WASHINGTON FEDERAL INC
Form 10-K
November 02, 2009

United States

Securities and Exchange Commission

Washington, D.C. 20549

FORM 10-K

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

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2009.

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: 0-25454

Washington Federal, Inc.

(Exact name of registrant as specified in its charter)

Washington	**91-1661606**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

425 Pike Street, Seattle, Washington 98101

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (206) 624-7930

Securities registered pursuant to Section 12(b) of the Act:

Title of each class NA Name of each exchange on which registered NA

Securities registered pursuant to section 12(g) of the Act:

Common Stock, $1.00 par value per share (title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceeding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

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

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

As of March 31, 2009, the aggregate market value of the 87,343,442 shares of Common Stock of the Registrant issued and outstanding on such date, which excludes 703,996 shares held by all directors and executive officers of the Registrant as a group, was $1,160,794,344. This figure is based on the closing sale price of $13.29 per share of the Registrant s Common Stock on March 31, 2009, as reported by Bloomberg.

Number of shares of Common Stock outstanding as of October 30, 2009: 112,270,330

DOCUMENTS INCORPORATED BY REFERENCE

List hereunder the following documents incorporated by reference and the Part of Form 10-K into which the document is incorporated:

(1) Portions of the Registrant s Annual Report to Stockholders for the fiscal year ended September 30, 2009, are incorporated into Part II, Items 5-8 and Part III, Item 12 of this Form 10-K.

(2) Portions of the Registrant s definitive proxy statement for its Annual Meeting of Stockholders to be held on January 20, 2010 are incorporated into Part III, Items 10-14 of this Form 10-K.

PART I

In addition to historical information, this Annual Report on Form 10-K includes certain forward-looking statements, as defined in the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, based on current management expectations. Actual results could differ materially from those management expects. Such forward-looking statements include statements regarding Washington Federal s intentions, beliefs or current expectations as well as the assumptions on which such statements are based. Stockholders and potential stockholders are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those contemplated by such forward-looking statements. Factors that could cause future results to vary from current management expectations include, but are not limited to: general economic conditions; legislative and regulatory changes; monetary fiscal policies of the federal government; changes in tax policies; rates and regulations of federal, state and local tax authorities; changes in interest rates; deposit flows; cost of funds; demand for loan products; demand for financial services; competition; changes in the quality or composition of the Company s loan and investment portfolios; changes in accounting principles; policies or guidelines and other economic, competitive, governmental and technological factors affecting Washington Federal s operations, markets, products services and fees. Washington Federal undertakes no obligation to update or revise any forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time.

Item 1. Business

General

Washington Federal, Inc., formed in November 1994, is a Washington corporation headquartered in Seattle, Washington. The Company is a non-diversified unitary savings and loan holding company within the meaning of the Home Owners Loan Act (HOLA) that conducts its operations through a federally insured savings and loan association subsidiary, Washington Federal Savings. As used throughout this report, the terms Washington Federal or the Company refer to Washington Federal, Inc. and its consolidated subsidiaries.

The Company, doing business as Washington Federal Savings, is a federally-chartered savings and loan association that began operations in Washington as a state-chartered mutual company in 1917. In 1935, the Company converted to a federal charter and became a member of the Federal Home Loan Bank (FHLB) system. On November 9, 1982, Washington Federal Savings converted from a federal mutual to a federal capital stock company.

The Company s fiscal year end is September 30th. All references to 2009, 2008 and 2007 represent balances as of September 30, 2009, September 30, 2008 and September 30, 2007, or activity for the fiscal years then ended, respectively.

The business of Washington Federal consists primarily of attracting deposits from the general public and investing these funds in loans of various types, including first lien mortgages on single-family dwellings, construction loans, land acquisition and development loans, loans on multi-family and other income producing properties, home equity loans and business loans. It also invests in certain United States government and agency obligations and other investments permitted by applicable laws and regulations. Washington Federal has 150 full service branches located in Washington, Oregon, Idaho, Arizona, Utah, Nevada, New Mexico and Texas. Through its subsidiaries, the Company is engaged in real estate investment and insurance brokerage activities.

The principal sources of funds for the Company s activities are retained earnings, loan repayments (including prepayments), net deposit inflows, repayments and sales of investments and borrowings. Washington Federal s principal sources of revenue are interest on loans, interest and dividends on investments. Its principal expenses are interest paid on deposits, credit costs, general and administrative expenses, interest on borrowings and income taxes.

The Company s growth has been generated both internally and as a result of 14 mergers and four assumptions of deposits completed in the Company s history. In February 2008, the Company completed its acquisition of First Mutual Bancshares, Inc. First Mutual Bancshares was the holding company for First Mutual Bank, a Washington-chartered savings bank, headquartered in Bellevue, Washington.

The Company is subject to extensive regulation, supervision and examination by the Office of Thrift Supervision (OTS), as its chartering authority and primary federal regulator, and by the Federal Deposit Insurance Corporation (FDIC), which insures its deposits up to applicable limits. Such regulation and supervision establishes a comprehensive framework of activities in which an institution may engage and is intended primarily for the protection of the deposits and the Deposit Insurance Fund (DIF) administered by the FDIC. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities. Any change in such regulation, whether by the OTS, the FDIC or the U.S. Congress, could have a significant impact on the Company and its operations. See Regulation.

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Average Statements of Financial Condition

	Year Ended September 30,								
	2007			2008			2009		
	Average Balance	Interest	Average Rate	Average Balance	Interest (In thousands)	Average Rate	Average Balance	Interest	Average Rate
Assets									
Loans (1)	$ 7,634,825	$ 526,923	6.90%	$ 9,013,671	$ 599,878	6.66%	$ 9,422,953	$ 579,244	6.15%
Mortgage-backed securities	1,354,689	75,478	5.57	1,565,590	88,425	5.65	1,974,954	109,486	5.54
Investment securities (2)	264,345	15,525	5.87	214,871	11,408	5.31	212,490	2,634	1.24
FHLB stock	131,663	756	0.57	140,569	1,717	1.22	144,522	410	.28
Total interest-earning assets	9,385,522	618,682	6.59	10,934,701	701,428	6.41	11,754,919	691,774	5.88
Other assets	272,300			381,090			499,324		
Total assets	$ 9,657,822			$ 11,315,791			$ 12,254,243		
Liabilities and Stockholders Equity									
Checking accounts	$ 351,558	5,572	1.58%	$ 473,999	6,813	1.44%	494,152	3,144	.64%
Passbook and statement accounts	188,853	2,902	1.54	197,448	2,724	1.38	192,141	1,441	.75
Insured money market accounts	748,436	22,309	2.98	996,164	25,571	2.57	1,232,723	16,488	1.34
Certificate accounts (time deposits)	4,408,864	212,237	4.81	5,032,005	224,114	4.45	5,525,855	169,301	3.06
Repurchase agreements with customers	21,567	817	3.79	15,787	547	3.46	38,922	1,061	2.73
FHLB advances	1,623,864	78,033	4.81	2,022,596	94,048	4.65	2,243,242	94,804	4.23
Securities sold under agreements to repurchase	785,753	31,962	4.07	803,825	34,260	4.26	800,000	31,061	3.88
Federal funds purchased	87,939	4,669	5.31	296,529	9,564	3.23	191,989	1,327	.69
Total interest-bearing liabilities	8,216,834	358,501	4.36	9,838,353	397,641	4.04	10,719,024	318,627	2.97
Other liabilities	150,320			120,584			116,929		
Total liabilities	8,367,154			9,958,937			10,835,953		
Stockholders equity	1,290,668			1,356,854			1,418,290		
Total liabilities and stockholders equity	$ 9,657,822			$ 11,315,791			$ 12,254,243		
Net interest income/Interest rate spread		$ 260,181	2.23%		$ 303,787	2.37%		$ 373,147	2.91%
Net interest margin (3)			2.77%			2.78%			3.17%

(1)

The average balance of loans includes nonaccruing loans, interest on which is recognized on a cash basis. It also includes net accretion of deferred loan fees and costs of $18.1 million, $12.7 million and $11.5 million for years 2007, 2008 and 2009, respectively.

(2) Includes cash equivalents and repurchase agreements.

(3) Net interest income divided by average interest-earning assets.

Lending Activities

General. The Company s net portfolio of loans totaled $9.0 billion at September 30, 2009, representing approximately 71% of its total assets. The Company concentrates its lending activities on the origination of conventional mortgage loans, which are loans that are neither insured nor guaranteed by agencies of the United States government.

Washington Federal s lending activity is concentrated on the origination of loans secured by real estate, including long-term fixed-rate mortgage loans, adjustable-rate construction loans, adjustable-rate land development loans and fixed-rate multi-family loans.

The following table sets forth the composition of the Company s gross loan portfolio, by loan type, as of September 30 for the years indicated.

	2005		2006		2007		2008		2009	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
					(In thousands)					
Loans:										
Single-family residential	$ 4,630,411	70.3%	$ 5,416,501	70.3%	$ 6,067,194	69.4%	$ 6,868,956	69.5%	$ 6,785,723	72.3%
Construction speculative (2)	629,594	9.6	716,828	9.3	707,503	8.1	439,616	4.4	267,430	2.8
Construction custom (2)	391,825	5.9	373,534	4.9	328,929	3.8	317,894	3.2	258,839	2.8
Land acquisition and development (1)	317,132	4.8	517,969	6.7	755,577	8.6	724,421	7.3	519,130	5.5
Land consumer lot loans (1)	121,489	1.8	148,842	1.9	159,001	1.8	210,816	2.1	195,812	2.1
Multi-family	501,824	7.6	527,719	6.9	558,846	6.4	683,508	6.9	705,212	7.5
Commercial Real Estate					112,659	1.3	282,138	2.8	294,109	3.1
Commercial & Industrial					23,251	.3	151,844	1.5	119,019	1.3
HELOC					13,690	.2	80,407	.8	122,184	1.3
Consumer					10,377	.1	153,072	1.5	120,081	1.3
GROSS LOANS	$ 6,592,275	100.0%	$ 7,701,393	100.0%	$ 8,737,027	100.0%	$ 9,912,672	100.0%	$ 9,387,539	100.0%
Less LIP, Allowance and net def. costs & fees	(583,343)		(622,950)		(548,749)		(411,052)		(404,109)	
NET LOANS	$ 6,008,932		$ 7,078,443		$ 8,188,278		$ 9,501,620		$ 8,983,430	

(1) Represents loans to builders / intended occupants for the purpose of financing the acquisition and development of single-family residences.
(2) Represents loans to builders / intended occupants for the purpose of financing the construction of single-family or multi-family residences.

The following table summarizes the scheduled contractual gross loan maturities for the Company s total loan portfolio due for the periods indicated as of September 30, 2009. Amounts are presented prior to deduction of discounts, premiums, loans in process, deferred net loan origination fees and allowance for loan losses. Adjustable-rate loans are shown in the period in which loan principal payments are contractually due.

Contractual Maturities:

	Total	Less than 1 Year	1 to 5 Years	After 5 Years
		(In thousands)		
Single-family residential	$ 6,785,723	$ 100,684	$ 133,756	$ 6,551,283
Construction speculative	267,430	265,286	2,144	
Construction custom	258,839	3,871	2,768	252,200
Land acquisition and development	519,130	468,851	22,362	27,917
Land consumer lot loans	195,812	5,684	28,482	161,646
Multi-family	705,212	49,054	287,012	369,146
Commercial Real Estate	294,109	27,705	114,444	151,960
Commercial & Industrial	119,019	55,315	47,598	16,106
HELOC	122,184	1,585	2,225	118,374
Consumer	120,081	687	15,335	104,059
	$ 9,387,539	$ 978,722	$ 656,126	$ 7,752,691
Loans maturing after one year:				
Adjustable-rate	$ 920,024			
Fixed-rate	7,488,793			
Total	$ 8,408,817			

The original contractual loan payment period for residential mortgage loans originated by the Company normally ranges from 15 to 30 years. Experience during recent years has indicated that, because of prepayments in connection with refinancing and sales of property, residential loans remain outstanding an average of less than eight and one half years.

Lending Programs and Policies. The Company s principal lending activity is the origination of real estate mortgage loans to purchase or refinance single-family residences. The Company also originates a significant number of construction and land development loans, along with multi-family residential and commercial loans. At September 30, 2009, single-family residential loans totaled $6.8 billion, or 72.3% of the Company s gross loan portfolio; construction-speculative loans totaled $267 million, or 2.8% of the Company s gross loan portfolio; construction custom loans totaled $259 million, or 2.8% of the Company s gross loan portfolio; land acquisition and development loans totaled $519 million, or 5.5% of the Company s gross loan portfolio; land consumer lot loans totaled $196 million, or 2.1% of the Company s gross loan portfolio; multi-family loans totaled $705 million, or 7.5% of the Company s gross loan portfolio; commercial real estate loans totaled $294 million, or 3.1% of the Company s gross loan portfolio; commercial and industrial loans totaled $119 million, or 1.3% of the Company s gross loan portfolio; HELOC loans totaled $122 million, or 1.3% of the Company s gross loan portfolio and consumer loans totaled $120 million, or 1.3% of the Company s gross loan portfolio.

Single-family residential loans. The Company primarily originates 30 year fixed-rate loans secured by single-family residences. Generally, these loans are made on terms, conditions and documentation that permit sale in the secondary market. Moreover, it is the Company s general policy to include in the documentation evidencing its conventional mortgage loans a due-on-sale clause, which facilitates adjustment of interest rates on such loans when the property securing the loan is sold or transferred.

All of the Company s mortgage lending is subject to written, nondiscriminatory underwriting standards, loan origination procedures and lending policies prescribed by the Company s Board of Directors. Property valuations are required on all real estate loans. Appraisals are prepared by independent appraisers approved by the Company s management, and reviewed by the Company s staff. Property evaluations are sometimes utilized in lieu of an appraisal on single-family real estate loans of $250,000 or less and are prepared by the Company s staff. Detailed loan applications are obtained to determine the borrower s ability to repay and the more significant items on these applications are verified through the use of credit reports, financial statements or written confirmations. Depending on the size of the loan involved, a varying number of officers of the Company must approve the application before the loan can be granted.

Federal guidelines limit the amount of a real estate loan made by a federally-chartered savings institution, such as Washington Federal Savings, to a specified percentage of the value of the property securing the loan as determined by an evaluation at the time the loan is originated, referred to as the loan-to-value ratio. The guidelines provide that at the time of origination a real estate loan may not exceed 100% of the value of the security property. Maximum loan-to-value ratios for each type of real estate loan are established by the Company s Board of Directors. When establishing general reserves for loans with loan-to-value ratios exceeding 80% that are not insured by private mortgage insurance, Washington Federal considers the additional risk inherent with these products, as well as their relative loan loss experience, and provides reserves when deemed appropriate. The total balance for loans with loan-to-value ratios exceeding 80% at September 30, 2009, was $556 million, with allocated reserves of $2.8 million.

Construction loans. The Company originates construction loans to finance construction of single-family and multi-family residences as well as commercial properties. These loans to builders are generally indexed to the Prime rate and normally have maturities of two years or less. Loans made to individuals for construction of their home generally are 30 year fixed rate loans. The Company s policies provide that construction loans may be made for 80% or less of the appraised value of the property upon completion for residential construction loans. As a result of activity over the past three decades, the Company believes that it is a construction lender of choice by builders of single-family residences in its market areas. Because of this history, the Company has developed a staff with in depth land development and construction experience and working relationships builders that have been selected based on their operating histories and financial stability.

Construction lending involves a higher level of risk than single-family residential lending due to the concentration of principal in a limited number of loans and borrowers, as well as the effects of general economic conditions in the homebuilding industry. Moreover, a construction loan can involve additional risks because of the inherent difficulty in estimating both a property s value at completion of the project and the estimated cost (including interest) of the project. These loans are generally more difficult to evaluate and monitor.

Land loans. The Company s land development loans are of a short-term nature and are generally made for 75% or less of the appraised value of the property. Funds are disbursed periodically at various stages of completion as authorized by the Company s personnel. The interest rate on these loans generally adjusts every 90 days in accordance with a designated index.

Land development loans involve a higher degree of credit risk than long-term financing on owner-occupied real estate. Mitigation of risk of loss on a land development loan is dependent largely upon the accuracy of the initial estimate of the property s value at completion of development compared to the estimated cost (including interest) of development and the financial strength of the borrower.

The Company s permanent land loans (also called consumer lot loans) are generally made on improved land, with the intent of building a primary or secondary residence. These loans are limited to 80% or less of the appraised value of the property, up to a maximum loan amount of $350,000. The interest rate on permanent land loans is generally fixed for 20 years.

Multi-family residential loans. Multi-family residential (five or more dwelling units) loans generally are secured by multi-family rental properties, such as apartment buildings. In underwriting multi-family residential loans, the Company considers a number of factors, which include the projected net cash flow to the loan s debt service requirement, the age and condition of the collateral, the financial resources and income level of the borrower and the borrower s experience in owning or managing similar properties. Multi-family residential loans are originated in amounts up to 75% of the appraised value of the property securing the loan.

Loans secured by multi-family residential real estate generally involve a greater degree of credit risk than single-family residential loans and carry larger loan balances. This increased credit risk is a result of several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income-producing properties, and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by multi-family mortgages typically depends upon the successful operation of the related real estate property. If the cash flow from the project is reduced, the borrower s ability to repay the loan may be impaired. The Company seeks to minimize these risks through its underwriting policies, which require such loans to be qualified at origination on the basis of the property s income and debt service ratio. The Company generally limits its multi-family residential loans to $5.0 million on any one loan.

It is the Company s policy to obtain title insurance ensuring that the Company has a valid first lien on the mortgaged real estate serving as collateral. Borrowers must also obtain hazard insurance prior to closing and, when required by regulation, flood insurance. Borrowers may be required to advance funds on a monthly basis, together with each payment of principal and interest, to a mortgage escrow account from which the Company makes disbursements for items such as real estate taxes, hazard insurance premiums and private mortgage insurance premiums when due.

Commercial and industrial loans. The Company generally makes various types of secured owner occupied commercial real estate and business loans to customers in its market area for the purposes of acquiring real estate, equipment or other business purposes. The terms of these loans generally range from less than one year to a maximum of ten years. The loans are either negotiated on a fixed-rate basis or carry adjustable interest rates indexed to Prime or another market rate.

Commercial credit decisions are based upon the Company s assessment of the borrower s ability and willingness to repay along with an evaluation of the liquidity and marketability of collateral. Most such loans are extended to closely held businesses and the personal guaranty of the principals are usually obtained. Non real estate commercial loans have a relatively high risk of default, compared to residential real estate loans. Pricing of commercial loans is based on the credit risk of the borrower and the adequacy of collateral, with consideration given to the overall relationship of the borrower, including deposits. The acquisition of business deposits is an important focus of this business line. The cost of funds from businesses is usually lower than the cost of funds raised through CDs in our retail branches.

Consumer loans. Through its two most recent acquisitions, the Company obtained its portfolio of $120 million of consumer loans. These loans are primarily home improvement loans made through third party originators that bear interest rates of 10% and higher. Due to the nature of these loans the average charge off rate has been 3 to 5% per year. After extensive review of this program, the Company decided in fiscal 2008 to cease origination of consumer loans, as the risk profile did not match with the Company s long term business plan. The Company will continue to service the portfolio until the balances are repaid.

Home equity loans. The company makes revolving line of credit loans to consumers that are secured by a first or second mortgage on a single family residence. The interest rates on these loans adjust monthly indexed to Prime. Loan-to-value rates is limited to 75%. Terms are a ten year draw period followed by a fifteen year amortization period

Origination and Purchase of Loans. The Company has general authority to lend anywhere in the United States; however, the primary lending areas are within the states of Washington, Oregon, Idaho, Arizona, Utah, Nevada, New Mexico and Texas.

Loan originations come from a number of sources. Residential loan originations result from referrals from real estate brokers, walk-in customers, purchasers of property in connection with builder projects financed by the Company, mortgage brokers and refinancings for existing customers. Construction loan originations are obtained primarily by direct solicitation of builders and continued business from builders who have previously borrowed from the Company.

The Company also purchases loans and mortgage-backed securities when lending rates and mortgage volume for new loan originations in its market area do not fulfill its needs. The table below shows total loan origination, purchase and repayment activities of the Company for the years indicated.

	2005	2006	2007 (In thousands)	2008	2009
Loans originated (1):					
Single-family residential	$ 787,455	$ 718,915	$ 827,270	$ 857,334	$ 855,212
Construction-speculative	716,569	704,314	518,024	218,145	102,630
Construction custom	422,100	385,084	337,575	303,844	262,952
Land Acquisition & Development	358,863	398,669	443,793	148,221	45,425
Land Consumer Lot Loans		59,869	42,299	25,909	14,681
Multi-family	151,839	135,496	98,453	105,805	97,621
Commercial Real Estate			16,266	66,876	117,447
Commercial & Industrial			10,320	187,748	243,240
HELOC			5,074	63,855	85,755
Consumer			2,871	96,438	15,497
Total loans originated	2,436,826	2,402,347	2,301,945	2,074,175	1,840,460
Loans purchased (2)	331,456	399,766	414,153	946, 826	385,645
Loan principal repayments	(1,769,058)	(1,694,530)	(1,718,798)	(1,845,324)	(2,116,355)
Net change in loans in process, discounts, etc.	(83,735)	(38,072)	112,535	137,665	(627,940)
Net loan activity increase (decrease)	$ 915,489	$ 1,069,511	$ 1,109,835	$ 1,313,342	$ (518,190)
Beginning balance	$ 5,093,443	$ 6,008,932	$ 7,078,443	$ 8,188,278	$ 9,501,620
Ending balance	$ 6,008,932	$ 7,078,443	$ 8,188,278	$ 9,501,620	$ 8,983,430

(1) Includes undisbursed loan in process and does not include savings account loans, which were not material during the periods indicated.
(2) Includes loans acquired through acquisitions and whole loan purchases.

Interest Rates, Loan Fees and Service Charges. Interest rates charged by the Company on mortgage loans are primarily determined by the competitive loan rates offered in its lending areas and in the secondary market. Mortgage loan rates reflect factors such as general interest rates, the supply of money available to the savings and loan industry and the demand for such loans. These factors are in turn affected by general economic conditions, the regulatory programs and policies of federal and state agencies, changes in tax laws and governmental budgetary programs.

The Company receives fees for originating loans in addition to various fees and charges related to existing loans, which may include prepayment charges, late charges and assumption fees.

In making one-to-four family home mortgage loans, the Company does not normally charge a commitment fee. As part of the loan application, the borrower pays the Company for out-of-pocket costs, such as the appraisal fee, in reviewing the application, whether or not the borrower closes the loan. The interest rate charged is normally the prevailing rate at the time the loan application is approved. In the case of construction loans, the Company normally charges an origination fee. Loan origination fees and other terms of multi-family residential loans are individually negotiated.

Nonperforming Assets. When a borrower fails to make a required payment on a loan, the Company attempts to cure the deficiency by contacting the borrower. Contact is made after a payment is 30 days past due. In most cases, deficiencies are cured promptly. If the delinquency is not cured within 90 days, the Company may institute appropriate action to foreclose on the property. If foreclosed, the property will be sold at a public sale and may be purchased by the Company. There are circumstances under which the Company may choose to foreclose a deed of trust as mortgagee, and when this procedure is followed, certain redemption rights are involved.

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

Loans are placed on nonaccrual status when, in the judgment of management, the probability of collection of interest is deemed to be insufficient to warrant further accrual. When a loan is placed on nonaccrual status, previously accrued but unpaid interest is deducted from interest income. The Company does not accrue interest on loans 90 days past due or more. See Note A to the Consolidated Financial Statements included in Item 8 hereof.

Real estate acquired by foreclosure or deed-in-lieu thereof (REO or Real Estate Owned) is either classified as real estate held for sale until it is sold or transferred to Real Estate Held for Investment(REHI). When property is acquired, it is recorded at the lower of carrying cost or fair value at the date of acquisition, and any writedown resulting therefrom is charged to the allowance for loan losses. Interest accrual ceases on the date of acquisition and all costs incurred in maintaining the property from that date forward are expensed as incurred. Costs incurred for the improvement or development of such property are capitalized. See Note A to the Consolidated Financial Statements included in Item 8 hereof.

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

	2005	2006	2007	2008	2009
			(In thousands)		
Restructured loans (1)	$ 573	$	$ 250	$ 6,210	$ 136,894
Nonaccrual loans:					
Single-family residential	5,765	5,700	9,820	38,017	116,268
Construction Speculative		1,002	2,446	33,003	50,348
Construction custom				1,315	
Land Acquisition & Development	403	126	1,809	51,562	187,061
Land consumer lot loans					
Multi-family	420	353	148	748	4,368
Commercial Real Estate			253	1,929	2,733
Commercial & Industrial			42		18,823
HELOC					
Consumer				535	656
Total nonaccrual loans (2)	6,588	7,181	14,518	127,109	380,257
Total REO (3)	756	479	1,413	37,082	120,105
Total REHI(4)					56,758
Total nonperforming assets	$ 7,344	$ 7,660	$ 15,931	$ 164,191	$ 557,120
Total nonperforming assets and restructured loans	$ 7,917	$ 7,660	$ 16,181	$ 170,401	$ 694,014
Total nonperforming assets and restructured loans as a percent of total assets	0.09%	0.08%	0.16%	1.44%	5.52%

(1) Performing in accordance with restructured terms.

(2) The Company recognized interest income on nonaccrual loans of approximately $326,000 in 2009. Had these loans performed according to their original contract terms, the Company would have recognized interest income of approximately $13,099,000 in 2009.

In addition to the nonaccrual loans reflected in the above table, at September 30, 2009, the Company had $305.9 million of loans that were less than 90 days delinquent but which were classified as substandard for one or more reasons. If these loans were deemed nonperforming, the Company s ratio of total nonperforming assets and restructured loans as a percent of total assets would have been 7.95% at September 30, 2009. For a discussion of the Company s policy for placing loans on nonaccrual status, see Note A to the Consolidated Financial Statements included in Item 8 hereof.

(3) Total REO includes real estate held for sale acquired in settlement of loans or acquired from purchased institutions in settlement of loans.

(4) Total REHI includes real estate held for investment acquired in settlement of loans.

The following table analyzes the Company s allowance for loan losses at the dates indicated.

	2005	2006	September 30, 2007 (In thousands)	2008	2009
Beginning balance	$ 25,140	$ 24,756	$ 24,993	$ 28,520	$ 85,058
Charge-offs:					
Single-Family Residential	154	226	40	2,177	18,013
Construction Speculative	90	20	1,024	6,858	22,604
Construction Custom					289
Land Acquisition & Development			58	3,513	50,552
Land Consumer Lot Loans				140	1,822
Multi-Family	14	52	34	25	1,028
Commercial Real Estate				225	
Commercial & Industrial Loans				14	11,573
HELOC					151
Consumer				2,471	6,841
	258	298	1,156	15,423	112,873
Recoveries:					
Single-Family Residential	8		1		117
Construction Speculative				34	8
Construction Custom					
Land Acquisition & Development					16
Land Consumer Lot Loans					
Multi-family					
Commercial Real Estate			2		
Commercial & Industrial Loans					948
HELOC					
Consumer				230	562
	8		3	264	1,651
Net charge-offs	250	298	1,153	15,159	111,222
Acquired through acquisition			3,130	11,181	
Provision (reversal of reserve) for loan losses	(134)	535	1,550	60,516	193,000
Ending balance	$ 24,756	$ 24,993	$ 28,520	$ 85,058	$ 166,836
Ratio of net charge-offs to average loans outstanding	.01%	.01%	.02%	.17%	1.18%

The following table sets forth the allocation of the Company s allowance for loan losses at the dates indicated.

	September 30,									
	2005		2006		2007		2008		2009	
	Amount	%(1)	Amount	%(1)	Amount	%(1)	Amount	%(1)	Amount	%(1)
					(In thousands)					
Allowance allocation:										
Single-family residential	$ 8,643	70.2%	$ 8,397	70.3%	$ 10,083	69.4%	$ 17,055	69.5%	$ 18,547	72.3%
Construction speculative	6,977	15.5	6,706	14.8	4,716	8.1	10,069	4.4	21,841	2.8
Construction custom					1,163	3.8	1,328	3.2	81	2.8
Land acquisition & development	3,360	6.7	4,829	8.0	4,506	8.6	28,679	7.3	104,569	5.5
Land consumer lot loans					1,136	1.8	2,279	2.1	1,298	2.1
Multi-family	5,776	7.6	5,061	6.9	5,299	6.4	4,514	6.9	1,878	7.5
Commercial real estate					1,297	1.3	4,536	2.8	1,344	3.1
Commercial & industrial					320	.3	3,807	1.5	7,327	1.3
HELOC						.2	1,338	0.8	377	1.3
Consumer						.1	11,453	1.5	9,574	1.3
Unallocated										
Total allowance for loan losses	$ 24,756		$ 24,993		$ 28,520		$ 85,058		$ 166,836	

(1) Represents the total amount of the loan category as a % of total loans outstanding.

The Company maintains an allowance for loan losses to absorb losses inherent in the loan portfolio. The allowance is based on ongoing, quarterly assessments of the probable and estimable losses inherent in the loan portfolio. The Company s methodology for assessing the appropriateness of the allowance consists of two components, which include the general allowance and specific allowance. As part of the process for determining the adequacy of the allowance for loan losses, management reviews the loan portfolio for specific weaknesses.

The general loan loss allowance is established by applying a loss percentage factor to the different loan types. The allowance is based on management s continuing evaluation of the pertinent factors underlying the quality of the loan portfolio, including changes in the size and composition of the loan portfolio, actual loan loss experience, current economic conditions, geographic concentrations, seasoning of the loan portfolio, specific industry conditions, and the duration of the current business cycle. The recovery of the carrying value of loans is susceptible to future market conditions beyond the Company s control, which may result in losses or recoveries differing from those provided. A portion of the allowance is then allocated to reflect the estimated loss exposure. Residential real estate loans are not individually analyzed for impairment and loss exposure because of the significant number of loans, their relatively small balances and their historically low level of losses. In determining the adequacy of reserves, management considers the above mentioned factors.

Specific allowances are established in cases where management has identified conditions or circumstances related to a loan that management believes indicate the probability that a loss has been incurred.

Investment Activities

As a federally-chartered savings institution, Washington Federal Savings is obligated to maintain adequate liquidity and does so by investing in securities. These investments may include, among other things, certain certificates of deposit, repurchase agreements, bankers acceptances, loans to financial institutions whose deposits are federally-insured, federal funds, United States government and agency obligations and mortgage-backed securities.

The following table sets forth the composition of the Company s investment portfolio at the dates indicated.

September 30,	**2007**		**2008**		**2009**	
	Amortized Cost	**Fair Value**	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**
			(In thousands)			
U.S. government and agency obligations	$ 236,352	$ 232,285	$ 37,253	$ 41,231	$ 9,800	$ 13,824
State and political subdivisions	8,107	8,646	7,770	8,306	7,435	7,980
Agency mortgage-backed securities	1,430,208	1,409,881	1,551,674	1,549,878	2,200,834	2,286,542
	$ 1,674,667	$ 1,650,812	$ 1,596,697	$ 1,599,415	$ 2,218,069	$ 2,308,346

The investment portfolio at September 30, 2009 was categorized by maturity as follows:

	Amortized Cost	**Wtd Avg Yield**
	(In thousands)	
Due in less than one year	$ 500	4.00%
Due after one year through five years	1,140	8.77
Due after five years through 10 years	9,300	10.38
Due after 10 years	2,207,129	5.76
	$ 2,218,069	5.78%

Sources of Funds

General. Deposits are the primary source of the Company s funds for use in lending and other general business purposes. In addition to deposits, Washington Federal derives funds from loan repayments, advances from the FHLB and other borrowings and, to a lesser extent, from investment repayments and sales. Loan repayments are a relatively stable source of funds, while deposit inflows and outflows are significantly influenced by general interest rates and money market conditions. Borrowings may be used on a short-term basis to compensate for reductions in normal sources of funds, such as deposit inflows at less than projected levels. Borrowings may also be used on a longer-term basis to support expanded activities.

Deposits. The Company chooses to rely on term certificate accounts and other deposit alternatives that have no fixed term and pay interest rates that are more responsive to market interest rates than passbook accounts. This greater variety of deposits allows the Company to be more competitive in obtaining funds and to more effectively manage its liabilities.

Certificates with a maturity of one year or less have penalties for premature withdrawal equal to 90 days of interest. When the maturity is greater than one year but less than four years, the penalty is 180 days of interest. When the maturity is greater than 4 years, the penalty is 365 days interest. Early withdrawal penalties during 2007, 2008 and 2009 amounted to approximately $1,005,000, $859,000 and $700,000, respectively.

The Company offers two checking account products; the accounts pay interest on monthly average balances over $1,000 and $10,000 respectively.

The Company s deposits are obtained primarily from residents of Washington, Oregon, Idaho, Arizona, Utah, Nevada, New Mexico and Texas. The Company does not advertise for deposits outside of these states.

The following table sets forth certain information relating to the Company s savings deposits at the dates indicated.

	September 30, 2007 Amount	2007 Rate	2008 Amount (In thousands)	2008 Rate	2009 Amount	2009 Rate
Balance by interest rate:						
Checking accounts	$ 409,098	1.90%	$ 516,972	1.14%	$ 526,321	.39%
Passbook and statement accounts	198,876	1.70	188,546	1.22	197,025	.50
Money market accounts	739,554	2.85	1,231,542	2.48	1,214,812	.87
	1,347,528		1,937,060		1,938,158	
Fixed-rate certificates:						
Under 2.00%			11,951		1,765,881	
2.00% to 2.99%	4,228		880,676		3,220,833	
3.00% to 3.99%	150,926		2,887,138		457,425	
4.00% to 4.99%	1,283,837		1,346,039		370,967	
5.00% to 5.99%	3,190,141		81,911		32,982	
6.00% and above	2,389		1,270		221	
	4,631,521		5,208,985		5,848,309	
	$ 5,979,049		$ 7,146,045		$ 7,786,467	

The following table sets forth, by various interest rate categories, the amount of certificates of deposit of the Company at September 30, 2009, which mature during the periods indicated.

	1 to 3 Months	4 to 6 Months	7 to 12 Months	Maturing in 13 to 24 Months (In thousands)	25 to 36 Months	37 to 60 Months	Total
Fixed-rate certificates:							
Under 2.00%	$ 440,453	$ 778,076	$ 486,149	$ 61,072	$	$ 131	$ 1,765,881
2.00% to 2.99%	2,192,151	139,110	287,882	545,159	45,671	10,860	3,220,833
3.00 to 3.99%	165,226	43,773	51,788	67,055	27,550	102,033	457,425
4.00 to 4.99%	52,926	32,220	48,300	62,480	77,325	97,716	370,967
5.00 to 5.99%	3,572	2,481	4,377	13,001	8,715	836	32,982
6.00 and above			219			2	221
Total	$ 2,854,328	$ 995,660	$ 878,715	$ 748,767	$ 159,261	$ 211,578	$ 5,848,309

Historically, a significant number of certificate holders roll over their balances into new certificates of the same term at the Company s then current rate. To ensure a continuity of this trend, the Company expects to continue to offer market rates of interest. Its ability to retain maturing deposits in certificate accounts is difficult to project; however, the Company is confident that by competitively pricing these certificates, levels deemed appropriate by management can be achieved on a continuing basis.

At September 30, 2009, the Company had $2.1 billion of certificates of deposit in amounts of $100,000 or more outstanding, maturing as follows: $1.1 billion within 3 months; $344 million over 3 months through 6 months; $311 million over 6 months through 12 months; and $414 million thereafter.

The following table sets forth the customer account and customer repurchase activities of the Company for the years indicated.

	September 30, 2007	September 30, 2008	September 30, 2009
	(In thousands)		
Deposits	$ 2,617,541	$ 8,846,229	$ 9,900,370
Acquired Deposits	379,090	744,182	
Withdrawals	(2,555,597)	(8,677,426)	(9,419,034)
Net increase in deposits before interest credited	441,034	912,985	481,336
Interest credited	244,025	259,769	191,435
Net increase in customer accounts	$ 685,059	$ 1,172,754	$ 672,771

Borrowings. The Company obtains advances from the FHLB upon the security of the FHLB capital stock it owns and certain of its home mortgages, provided certain standards related to credit worthiness have been met. See Regulation Washington Federal Savings Federal Home Loan Bank System below. Such advances are made pursuant to several different credit programs. Each credit program has its own interest rate and range of maturities, and the FHLB prescribes acceptable uses to which the advances pursuant to each program may be put, as well as limitations on the size of such advances. Depending on the program, such limitations are based either on a fixed percentage of assets or the Company s creditworthiness. The FHLB is required to review its credit limitations and standards at least annually. FHLB advances have, from time to time, been available to meet seasonal and other withdrawals of savings accounts and to expand Washington Federal s lending program. The Company had $2.1 billion of FHLB advances outstanding at September 30, 2009.

The Company also uses reverse repurchase agreements as a form of borrowing. Under reverse repurchase agreements, the Company sells an investment security to a dealer for a period of time and agrees to buy back that security at the end of the period and pay the dealer a stated interest rate for the use of the dealer s funds. The amount of securities sold under such agreements depends on many factors, including the terms available for such transactions, the perceived ability to apply the proceeds to investments yielding a higher return, the demand for the securities and management s perception of trends in interest rates. The Company had $800 million of securities sold under such agreements at September 30, 2009. See Note I to the Consolidated Financial Statements included in Item 8 hereof for additional information.

The Company may need to borrow funds for short periods of time to meet day-to-day financing needs. In these instances, funds are borrowed from other financial institutions for periods generally ranging from 1 to 7 days at the then current borrowing rate. At September 30, 2009, the Company had only $600,000 of such short-term borrowings.

The Company also offers two forms of repurchase agreements to its customers. One form has an interest rate that floats like a money market deposit account. The other form has a fixed rate and is offered in a minimum denomination of $100,000. Both forms are fully collateralized by securities. These obligations are not insured by FDIC and are classified as borrowings for regulatory purposes. The Company had $55.8 million of such agreements outstanding at September 30, 2009.

The following table presents certain information regarding borrowings of Washington Federal for the years indicated.

	2007	September 30, 2008 (In thousands)	2009
Federal funds and securities sold to dealers under agreements to repurchase:			
Average balance outstanding	$ 873,692	$ 1,100,354	$ 991,989
Maximum amount outstanding at any month-end during the period	1,175,000	1,275,000	1,040,600
Weighted-average interest rate during the period (1)	4.19%	3.98%	3.26%
FHLB advances:			
Average balance outstanding	$ 1,623,864	$ 2,022,596	$ 2,243,242
Maximum amount outstanding at any month-end during the period	1,800,000	2,206,000	2,743,026
Weighted-average interest rate during the period (1)	4.81%	4.65%	4.23%
Securities sold to customers under agreements to repurchase:			
Average balance outstanding	$ 21,567	$ 15,787	$ 38,922
Maximum amount outstanding at any month-end during the period	24,758	23,494	55,843
Weighted-average interest rate during the period (1)	3.79%	3.46%	2.73%
Total average borrowings	$ 2,519,123	$ 3,138,737	$ 3,274,153
Weighted-average interest rate on total average borrowings (1)	4.58%	4.41%	3.92%

(1) Interest expense divided by average daily balances.

Other Ratios

The following table sets forth certain ratios related to the Company for the periods indicated.

	2007	September 30, 2008	2009
Return on assets (1)	1.40%	.55%	.33%
Return on equity (2)	10.46	4.59	2.87
Average equity to average assets	13.36	11.99	11.57
Dividend payout ratio (3)	53.90	118.31	43.48

(1) Net income divided by average total assets.
(2) Net income divided by average equity.
(3) Dividends declared per share divided by net income per share.

Rate/Volume Analysis

The table below sets forth certain information regarding changes in interest income and interest expense of the Company for the years indicated. For each category of interest-earning asset and interest-bearing liability, information is provided on changes attributable to: (1) changes in volume (changes in volume multiplied by old rate) and (2) changes in rate (changes in rate multiplied by old average volume). The change in interest income and interest expense attributable to changes in both volume and rate has been allocated proportionately to the change due to volume and the change due to rate.

	September 30,								
	2007 vs. 2006			2008 vs. 2007			2009 vs. 2008		
	Increase (Decrease) Due to			Increase (Decrease) Due to			Increase (Decrease) Due to		
	Volume	Rate	Total	Volume	Rate	Total	Volume	Rate	Total
	(In thousands)			(In thousands)			(In thousands)		
Interest income:									
Loan portfolio	$ 76,942	$ 10,643	$ 87,585	$ 91,897	$ (18,942)	$ 72,955	$ 26,547	$ (47,181)	$ (20,634)
Mortgage-backed securities	6,772	1,768	8,540	11,854	1,093	12,947	22,807	(1,746)	21,061
Investments (1)	(9,296)	1,970	(7,326)	(1,580)	(1,576)	(3,156)	58	(10,139)	(10,081)
All interest-earning assets	74,418	14,381	88,799	102,171	(19,425)	82,746	49,412	(59,066)	(9,654)
Interest expense:									
Customer accounts	21,479	42,753	64,232	39,675	(23,743)	15,932	27,267	(95,601)	(68,334)
FHLB advances and other borrowings	20,073	835	20,908	27,844	(4,636)	23,208	4,792	(15,472)	(10,680)