 2006.

Provision for Income Taxes: The provision for income taxes increased to \$1.00 million for the quarter ended June 30, 2007 from \$964,000 for the quarter ended June 30, 2006 primarily as a result of higher income before taxes. The Company's effective tax rate was 31.87% for the quarters ended June 30, 2007 and June 30, 2006.

The provision for income taxes was \$2.81 million for the nine months ended June 30, 2007 and the nine months ended June 30, 2006. The Company's effective tax rate was 31.83% for the nine months ended June 30, 2007 and 31.84% for the nine months ended June 30, 2006.

### Liquidity and Capital Resources

-----  
The Company's primary sources of funds are customer deposits, proceeds from principal and interest payments on loans and mortgage-backed securities, proceeds from the sale of loans, proceeds from maturing securities, FHLB advances, and other borrowings. While maturities and the scheduled amortization of loans are a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition.

An analysis of liquidity should include a review of the Condensed Consolidated Statement of Cash Flows for the nine months ended June 30, 2007. The statement of cash flows includes operating, investing and financing

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categories. Operating activities include net income, which is adjusted for non-cash items, and increases or decreases in cash due to changes in assets and liabilities. Investing activities consist primarily of proceeds from maturities and sales of securities, purchases of securities, and the net change in loans. Financing activities present the cash flows associated with the Company's deposit accounts, other borrowings and stock related transactions.

25

The Company's total cash equivalents decreased by \$9.60 million to \$13.19 million at June 30, 2007 from \$22.79 million at September 30, 2006. The Company's decreased liquid assets were primarily a result of funding loan growth.

The Bank must maintain an adequate level of liquidity to ensure the availability of sufficient funds for loan originations and deposit withdrawals, to satisfy other financial commitments and to take advantage of investment opportunities. The Bank generally maintains sufficient cash and short-term investments to meet short-term liquidity needs. At June 30, 2007, the Bank's regulatory liquidity ratio (net cash, and short-term and marketable assets, as a percentage of net deposits and short-term liabilities) was 8.95%. The Bank maintained an uncommitted credit facility with the FHLB of Seattle that provided for immediately available advances up to an aggregate amount of \$181.20 million, under which \$112.46 million was outstanding at June 30, 2007. The Bank also has a \$10.00 million overnight credit line with Pacific Coast Banker's Bank. At June 30, 2007, the Bank did not have any outstanding advances on this credit line.

Liquidity management is both a short and long-term responsibility of the Bank's management. The Bank adjusts its investments in liquid assets based upon management's assessment of (i) expected loan demand, (ii) projected loan sales, (iii) expected deposit flows, and (iv) yields available on interest-bearing deposits. Excess liquidity is invested generally in interest-bearing overnight deposits, federal funds sold, and other short-term investments. If the Bank requires funds that exceed its ability to generate them internally, it has additional borrowing capacity with the FHLB and Pacific Coast Banker's Bank.

The Bank's primary investing activity is the origination of one- to four-family mortgage loans, commercial mortgage loans, construction and land development loans, land loans, consumer loans, and commercial business loans. At June 30, 2007, the Bank had loan commitments totaling \$43.30 million and undisbursed loans in process totaling \$66.60 million. The Bank anticipates that it will have sufficient funds available to meet current loan commitments. Certificates of deposit that are scheduled to mature in less than one year from June 30, 2007 totaled \$170.45 million. Historically, the Bank has been able to retain a significant amount of its certificates of deposit as they mature.

Federally-insured state-chartered banks are required to maintain minimum levels of regulatory capital. Under current FDIC regulations, insured state-chartered banks generally must maintain (i) a ratio of Tier 1 leverage capital to total assets of at least 3.0% (4.0% to 5.0% for all but the most highly rated banks), (ii) a ratio of Tier 1 capital to risk weighted assets of at least 4.0% and (iii) a ratio of total capital to risk weighted assets of at least 8.0%. At June 30, 2007, the Bank was in compliance with all applicable capital requirements. For additional details see the section below entitled "Regulatory Capital."

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Regulatory Capital

The following table compares the Bank's regulatory capital at June 30, 2007 to its minimum regulatory capital requirements at that date (Dollars in thousands):

|  | Amount   | Percent of<br>Adjusted Total Assets (1) |
|--|----------|---|
|  | -----    | -----                                   |
| Tier 1 (leverage) capital                | \$59,101 | 9.69%                                   |
| Tier 1 (leverage) capital requirement    | 24,409   | 4.00                                    |
|  | -----    | -----                                   |
| Excess                                   | \$34,692 | 5.69%                                   |
|  | =====    | =====                                   |
| <br>                                     |          |   |
| Tier 1 risk adjusted capital             | \$59,101 | 11.60%                                  |
| Tier 1 risk adjusted capital requirement | 20,380   | 4.00                                    |
|  | -----    | -----                                   |
| Excess                                   | \$38,721 | 7.60%                                   |
|  | =====    | =====                                   |

26

|                                      |          |        |
|--------------------------------------|----------|--------|
| Total risk based capital             | \$63,630 | 12.49% |
| Total risk based capital requirement | 40,761   | 8.00   |
|                                      | -----    | -----  |
| Excess                               | \$22,869 | 4.49%  |
|                                      | =====    | =====  |

(1) For the Tier 1 (leverage) capital, percent of total average assets calculation, total average of assets were \$610.22 million. For the Tier 1 risk-based capital and total risk-based capital calculations, total risk-weighted assets were \$509.51 million.

27

TIMBERLAND BANCORP, INC. AND SUBSIDIARIES  
KEY FINANCIAL RATIOS AND DATA  
(Dollars in thousands, except per share data)

| Three Months Ended |      | Nine Months Ended |      |
|--------------------|------|-------------------|------|
| June 30,           |      | June 30,          |      |
| 2007               | 2006 | 2007              | 2006 |
| -----              |      | -----             |      |

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PERFORMANCE RATIOS:

|                              |        |        |        |        |
|------------------------------|--------|--------|--------|--------|
| Return on average assets (1) | 1.38%  | 1.49%  | 1.34%  | 1.45%  |
| Return on average equity (1) | 11.24% | 10.57% | 10.36% | 10.48% |
| Net interest margin (1)      | 4.67%  | 5.00%  | 4.72%  | 4.90%  |
| Efficiency ratio             | 58.35% | 61.30% | 61.26% | 61.59% |

|  | At<br>June 30,<br>2007 | At<br>September 30,<br>2006 |
|--|------------------------|-----------------------------|
| -----  |                        |                             |
| ASSET QUALITY RATIOS:                                |                        |                             |
| Non-performing loans                                 | \$ 982                 | \$ 80                       |
| OREO and other repossessed assets                    | 68                     | 15                          |
| -----  |                        |                             |
| Total non-performing assets                          | \$1,050                | \$ 95                       |
| Non-performing assets to total assets                | 0.17%                  | 0.02%                       |
| Allowance for loan losses to<br>non-performing loans | 461%                   | 5,153%                      |
|  |                        |                             |
| Book value per share (2)                             | \$10.53                | \$10.56                     |
| Book value per share (3)                             | \$11.19                | \$11.22                     |
| Tangible book value per share (2) (4)                | \$ 9.54                | \$ 9.61                     |
| Tangible book value per share (3) (4)                | \$10.14                | \$10.21                     |

- 
- (1) Annualized  
(2) Calculation includes ESOP shares not committed to be released  
(3) Calculation excludes ESOP shares not committed to be released  
(4) Calculation subtracts goodwill and core deposit intangible from the equity component

|   | Three Months Ended<br>June 30, |           | Nine Months Ended<br>June 30, |           |
|---|--------------------------------|-----------|-------------------------------|-----------|
|   | 2007                           | 2006      | 2007                          | 2006      |
| -----   |                                |           |                               |           |
| AVERAGE BALANCE SHEET:                        |                                |           |                               |           |
| -----   |                                |           |                               |           |
| Average total loans                           | \$494,137                      | \$399,849 | \$466,200                     | \$396,141 |
| Average total interest<br>earning assets      | 570,597                        | 502,804   | 548,942                       | 499,624   |
| Average total assets                          | 619,120                        | 554,716   | 598,688                       | 552,100   |
| Average total interest bearing<br>deposits    | 388,610                        | 366,228   | 381,946                       | 363,246   |
| Average FHLB advances and<br>other borrowings | 98,467                         | 55,597    | 82,139                        | 58,218    |
| Average shareholders' equity                  | 76,087                         | 77,969    | 77,364                        | 76,478    |

28

Item 3. Quantitative and Qualitative Disclosures About Market Risk

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There were no material changes in information concerning market risk from the information provided in the Company's Form 10-K for the fiscal year ended September 30, 2006.

Item 4. Controls and Procedures

- 
- (a) Evaluation of Disclosure Controls and Procedures: An evaluation of the  
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Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) was carried out under the supervision and with the participation of the Company's Chief Executive Officer, Chief Financial Officer and several other members of the Company's senior management as of the end of the period covered by this report. The Company's Chief Executive Officer and Chief Financial Officer concluded that as of June 30, 2007 the Company's disclosure controls and procedures were effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.
- (b) Changes in Internal Controls: There have been no changes in our internal  
-----  
control over financial reporting (as defined in 13a-15(f) of the Exchange Act) that occurred during the quarter ended June 30, 2007, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. The Company continued, however, to implement suggestions from its internal auditor and independent auditors to strengthen existing controls. The Company does not expect that its disclosure controls and procedures and internal controls over financial reporting will prevent all error and fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns in controls or procedures can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; as over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings  
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Neither the Company nor the Bank is a party to any material legal proceedings at this time. Further, neither the Company nor the Bank is aware of the threat of any such proceedings. From time to time, the Bank is involved in various claims and legal actions arising in the ordinary course of business.

Item 1A. Risk Factors  
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There have been no material changes in the Risk Factors previously disclosed

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in Item 1A of the Company's 2006 Form 10-K.

29

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

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Not applicable

#### Stock Repurchases

The following table sets forth the shares repurchased by the Company during the quarter ended June 30, 2007:

| Period                     | Total<br>No. of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total No.<br>of Shares<br>Purchased as<br>Part of<br>Publicly<br>Announced<br>Plan (1) (2) | Maximum No.<br>of Shares that<br>May Yet Be<br>Purchased Under<br>the Plan(1) (2) |
|----------------------------|--|------------------------------------|--|---|
| 04/01/2007 -<br>04/30/2007 | 50,000                                 | \$17.74                            | 50,000   | 120,532   |
| 05/01/2007 -<br>05/31/2007 | 170,532                                | 17.90                              | 170,532  | 306,950   |
| 06/01/2007 -<br>06/30/2007 | 90,000                                 | 18.41                              | 90,000   | 216,950   |
| <b>Total</b>               | <b>310,532</b>                         | <b>\$18.02</b>                     | <b>310,532</b>   |   |

(1) On May 7, 2007, the Company completed its previously announced share repurchase program. The Company repurchased 5% of its outstanding common shares or 372,532 shares, at an average price of \$18.23 per share. All shares were repurchased through open market broker transactions and no shares were directly repurchased from directors or officers of the Company.

(2) On May 25, 2007, the Company announced a share repurchase plan authorizing the repurchase of up to 5% of its outstanding shares, or 356,950 shares. As of June 30, 2007, a total of 140,000 shares had been repurchased at an average price of \$18.09 per share. All shares were repurchased through open market broker transactions and no shares were directly repurchased from directors or officers of the Company.

### Item 3. Defaults Upon Senior Securities

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None to be reported.

### Item 4. Submission of Matters to a Vote of Security Holders

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None to be reported



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Item 5. Other Information

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None to be reported.

30

Item 6. Exhibits

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- (a) Exhibits
    - 3.1 Articles of Incorporation of the Registrant (1)
    - 3.2 Bylaws of the Registrant (1)
    - 3.3 Amendment to Bylaws (2)
    - 10.1 Employee Severance Compensation Plan, as revised (3)
    - 10.2 Employee Stock Ownership Plan (3)
    - 10.3 1999 Stock Option Plan (4)
    - 10.4 Management Recognition and Development Plan (4)
    - 10.5 2003 Stock Option Plan (5)
    - 10.6 Form of Incentive Stock Option Agreement (6)
    - 10.7 Form of Non-qualified Stock Option Agreement (6)
    - 10.8 Form of Management Recognition and Development Award Agreement (6)
    - 10.9 Employment Agreement between the Company and the Bank and Michael R. Sand (7)
    - 10.10 Employment Agreement between the Company and the Bank and Dean J. Brydon (7)
    - 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes Oxley Act
    - 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes Oxley Act
    - 32 Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes Oxley Act

- 
- (1) Incorporated by reference to the Registrant's Registration Statement of Form S-1 (333- 35817).
  - (2) Incorporated by reference to the Registrant's Annual Report on Form 10-K for the year ended September 30, 2002.
  - (3) Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 1997; and to the Registrant's Current Report on Form 8-K dated April 13, 2007.
  - (4) Incorporated by reference to the Registrant's 1999 Annual Meeting Proxy Statement dated December 15, 1998.
  - (5) Incorporated by reference to the Registrant's 2004 Annual Meeting Proxy Statement dated December 24, 2003.
  - (6) Incorporated by reference to the Registrant's Annual Report on Form 10-K for the year ended September 30, 2005.
  - (7) Incorporated by reference to the Registrant's Current Report on Form 8-K dated April 13, 2007.

31

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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.

Timberland Bancorp, Inc.

Date: August 7, 2007

By:/s/Michael R. Sand

-----  
Michael R. Sand  
Chief Executive Officer  
(Principal Executive Officer)

Date: August 7, 2007

By:/s/Dean J. Brydon

-----  
Dean J. Brydon  
Chief Financial Officer  
(Principal Financial Officer)

32

EXHIBIT INDEX

| Exhibit No. | Description of Exhibit   |
|-------------|--|
| 31.1        | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act |
| 31.2        | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act |
| 32          | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act                            |

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

I, Michael R. Sand, certify that:

1. I have reviewed this Form 10-Q of Timberland Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

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(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 7, 2007

/s/Michael R. Sand

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Michael R. Sand  
Chief Executive Officer

34

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

I, Dean J. Brydon, certify that:

1. I have reviewed this Form 10-Q of Timberland Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others

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within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 7, 2007

/s/Dean J. Brydon

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Dean J. Brydon  
Chief Financial Officer

35

EXHIBIT 32

Certification Pursuant to Section 906 of the Sarbanes Oxley Act

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER  
OF TIMBERLAND BANCORP, INC.  
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350), each of the undersigned hereby certifies in his capacity as an

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officer of Timberland Bancorp, Inc. (the "Company") and in connection with the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2007 ("Report"), that:

- \* the Report fully complies with the requirements of Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, and
- \* the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods presented in the financial statements included in the Report.

/s/Michael R. Sand

/s/Dean J. Brydon

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Michael R. Sand  
Chief Executive Officer

-----  
Dean J. Brydon  
Chief Financial Officer

Date: August 7, 2007