

CATHAY GENERAL BANCORP

Form 10-Q

November 06, 2009

[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended 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 0-18630

CATHAY GENERAL BANCORP

(Exact name of registrant as specified in its charter)

Edgar Filing: CATHAY GENERAL BANCORP - Form 10-Q

Delaware (State of other jurisdiction of incorporation or organization)	95-4274680 (I.R.S. Employer Identification No.)
777 North Broadway, Los Angeles, California (Address of principal executive offices)	90012 (Zip Code)
Registrant's telephone number, including area code: (213) 625-4700	
(Former name, former address and former fiscal year, if changed since last report)	

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

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

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

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined 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.

Common stock, \$.01 par value, 61,829,540 shares outstanding as of October 31, 2009.

Table of Contents

CATHAY GENERAL BANCORP AND SUBSIDIARIES

3RD QUARTER 2009 REPORT ON FORM 10-Q

TABLE OF CONTENTS

<u>PART I FINANCIAL INFORMATION</u>	6
Item 1. <u>FINANCIAL STATEMENTS (Unaudited)</u>	6
<u>NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)</u>	9
Item 2. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	30
Item 3. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	57
Item 4. <u>CONTROLS AND PROCEDURES</u>	58
<u>PART II OTHER INFORMATION</u>	59
Item 1. <u>LEGAL PROCEEDINGS</u>	59
Item 1A. <u>RISK FACTORS</u>	59
Item 2. <u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	59
Item 3. <u>DEFAULTS UPON SENIOR SECURITIES</u>	60
Item 4. <u>SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS</u>	60
Item 5. <u>OTHER INFORMATION</u>	60
Item 6. <u>EXHIBITS</u>	60
<u>SIGNATURES</u>	61

Table of Contents

Forward-Looking Statements

In this quarterly Report on Form 10-Q, the term **Bancorp** refers to Cathay General Bancorp and the term **Bank** refers to Cathay Bank. The terms **Company**, **we**, **us**, and **our** refer to Bancorp and the Bank collectively. The statements in this report include forward-looking statements within the meaning of the applicable provisions of the Private Securities Litigation Reform Act of 1995 regarding management's beliefs, projections, and assumptions concerning future results and events. We intend such forward-looking statements to be covered by the safe harbor provision for forward-looking statements in these provisions. All statements other than statements of historical fact are forward-looking statements for purposes of federal and state securities laws, including statements about anticipated future operating and financial performance, financial position and liquidity, growth opportunities and growth rates, growth plans, acquisition and divestiture opportunities, business prospects, strategic alternatives, business strategies, financial expectations, regulatory and competitive outlook, investment and expenditure plans, financing needs and availability and other similar forecasts and statements of expectation and statements of assumptions underlying any of the foregoing. Words such as **aims**, **anticipates**, **believes**, **could**, **estimates**, **expects**, **hopes**, **intends**, **may**, **plans**, **projects**, **seeks**, **predicts**, **potential**, **continue**, and variations of these words and similar expressions are intended to identify these forward-looking statements. Forward-looking statements by us are based on estimates, beliefs, projections, and assumptions of management and are not guarantees of future performance. These forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. Such risks and uncertainties and other factors include, but are not limited to, adverse developments or conditions related to or arising from:

Risks relating to our business-

Difficult economic and market conditions have adversely affected our industry.

If current levels of market disruption and volatility continue or worsen, there can be no assurance that we will not experience an adverse effect, which may be material, on our ability to access capital and on our business, financial condition and results of operations.

We may be subject to supervisory action by bank supervisory authorities that could have a material negative effect on our business, financial condition and the value of our common stock.

U.S. and international financial markets and economic conditions could adversely affect our liquidity, results of operations, and financial condition.

We may be required to make additional provisions for loan losses and charge off additional loans in the future, which could adversely affect our results of operations.

We are subject to extensive laws and regulations and supervision that could limit or restrict our activities and adversely affect our profitability.

The allowance for credit losses is an estimate of probable credit losses. Actual credit losses in excess of the estimate could adversely affect our net income and capital.

We may experience goodwill impairment.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.

Our business is subject to interest rate risk and fluctuations in interest rates could reduce our net interest income and adversely affect our business.

We have engaged in and may continue to engage in further expansion through acquisitions, which could negatively affect our business and earnings.

Table of Contents

We may engage in FDIC-assisted transactions, which could present additional risks to our business.

Inflation and deflation may adversely affect our financial performance.

As we expand our business outside of California markets, we will encounter risks that could adversely affect us.

Our loan portfolio is largely secured by real estate, which has adversely affected and may continue to adversely affect our net income.

Our use of appraisals in deciding whether to make a loan on or secured by real property does not ensure the value of the real property collateral.

We face substantial competition from larger competitors.

We are subject to extensive government regulation that could limit or restrict our activities, which, in turn, may hamper our ability to increase our assets and earnings.

The short term and long term impact of the new Basel II capital standards and the forthcoming new capital rules to be proposed for non-Basel II U.S. banks is uncertain.

We are dependent on key personnel and the loss of one or more of those key personnel may materially and adversely affect our prospects.

Managing reputational risk is important to attracting and maintaining customers, investors and employees.

Natural disasters and geopolitical events beyond our control could adversely affect us.

Adverse conditions in Asia could adversely affect our business.

Because of our participation in the TARP Capital Purchase Program, we are subject to several restrictions including restrictions on compensation paid to our executives.

Our need to continue to adapt to our information technology systems to allow us to provide new and expanded services could present operational issues and require significant capital spending.

Certain provisions of our charter, bylaws, and rights agreement could make the acquisition of our company more difficult.

Edgar Filing: CATHAY GENERAL BANCORP - Form 10-Q

Our financial results could be adversely affected by changes in accounting standards or tax laws and regulations.
Risks relating to our common stock -

The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive.

Statutory restrictions on dividends and other distributions from the Bank may adversely impact us by limiting the amount of distributions Cathay General Bancorp may receive. State laws may restrict our ability to pay dividends.

The terms of our outstanding preferred stock limit our ability to pay dividends on and repurchase our common stock and there can be no assurance of any future dividends on our common stock generally.

Our outstanding preferred stock impacts net income available to our common stockholders and earnings per common share, and the Warrant as well as other potential issuances of equity securities may be dilutive to holders of our common stock.

The issuance of additional shares of preferred stock could adversely affect holders of common stock, which may negatively impact your investment.

Our outstanding debt securities restrict our ability to pay dividends on our capital stock.

If economic conditions continue to deteriorate, we may need even more capital.

Table of Contents

These and other factors are further described in Cathay General Bancorp's Current Report on Form 8-K filed on October 13, 2009, other reports and registration statements filed with the Securities and Exchange Commission (SEC), and other filings it makes with the SEC from time to time. Actual results in any future period may also vary from the past results discussed in this report. Given these risks and uncertainties, readers are cautioned not to place undue reliance on any forward-looking statements, which speak to the date of this report. Cathay General Bancorp has no intention and undertakes no obligation to update any forward-looking statement or to publicly announce any revision of any forward-looking statement to reflect future developments or events, except as required by law.

Cathay General Bancorp's filings with the SEC are available at the website maintained by the SEC at <http://www.sec.gov>, or by request directed to Cathay General Bancorp, 9650 Flair Drive, El Monte, California 91731, Attention: Investor Relations (626) 279-3286.

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)****CATHAY GENERAL BANCORP AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

	September 30, 2009	December 31, 2008
	(In thousands, except share and per share data)	
ASSETS		
Cash and due from banks	\$ 198,237	\$ 84,818
Short-term investments	331,767	25,000
Securities purchased under agreements to resell		201,000
Securities held-to-maturity	99,865	
Securities available-for-sale (amortized cost of \$3,266,440 in 2009 and \$3,043,566 in 2008)	3,294,808	3,083,817
Trading securities	12	12
Loans	7,115,582	7,472,368
Less: Allowance for loan losses	(189,370)	(122,093)
Unamortized deferred loan fees	(8,880)	(10,094)
Loans, net	6,917,332	7,340,181
Federal Home Loan Bank stock	71,791	71,791
Other real estate owned, net	87,769	61,015
Investments in affordable housing partnerships, net	98,046	103,562
Premises and equipment, net	109,369	104,107
Customers liability on acceptances	28,974	39,117
Accrued interest receivable	33,459	43,603
Goodwill	316,340	319,557
Other intangible assets	24,448	29,246
Other assets	137,546	75,813
Total assets	\$ 11,749,763	\$ 11,582,639
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits		
Non-interest-bearing demand deposits	\$ 829,302	\$ 730,433
Interest-bearing accounts:		
NOW accounts	324,774	257,234
Money market accounts	965,159	659,454
Saving accounts	349,298	316,263
Time deposits under \$100,000	1,484,056	1,644,407
Time deposits of \$100,000 or more	3,756,142	3,228,945
Total deposits	7,708,731	6,836,736
Federal funds purchased		52,000
Securities sold under agreements to repurchase	1,550,000	1,610,000
Advances from the Federal Home Loan Bank	929,362	1,449,362
Other borrowings from financial institutions	1,313	

Edgar Filing: CATHAY GENERAL BANCORP - Form 10-Q

Other borrowings for affordable housing investments	19,355	19,500
Long-term debt	171,136	171,136
Acceptances outstanding	28,974	39,117
Other liabilities	61,427	103,401
Total liabilities	10,470,298	10,281,252
Commitments and contingencies		
Stockholders' equity		
Preferred stock, 10,000,000 shares authorized, 258,000 issued and outstanding in 2009 and in 2008	243,103	240,554
Common stock, \$0.01 par value; 100,000,000 shares authorized, 57,279,715 issued and 53,072,150 outstanding at September 30, 2009 and 53,715,815 issued and 49,508,250 outstanding at December 31, 2008	573	537
Additional paid-in-capital	545,010	508,613
Accumulated other comprehensive income, net	16,441	23,327
Retained earnings	591,574	645,592
Treasury stock, at cost (4,207,565 shares in 2009 and in 2008)	(125,736)	(125,736)
Total Cathay General Bancorp stockholders' equity	1,270,965	1,292,887
Noncontrolling Interest	8,500	8,500
Total equity	1,279,465	1,301,387
Total liabilities and equity	\$ 11,749,763	\$ 11,582,639

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**CATHAY GENERAL BANCORP AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME/(LOSS)****(Unaudited)**

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
	(In thousands, except share and per share data)			
INTEREST AND DIVIDEND INCOME				
Loan receivable, including loan fees	\$ 99,588	\$ 114,005	\$ 302,232	\$ 341,880
Investment securities- taxable	31,589	27,575	94,104	84,507
Investment securities- nontaxable	167	284	620	974
Federal Home Loan Bank stock	149	1,004	149	2,685
Agency preferred stock		313		1,621
Federal funds sold and securities purchased under agreements to resell	35	2,899	1,338	12,294
Deposits with banks	119	42	250	523
Total interest and dividend income	131,647	146,122	398,693	444,484
INTEREST EXPENSE				
Time deposits of \$100,000 or more	20,224	26,226	65,337	86,398
Other deposits	10,622	17,100	40,196	49,519
Securities sold under agreements to repurchase	16,555	15,174	48,527	44,716
Advances from Federal Home Loan Bank	10,664	11,785	31,781	35,229
Long-term debt	1,067	2,030	3,891	6,889
Short-term borrowings		206	24	828
Total interest expense	59,132	72,521	189,756	223,579
Net interest income before provision for credit losses	72,515	73,601	208,937	220,905
Provision for credit losses	76,000	15,800	216,000	43,800
Net interest (loss)/income after provision for credit losses	(3,485)	57,801	(7,063)	177,105
NON-INTEREST INCOME/(LOSS)				
Securities gains/(losses), net	2,883	(15,313)	52,319	(12,980)
Letters of credit commissions	1,150	1,465	3,159	4,281
Depository service fees	1,272	1,189	3,940	3,636
Other operating income	4,982	4,290	10,964	12,393
Total non-interest income (loss)	10,287	(8,369)	70,382	7,330
NON-INTEREST EXPENSE				
Salaries and employee benefits	14,410	16,376	46,369	50,643
Occupancy expense	3,999	3,393	12,126	9,918
Computer and equipment expense	2,052	1,848	5,938	6,024
Professional services expense	3,694	3,410	10,021	8,890
FDIC and State assessments	4,464	1,336	15,372	3,172

Edgar Filing: CATHAY GENERAL BANCORP - Form 10-Q

Marketing expense	669	584	2,153	2,449
Other real estate owned expense	4,135	1,182	20,150	1,806
Operations of affordable housing investments , net	1,407	2,840	5,255	5,361
Amortization of core deposit intangibles	1,689	1,722	5,089	5,196
Other operating expense	2,288	2,329	7,863	6,970
Total non-interest expense	38,807	35,020	130,336	100,429
(Loss)/income before income tax (benefit)/expense	(32,005)	14,412	(67,017)	84,006
Income tax (benefit)/expense	(14,482)	7,370	(35,362)	30,133
Net (loss)/income	(17,523)	7,042	(31,655)	53,873
Less: net income attributable to noncontrolling interest	(156)	(151)	(457)	(452)
Net (loss)/income attributable to Cathay General Bancorp	(17,679)	6,891	(32,112)	53,421
Dividends on preferred stock	(4,086)		(12,249)	
Net (loss)/income available to common stockholders	(21,765)	6,891	(44,361)	53,421
Other comprehensive income (loss) , net of tax				
Unrealized holding gains/(losses) arising during the period	29,233	(5,833)	15,109	(18,106)
Less: reclassification adjustments included in net income	1,212	(8,910)	21,995	(2,730)
Total other comprehensive gain/(loss), net of tax	28,021	3,077	(6,886)	(15,376)
Total comprehensive income/(loss)	\$ 6,256	\$ 9,968	\$ (51,247)	\$ 38,045
Net (loss)/income per common share:				
Basic	\$ (0.43)	\$ 0.14	\$ (0.89)	\$ 1.08
Diluted	\$ (0.43)	\$ 0.14	\$ (0.89)	\$ 1.08
Cash dividends paid per common share	\$ 0.010	\$ 0.105	\$ 0.195	\$ 0.315
Basic average common shares outstanding	50,183,296	49,441,621	49,758,833	49,392,655
Diluted average common shares outstanding	50,183,296	49,530,272	49,758,833	49,497,171

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**CATHAY GENERAL BANCORP AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

	Nine Months Ended September 30	
	2009	2008
	(In thousands)	
Cash Flows from Operating Activities		
Net (loss)/income attributable to Cathay General Bancorp	\$ (32,112)	\$ 53,421
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	216,000	43,800
Provision for losses on other real estate owned	18,050	1,248
Deferred tax benefit	(42,630)	(24,489)
Depreciation	5,753	3,184
Net gains on sale of other real estate owned	(779)	(75)
Net gains on sale of loans held for sale	(3,949)	(245)
Proceeds from sale of loans held for sale	29,267	10,599
Originations of loans held for sale	(5,350)	(10,395)
Write-downs on venture capital investments	1,573	270
Write-downs on impaired securities	82	33,654
Gain on sales and calls of securities	(52,401)	(20,674)
Decrease in fair value of warrants	47	26
Amortization of security premiums, net	1,699	1,651
Amortization of intangibles	5,134	5,277
Excess tax short-fall from share-based payment arrangements	195	240
Stock based compensation expense	4,123	5,828
Gain on sale of premises and equipment		(21)
Decrease in accrued interest receivable	10,144	11,638
Decrease in income tax payable	(12,491)	
Increase/(decrease) in other assets, net	(7,610)	7,519
(Decrease)/increase in other liabilities	(20,690)	5,028
Net cash provided by operating activities	114,055	127,484
Cash Flows from Investing Activities		
Increase in short-term investments	(306,767)	(2,907)
Decrease in long-term investment		50,000
Decrease in securities purchased under agreements to resell	201,000	366,100
Purchase of investment securities available-for-sale	(1,048,251)	(1,503,844)
Proceeds from maturity and call of investment securities available-for-sale	1,036,522	819,939
Proceeds from sale of investment securities available-for-sale	4,989	586,932
Purchase of mortgage-backed securities available-for-sale	(2,487,276)	(1,580,092)
Proceeds from repayment and sale of mortgage-backed securities available-for-sale	2,321,756	1,391,236
Purchase of investment securities held-to-maturity	(99,858)	
Purchase of Federal Home Loan Bank stock		(4,765)
Redemption of Federal Home Loan Bank stock		5,498
Net decrease/(increase) in loans	118,747	(860,456)
Purchase of premises and equipment	(11,016)	(20,766)
Proceeds from sales of premises and equipment		21
Proceeds from sale of other real estate owned	25,675	105
Net increase in investment in affordable housing	(11,159)	(11,517)
Net cash used in investing activities	(255,638)	(764,516)

Edgar Filing: CATHAY GENERAL BANCORP - Form 10-Q

Cash Flows from Financing Activities

Net increase in demand deposits, NOW accounts, money market and saving deposits	505,149	187,385
Net increase/(decrease) in time deposits	366,846	383,418
Net (decrease)/increase in federal funds purchased and securities sold under agreement to repurchase	(112,000)	150,975
Advances from Federal Home Loan Bank	816,000	2,598,533
Repayment of Federal Home Loan Bank borrowings	(1,336,000)	(2,697,000)
Cash dividends paid to common stockholders	(9,657)	(15,555)
Issuance of common stock	31,390	
Cash dividends paid to preferred stockholders	(8,959)	
Proceeds from other borrowings	17,765	20,629
Repayment of other borrowings	(16,452)	(28,930)
Proceeds from shares issued to Dividend Reinvestment Plan	1,102	1,931
Proceeds from exercise of stock options	13	372
Excess tax short-fall from share-based payment arrangements	(195)	(240)
Net cash provided by financing activities	255,002	601,518
Decrease in cash and cash equivalents	113,419	(35,514)
Cash and cash equivalents, beginning of the period	84,818	118,437
Cash and cash equivalents, end of the period	\$ 198,237	\$ 82,923

Supplemental disclosure of cash flow information

Cash paid during the period:

Interest	\$ 200,507	\$ 226,210
Income taxes	\$ 24,749	\$ 56,699
Non-cash investing and financing activities:		
Net change in unrealized holding loss on securities available-for-sale, net of tax	\$ (6,886)	\$ (15,376)
Adjustment to initially apply EITF 06-4	\$	\$ (147)
Adjustment to initially apply SFAS No. 160	\$ 8,500	\$
Loans to facilitate other real estate owned	\$ 18,335	\$
Transfers to other real estate owned	\$ 87,687	\$ 28,357

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

CATHAY GENERAL BANCORP AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Business

Cathay General Bancorp (the Bancorp) is the holding company for Cathay Bank (the Bank), six limited partnerships investing in affordable housing investments in which the Bank is the sole limited partner, and GBC Venture Capital, Inc. The Bancorp also owns 100% of the common stock of five statutory business trusts created for the purpose of issuing capital securities. The Bank was founded in 1962 and offers a wide range of financial services. As of September 30, 2009, the Bank operates twenty branches in Southern California, eleven branches in Northern California, eight branches in New York State, three branches in Illinois, three branches in Washington State, two branches Texas, one branch in Massachusetts, one branch in New Jersey, one branch in Hong Kong, and a representative office in Shanghai and in Taipei. Deposit accounts at the Hong Kong branch are not insured by the Federal Deposit Insurance Corporation (the FDIC).

2. Acquisitions and Investments

We continue to look for opportunities to expand the Bank's branch network by seeking new branch locations and/or by acquiring other financial institutions to diversify our customer base in order to compete for new deposits and loans, and to be able to serve our customers more effectively.

For each acquisition, we develop an integration plan for the consolidated company that addresses, among other things, requirements for staffing, systems platforms, branch locations and other facilities. The established plans are evaluated regularly during the integration process and modified as required. Merger and integration expenses are summarized in the following primary categories: (i) severance and employee-related charges; (ii) system conversion and integration costs, including contract termination charges; (iii) asset write-downs, lease termination costs for abandoned space and other facilities-related costs; and (iv) other charges. Other charges include investment banking fees, legal fees, other professional fees relating to due diligence activities and expenses associated with preparation of securities filings, as appropriate. These costs are included in the allocation of the purchase price at the acquisition date based on our formal integration plans.

As of September 30, 2009, goodwill was \$316.3 million, a decrease of \$3.3 million, compared to \$319.6 million at December 31, 2008, due to the expiration of the statute of limitations for an uncertain tax position taken by GBC Bancorp which was previously recorded as a purchase accounting adjustment at the date of acquisition. Merger-related lease liability was \$378,000 at September 30, 2009, and \$424,000 at December 31, 2008.

3. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal

Table of Contents

recurring accruals) considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for the year ending December 31, 2009. For further information, refer to the audited consolidated financial statements and footnotes included in the Company's annual report on Form 10-K for the year ended December 31, 2008.

The preparation of the consolidated financial statements in accordance with GAAP requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. The most significant estimates subject to change are the allowance for loan losses, goodwill impairment, and other-than-temporary impairment.

4. Recent Accounting Pronouncements

In June 2009, the FASB issued Statement No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles*, a replacement of FASB Statement No. 162. SFAS 168 is to establish the FASB Accounting Standards Codification (ASC) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. New standards issued after the Codification's release will serve to update the Codification and will be referred to as Accounting Standards Updates (ASUs). Financial statements for interim and annual periods ended after September 15, 2009, shall use Codification references, not legacy GAAP references. SFAS 168 was codified into ASC 105 in June 2009. In conjunction with the issuance of SFAS 168, the FASB issued its first ASU No. 2009-1, *Topic 105- Generally Accepted Accounting Principles (ASU 2009-1)* and included SFAS 168 in its entirety. ASU 2009-1 was effective for the Company on September 15, 2009. The adoption of ASU 2009-1 did not have a material impact on the Company's consolidated financial statements.

SFAS No. 141, *Business Combinations (Revised 2007)* was codified into ASC Topic 805. ASC Topic 805 applies to all transactions and other events in which one entity obtains control over one or more other businesses and requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost-allocation process whereby the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their estimated fair value. ASC Topic 805 requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting and, instead, that contingency would be subject to the probable and estimable recognition criteria of ASC Topic 450, *Accounting for Contingencies*. ASC Topic 805 is expected to have a significant impact on the Company's accounting for business combinations closing on or after January 1, 2009.

Table of Contents

In April 2009, the FASB issued Staff Position (FSP) 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*. FSP 157-4 which was codified into ASC Topic 820 provides additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased when compared with normal market activity for the asset or liability and identifying transactions that are not orderly. In those circumstances, further analysis and significant adjustment to the transaction or quoted prices may be necessary to estimate fair value. This FSP reaffirms fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The adoption of this standard on June 15, 2009, did not have a material impact on the Company's consolidated financial statements. See Note 16- Fair Value Measurements for more information.

SFAS No. 160, *Noncontrolling Interest in Consolidated Financial Statements, an amendment of ARB Statement No. 51*. SFAS 160 amends Accounting Research Bulletin (ARB) No. 51, *Consolidated Financial Statements*, which was codified into ASC Topic 810 to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. ASC Topic 810 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is an ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, SFAS 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. It also requires disclosure, on the face of the consolidated income statement, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. The Company adopted ASC Topic 810 effective as of January 1, 2009, and reclassified non-controlling interest of \$8.5 million from other liabilities to equity.

In March 2008, the FASB issued Statement No. 161, *Disclosure about Derivative Instruments and Hedging Activities- an amendment of FASB Statement No. 133 (SFAS 161)*. SFAS 161 which was codified into ASC Topic 815 requires enhanced disclosures about how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for and how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. ASC Topic 815 was effective for the Company on November 15, 2008. The adoption of ASC Topic 815 did not have a material impact on the Company's consolidated financial statements.

In April 2009, the FASB issued Statement No. 107-1, *Interim Disclosure about Fair Value of Financial Instruments*. SFAS 107-1 was codified into ASC Topic 825. ASC Topic 825 requires publicly traded companies to disclose the fair value of financial instruments within the scope of ASC Topic 825 in interim financial statements, in addition to annual statements. Publicly traded companies also shall disclose the methods and significant assumptions used to estimate the fair value of financial instruments and shall describe changes in methods and significant assumptions, if any, during the period. The adoption of this standard on June 15, 2009, did not have a significant impact on the Company's financial statements.

In April 2009, the FASB also issued Statement No. 115-2, *Recognition and Presentation of Other-Than-Temporary Impairments*. SFAS 115-2 which was codified into ASC Topic 320 changes the requirements for recognizing other-than-temporary impairment (OTTI) for debt securities. This standard requires an entity to assess whether the entity has the intent to sell the debt security or more

Table of Contents

likely than not will be required to sell the debt security before its anticipated recovery. If either of these conditions is met, an entity must recognize an OTTI. OTTI is separated into the amount of the total impairment related to credit losses and the amount of the total impairment related to all other factors. An entity determines the impairment related to credit losses by comparing the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. OTTI related to the credit loss is then recognized in earnings. OTTI related to all other factors is recognized in other comprehensive income. OTTI not related to the credit loss for a held-to-maturity security should be recognized separately in a new category of other comprehensive income and amortized over the remaining life of the debt security as an increase in the carrying value of the security only when the entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its remaining amortized cost basis. This standard expands and increases the frequency of existing disclosures about OTTI for debt and equity securities. On June 15, 2009, the date the Company adopted this standard, no cumulative effect was recorded because the Company had not previously recorded any other-than-temporary impairment related to the credit loss associated with available-for-sale debt securities that the Company owned. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In May 2009, the FASB issued Statement No. 165, *Subsequent Events*. SFAS 165 which was codified into ASC Topic 855 applies to the accounting for and disclosure of subsequent events, but will not result in significant changes in practice. Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued or are available to be issued. There are two types of subsequent events- recognized subsequent events and non-recognized subsequent events. An entity shall recognize in the financial statements the effects of events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, a recognized subsequent event. An entity shall not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance but arose after that date, a non-recognized subsequent event. ASC Topic 855 is effective for annual financial statements covering the first fiscal year ending after June 15, 2009. Adoption of ASC Topic 855 did not have a significant impact on the Company's consolidated financial statements.

In June 2009, the FASB issued Statement No. 166, *Accounting for Transfers of Financial Assets an amendment of FASB Statement No. 140*. SFAS 166 removes the concept of a qualifying special-purpose entity and the provisions for guaranteed mortgage securitizations in earlier FASB pronouncements. A transferor should account for the transfer as a sale only if it transfers an entire financial asset and surrenders control over the entire transferred assets in accordance with the conditions in SFAS 166. SFAS limits the circumstances in which a financial asset should be derecognized. SFAS 166 is effective for annual financial statements covering the first fiscal year ending after November 15, 2009. The Company does not expect a material impact on its consolidated financial statements from adoption of SFAS 166.

Statement No. 167, *Amendments to FASB Interpretation No. 46(R)* was also issued in June 2009. SFAS 167 eliminates the quantitative approach previously required under FIN 46(R) (ASC Subtopic 810-10) for determining whether an entity is a variable interest entity. SFAS 167 requires an entity to perform an ongoing assessments to determine whether an entity is the primarily beneficiary of a variable interest entity. The ongoing assessments identify the power to direct the activities of a variable interest entity, the obligation to absorb losses of the entity and the right to receive benefits from the entity that could potentially be significant to the variable interest entity. SFAS 167 is

Table of Contents

effective for annual financial statements covering the first fiscal year ending after November 15, 2009. The Company does not expect a material impact on its consolidated financial statements from adoption of SFAS 167.

5. Earnings/Loss per Share

Basic earnings per share excludes dilution and is computed by dividing net income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock and resulted in the issuance of common stock that then shared in earnings. Potential dilution is excluded from computation of diluted per-share amounts when a net loss from operation exists.

Outstanding stock options with anti-dilutive effect were not included in the computation of diluted earnings per share. The following table sets forth basic and diluted earnings per share calculations and the average shares of stock options with anti-dilutive effect:

(Dollars in thousands, except share and per share data)	For the three months ended September 30,		For the nine months ended September 30,	
	2009	2008	2009	2008
Net(loss)/ Income attributable to Cathay General Bancorp	\$ (17,679)	\$ 6,891	\$ (32,112)	\$ 53,421
Dividends on preferred stock	(4,086)		(12,249)	
Net (loss)/ income available to common stockholders	\$ (21,765)	\$ 6,891	\$ (44,361)	\$ 53,421
Weighted-average shares:				
Basic weighted-average number of common shares outstanding	50,183,296	49,441,621	49,758,833	49,392,655
Dilutive effect of weighted-average outstanding common shares equivalents				
Stock Options	0	83,147	0	102,398
Restricted Stock	0	5,504	0	2,118
Diluted weighted-average number of common shares outstanding	50,183,296	49,530,272	49,758,833	49,497,171
Average shares of stock options and warrants with anti-dilutive effect				
	12,108,437	4,808,696	8,724,857	4,429,533
(Loss)/Earnings per common stock share:				
Basic	\$ (0.43)	\$ 0.14	\$ (0.89)	\$ 1.08
Diluted	\$ (0.43)	\$ 0.14	\$ (0.89)	\$ 1.08

6. Stock-Based Compensation

In 1998, the Board adopted the Cathay Bancorp, Inc. Equity Incentive Plan. Under the Equity Incentive Plan, as amended in September, 2003, directors and eligible employees may be granted incentive or non-statutory stock options and/or restricted stock units, or awarded non-vested stock, for up to 7,000,000 shares of the Company's common stock on a split adjusted basis. In May 2005, the stockholders of the Company approved the 2005 Incentive Plan which provides that 3,131,854 shares of the Company's common stock may be granted as incentive or non-statutory stock options, or as restricted stock, or as restricted stock units. In conjunction with the approval of the 2005 Incentive Plan, the Bancorp agreed to cease granting awards under the Equity Incentive Plan. As of September 30, 2009, the only options granted by the Company under the 2005 Incentive Plan were non-statutory

Table of Contents

stock options to selected bank officers and non-employee directors at exercise prices equal to the fair market value of a share of the Company's common stock on the date of grant. Such options have a maximum ten-year term and vest in 20% annual increments (subject to early termination in certain events) except options granted to the Chief Executive Officer of the Company for 100,000 shares granted on February 21, 2008, of which 50% were vested on February 21, 2009, and the remaining 50% would vest on February 21, 2010. If such options expire or terminate without having been exercised, any shares not purchased will again be available for future grants or awards. Stock options are typically granted in the first quarter of the year. There were no options granted during the first nine months of 2009. In February 21, 2008, the Company granted options of 689,200 shares and restricted stock units of 82,291 shares to selected bank officers and non-employee directors. The Company expects to issue new shares to satisfy stock option exercises and the vesting of restricted stock units.

Stock-based compensation expense for stock options is calculated based on the fair value of the award at the grant date for those options expected to vest, and is recognized as an expense over the vesting period of the grant. The Company uses the Black-Scholes option pricing model to estimate the value of granted options. This model takes into account the option exercise price, the expected life, the current price of the underlying stock, the expected volatility of the Company's stock, expected dividends on the stock and a risk-free interest rate. The Company estimates the expected volatility based on the Company's historical stock prices for the period corresponding to the expected life of the stock options. Based on SAB 107 and SAB 110, the Company has estimated the expected life of the options based on the average of the contractual period and the vesting period and has consistently applied the simplified method to all options granted starting from 2005. Option compensation expense totaled \$1.2 million for the three months ended September 30, 2009, and \$1.7 million for the three months ended September 30, 2008. For the nine months ended September 30, option compensation expense totaled \$3.9 million for 2009 and \$5.1 million for 2008. Stock-based compensation is recognized ratably over the requisite service period for all awards. Unrecognized stock-based compensation expense related to stock options totaled \$6.2 million at September 30, 2009, and is expected to be recognized over the next 1.9 years.

The weighted average per share fair value on the date of grant of the options granted was \$6.86 during the first quarter of 2008. There were no options granted in the first nine months of 2009. The Company estimated the expected life of the options based on the average of the contractual period and the vesting period. The fair value of stock options has been determined using the Black-Scholes option pricing model with the following assumptions:

	Nine months ended September 30, 2008
Expected life- number of years	6.4
Risk-free interest rate	3.09%
Volatility	30.04%
Dividend yield	1.80%

Table of Contents

No stock options were exercised during the third quarter of 2009 and 2,000 shares were exercised during the third quarter of 2008. Cash received from exercises of stock options totaled \$13,000 from the exercise of stock options on 1,280 shares during the nine months ended September 30, 2009, and \$372,000 from the exercise of 20,906 shares during the nine months ended September 30, 2008. No stock options were vested during the third quarter of 2009 and during the third quarter of 2008. The table below summarizes stock option activity for the periods indicated:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Balance at December 31, 2008	5,206,374	\$ 27.72	5.6	\$ 6,220
Granted				
Forfeited	(7,956)	31.10		
Exercised	(1,280)	10.63		
Balance at March 31, 2009	5,197,138	\$ 27.72	5.3	\$
Granted				
Forfeited	(5,438)	34.15		
Exercised				
Balance at June 30, 2009	5,191,700	\$ 27.71	5.1	\$
Granted				
Forfeited	(21,766)	27.96		
Exercised				
Balance at September 30, 2009	5,169,934	\$ 27.71	4.9	\$
Exercisable at September 30, 2009	4,233,106	\$ 27.34	4.3	\$

At September 30, 2009, 1,609,640 shares were available under the Company's 2005 Incentive Plan for future grants.

In addition to stock options above, in February 2008, the Company also granted restricted stock units on 82,291 shares of the Company's common stock to its eligible employees. On the date of granting of these restricted stock units, the closing price of the Company's stock was \$23.37 per share. Such restricted stock units have a maximum term of five years and vest in approximately 20% annual increments subject to employees' continued employment with the Company. On February 21, 2009, restricted stock units of 15,828 shares were vested at the closing price of \$8.94 per share. Among the 15,828 restricted stock units, 2,865 shares were cancelled immediately for employees who elected to satisfy income tax withholding amounts through cancellation of restricted stock units. Common stock shares of 12,963 were issued and outstanding as of February 21, 2009. The following table presents information relating to the restricted stock units grant as of September 30, 2009:

	Units
Balance at December 31, 2008	79,537
Vested	(12,963)
Cancelled or forfeited	(5,559)
Balance at September 30, 2009	61,015

The compensation expense recorded related to the restricted stock units above was \$82,000 for the three months ended September 30, 2009, and \$82,000 for the three months ended September 30, 2008. For the nine months ended September 30, compensation expense recorded was \$245,000 in 2009 and \$191,000 in 2008. Unrecognized stock-based compensation expense related to restricted stock units was \$1.1 million at

September 30, 2009, and is expected to be recognized over the next 3.4 years.

Table of Contents

Prior to 2006, the Company presented the entire amount of the tax benefit on options exercised as operating activities in the consolidated statements of cash flows. After adoption of SFAS No. 123R in January 2006, the Company reports only the benefits of tax deductions in excess of grant-date fair value as cash flows from operating activity and financing activity. The following table summarizes the tax benefit (short-fall) from share-based payment arrangements:

(Dollars in thousands)	For the three months ended		For the nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Short-fall of tax deductions in excess of grant-date fair value	\$ (64)	\$ (3)	\$ (195)	\$ (240)
Benefit of tax deductions on grant-date fair value	64	15	198	297
Total benefit of tax deductions	\$	\$ 12	\$ 3	\$ 57

7. Securities Purchased Under Agreements to Resell

Securities purchased under agreements to resell are usually collateralized by U.S. government agency and mortgage-backed securities. The counter-parties to these agreements are nationally recognized investment banking firms that meet credit requirements of the Company and with whom a master repurchase agreement has been duly executed. As of December 31, 2008, the Company had four resale agreements of \$201.0 million outstanding at an annualized weighted average interest rate of 5.39%. During the first quarter of 2009, one resale agreement of \$51.0 million matured in January 2009 and three long-term resale agreements of \$150.0 million were called in February 2009. As of September 30, 2009, the Company has no resale agreements outstanding.

For those securities obtained under the resale agreements, the collateral is either held by a third party custodian or by the counter-party and is segregated under written agreements that recognize the Company's interest in the securities. Interest income associated with securities purchased under resale agreements was zero for the third quarter of 2009 and \$1.3 million for the first nine months of 2009 and \$2.8 million for the third quarter of 2008 and \$12.0 million for the first nine months of 2008.

8. Securities

The following tables summarize the composition, amortized cost, gross unrealized gains, gross unrealized losses, and fair value of securities available-for-sale, as of September 30, 2009, and December 31, 2008:

	Amortized Cost	September 30, 2009		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
(In thousands)				
U.S. government sponsored entities	\$ 805,461	\$ 2,318	\$	\$ 807,779
State and municipal securities	15,844	167	29	15,982
Mortgage-backed securities	2,297,707	29,271	1,440	2,325,538
Collateralized mortgage obligations	127,929	406	2,500	125,835
Asset-backed securities	317		69	248
Corporate bonds	10,246		676	9,570
Preferred stock of government sponsored entities	701	1,621		2,322
Other securities foreign organization	6,450	1		6,451
Other equity securities	1,785		702	1,083
Total	\$ 3,266,440	\$ 33,784	\$ 5,416	\$ 3,294,808

Table of Contents

	Amortized Cost	December 31, 2008		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
(In thousands)				
U.S. treasury securities	\$ 10,510	\$ 35	\$	\$ 10,545
U.S. government sponsored entities	764,341	1,641		765,982
State and municipal securities	23,059	214	37	23,236
Mortgage-backed securities	2,029,265	53,476	5,278	2,077,463
Collateralized mortgage obligations	179,939	462	7,523	172,878
Asset-backed securities	423		63	360
Corporate bonds	35,246		2,676	32,570
Preferred stock of government sponsored entities	783			783
Total	\$ 3,043,566	\$ 55,828	\$ 15,577	\$ 3,083,817

Realized gains or losses on sales of securities available-for-sale are recorded using the specific identification method. The amortized cost and fair value of debt securities available-for-sale at September 30, 2009, by contractual maturities are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or repay obligations with or without call or repayment penalties.

	Amortized	
	Cost	Fair Value
(In thousands)		
Due in one year or less	\$ 8,195	\$ 8,212
Due after one year through five years	439,844	439,772
Due after five years through ten years	657,258	664,113
Due after ten years	2,161,143	2,182,711
Total	\$ 3,266,440	\$ 3,294,808

Proceeds from sales, calls, and repayments of securities available-for-sale were \$3.4 billion during the first nine months on 2009 compared to \$2.8 billion during the same period a year ago, and were \$424.2 million during the third quarter of 2009 compared to \$1.2 billion during the same quarter a year ago. Gains of \$52.4 million and no losses were realized on sales and calls of securities available-for-sale for the first nine months of 2009 compared with \$20.7 million in gains and \$6,000 in losses realized for the same period a year ago. Gains of \$2.9 million and no losses were realized on sales and calls of securities available-for-sale for the third quarter of 2009 compared with \$18.3 million in gains and no losses realized for the same quarter a year ago.

Between 2002 and 2004, the Company purchased a number of mortgage-backed securities and collateralized mortgage obligations comprised of interests in non-agency guaranteed residential mortgages. At September 30, 2009, the remaining par value was \$14.0 million for these mortgage-backed securities with unrealized losses of \$1.4 million and \$121.0 million for collateralized mortgage obligations with unrealized losses of \$2.4 million. The remaining par value of these securities totaled \$135.0 million which represents 4.1% of the fair value of the Company's securities available-for-sale and 1.1% of the Company's total assets. At September 30, 2009, the unrealized loss for these securities totaled \$3.8 million which represented 2.8% of the par amount of these non-agency guaranteed residential mortgages and resulted from increases in credit spreads subsequent to the date that these securities were purchased. Based on the Company's analysis at September 30, 2009, there

Table of Contents

was no other-than-temporary impairment in these securities due to the low loan to value ratio for the loans underlying these securities, the credit support provided by junior tranches of these securitizations, and the continued AAA rating for all but five issues of these securities. The Company's analysis also indicated the continued full ultimate collection of principal and interest for the five issues that were no longer rated AAA.

The Company's unrealized loss on investments in corporate bonds relates to two investments in bonds of financial institutions in the amounts of \$10 million and \$250,000, all of which were investment grade at the date of acquisition and as of September 30, 2009. The unrealized losses of \$676,000 were primarily caused by the widening of credit spreads since the dates of acquisition. The contractual terms of those investments do not permit the issuers to settle the security at a price less than the amortized cost of the investment. The Company currently does not believe it is probable that it will be unable to collect all amounts due according to the contractual terms of the investment. Therefore, it is expected that these debentures would not be settled at a price less than the amortized cost of the investment.

ASC Topic 320 changes the requirements for recognizing other-than-temporary impairment (OTTI) for debt securities. ASC Topic 320 requires an entity to assess whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The Company has no intent to sell and will not be required to sell available-for-sale securities that decline below their cost before their anticipated recovery. At September 30, 2009, there was no other-than-temporary impairment related to credit losses to be recognized in earnings. Other-than-temporary impairment related to all other factors was recognized in other comprehensive income.

The temporarily impaired securities represent 5.2% of the fair value of securities available-for-sale as of September 30, 2009. Unrealized losses for securities with unrealized losses for less than twelve months represent 2.1%, and securities with unrealized losses for twelve months or more represent 3.8% of the historical cost of these securities and generally resulted from increases in interest rates subsequent to the date that these securities were purchased. All of these securities are investment grade as of September 30, 2009. At September 30, 2009, 39 issues of securities had unrealized losses for 12 months or longer and 8 issues of securities had unrealized losses of less than 12 months. The table below shows the fair value, unrealized losses, and number of issuances as of September 30, 2009, of the temporarily impaired securities in the Company's available-for-sale securities portfolio:

Temporarily Impaired Securities as of September 30, 2009

Description of securities	Less than 12 months			12 months or longer			Total		
	Fair Value	Unrealized Losses	No. of Issuances	Fair Value	Unrealized Losses	No. of Issuances	Fair Value	Unrealized Losses	No. of Issuances
				(In thousands, except no. of issuances)					
State and municipal securities				668	29	1	668	29	1
Mortgage-backed securities	50,799	18	6	2,283	45	10	53,082	63	16
Non-agency mortgage-backed securities				12,565	1,377	3	12,565	1,377	3
Collateralized mortgage obligations	22,075	881	1	71,956	1,619	21	94,031	2,500	22
Asset-backed securities				249	69	1	249	69	1
Corporate bonds				9,320	676	3	9,320	676	3
Equity securities	1,083	702	1				1,083	702	1
Total	\$ 73,957	\$ 1,601	8	\$ 97,041	\$ 3,815	39	\$ 170,998	\$ 5,416	47

Table of Contents

On June 19, 2009, the Company securitized \$13.9 million real estate mortgage loans through Federal Home Loan Mortgage Corporation (FHLMC) and recognized mortgage servicing assets of \$139,000 for the servicing rights it retained. On June 26, 2009, the Company sold all of the resulting securities of \$13.9 million and recognized gains on sale of securities of \$492,000. Prior to June 2009, the Company had no securitization transactions.

In August, 2009, the Company purchased U.S. government agency securities at par of \$100.0 million and classified them as securities held-to-maturity securities. Book value for securities held-to-maturity were \$99.9 million at September 30, 2009 and zero at September 30, 2008.

9. Investments in Affordable Housing

The Company has invested in certain limited partnerships that were formed to develop and operate housing for lower-income tenants throughout the United States. The Company's investments in these partnerships were \$98.0 million at September 30, 2009, and \$103.6 million at December 31, 2008. At September 30, 2009 and December 31, 2008, six of the limited partnerships in which the Company has an equity interest were determined to be variable interest entities for which the Company is the primary beneficiary. The consolidation of these limited partnerships in the Company's consolidated financial statements increased total assets and liabilities by \$23.0 million at September 30, 2009, and by \$22.8 million at December 31, 2008. Other borrowings for affordable housing limited partnerships were \$19.4 million at September 30, 2009 and \$19.5 million at December 31, 2008; recourse is limited to the assets of the limited partnerships. Unfunded commitments for affordable housing limited partnerships of \$11.1 million as of September 30, 2009, and \$22.1 million as of December 31, 2008 were recorded under other liabilities.

10. Commitments and Contingencies

In the normal course of business, the Company becomes a party to financial instruments with off-balance sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit in the form of loans, or through commercial or standby letters of credit, and financial guarantees. These instruments represent varying degrees of exposure to risk in excess of the amounts included in the accompanying condensed consolidated balance sheets. The contractual or notional amount of these instruments indicates a level of activity associated with a particular class of financial instrument and is not a reflection of the level of expected losses, if any.

Table of Contents

The Company's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The following table summarizes the outstanding commitments as of the dates indicated:

(In thousands)	At September 30, 2009	At December 31, 2008
Commitments to extend credit	\$ 1,585,758	\$ 2,047,985
Standby letters of credit	57,284	79,423
Other letters of credit	60,267	66,220
Bill of lading guarantees	44	493
Total	\$ 1,703,353	\$ 2,194,121

As of September 30, 2009, \$11.1 million unfunded commitments for affordable housing investments were recorded under other liabilities compared to \$22.1 million at December 31, 2008.

Commitments to extend credit are agreements to lend to a customer provided there is no violation of any condition established in the commitment agreement. These commitments generally have fixed expiration dates and the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Company upon extension of credit is based on management's credit evaluation of the borrower. Letters of credit, including standby letters of credit and bill of lading guarantees, are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing these types of instruments is essentially the same as that involved in making loans to customers.

11. Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase were \$1.6 billion with a weighted average rate of 4.20% at September 30, 2009, compared to \$1.6 billion with a weighted average rate of 3.95% at December 31, 2008. Seventeen floating-to-fixed rate agreements totaling \$900.0 million are with initial floating rates for a period of time ranging from nine months to one year, with the floating rates ranging from the three-month LIBOR minus 100 basis points to the three-month LIBOR minus 340 basis points. Thereafter, the rates are fixed for the remainder of the term, with interest rates ranging from 4.29% to 5.07%. After the initial floating rate term, the counterparties have the right to terminate the transaction at par at the fixed rate reset date and quarterly thereafter. Thirteen fixed-to-floating rate agreements totaling \$650.0 million are with initial fixed rates ranging from 1.00% and 3.50% with initial fixed rate terms ranging from nine months to eighteen months. For the remainder of the seven year term, the rates float at 8% minus the three-month LIBOR rate with a maximum rate ranging from 3.25% to 3.75% and minimum rate of 0.0%. After the initial fixed rate term, the counterparties have the right to terminate the transaction at par at the floating rate reset date and quarterly thereafter. The table below provides summary data for securities sold under agreements to repurchase as of September 30, 2009:

Securities Sold Under Agreements to Repurchase

(Dollars in millions)	Fixed-to-floating				Floating-to-fixed				Total
Callable	All callable at September 30, 2009				All callable at September 30, 2009				
Rate type	Float Rate				Fixed Rate				
Rate index	8% minus 3 month LIBOR								
Maximum rate	3.75%	3.50%	3.50%	3.25%					
Minimum rate	0.0%	0.0%	0.0%	0.0%					
No. of agreements	3	5	4	1	2	1	10	4	30
Amount	\$ 150.0	\$ 250.0	\$ 200.0	\$ 50.0	\$ 100.0	\$ 50.0	\$ 550.0	\$ 200.0	\$ 1,550.0
Weighted average rate	3.75%	3.50%	3.50%	3.25%	4.77%	4.83%	4.54%	5.00%	4.20%
Final maturity	2014	2014	2015	2015	2011	2012	2014	2017	

Table of Contents

These transactions are accounted for as collateralized financing transactions and recorded at the amounts at which the securities were sold. The Company may have to provide additional collateral for the repurchase agreements, as necessary. The underlying collateral pledged for the repurchase agreements consists of U.S. Treasury securities, U.S. government agency security debt, and mortgage-backed securities with a fair value of \$1.8 billion as of September 30, 2009, and \$1.7 billion as of December 31, 2008.

12. Advances from the Federal Home Loan Bank

Total advances from the FHLB of San Francisco decreased \$520.0 million to \$929.4 million at September 30, 2009 from \$1.45 billion at December 31, 2008. Non-puttable advances totaled \$229.4 million with a weighted rate of 4.76% and puttable advances totaled \$700.0 million with a weighted average rate of 4.42% at September 30, 2009. The FHLB has the right to terminate the puttable transaction at par at each three-month anniversary after the first puttable date. As of September 30, 2009, all puttable FHLB advances were puttable but FHLB had not exercised its right to terminate any of the puttable transactions.

13. Subordinated Note and Junior Subordinated Debt

On September 29, 2006, the Bank issued \$50.0 million in subordinated debt in a private placement transaction (Bank Subordinated Securities). The debt has a maturity term of 10 years, is unsecured and bears interest at a rate of three month LIBOR plus 110 basis points, payable on a quarterly basis. At September 30, 2009, the per annum interest rate on the subordinated debt was 1.38% compared to 2.56% at December 31, 2008. The subordinated debt was issued through the Bank and qualifies as Tier 2 capital for regulatory reporting purposes and is included in long-term debt in the accompanying condensed consolidated balance sheets.

The Bancorp established three special purpose trusts in 2003 and two in 2007 for the purpose of issuing trust preferred securities to outside investors (Capital Securities). The trusts exist for the purpose of issuing the Capital Securities and investing the proceeds thereof, together with proceeds from the purchase of the common stock of the trusts by the Bancorp, in junior subordinated notes issued by the Bancorp (Junior Subordinated Securities). The five special purpose trusts are considered variable interest entities under GAAP. Because the Bancorp is not the primary beneficiary of the trusts, the financial statements of the trusts are not included in the consolidated financial statements of the Company. At September 30, 2009, junior subordinated debt securities totaled \$121.1 million with a weighted average interest rate of

Table of Contents

2.46% compared to \$121.1 million with a weighted average rate of 4.02% at December 31, 2008. The junior subordinated debt securities have a stated maturity term of 30 years and are currently included in the Tier 1 capital of the Bancorp for regulatory capital purposes.

14. Income Taxes and Implementation of FASB Interpretation No. 48

The income tax benefit totaled \$35.4 million, or an effective tax benefit rate of 52.4% for the first nine months of 2009 compared to income tax expense of \$30.1 million, or effective tax rate of 36.1%, for the same period a year ago. Income tax benefit/expense results in effective tax rates that differ from the statutory Federal income tax rate for the periods indicated as follows:

	Nine Months Ended September 30,			
	2009	(In thousands)		2008
Tax provision at Federal statutory rate	\$ (23,616)	35.0%	\$ 29,244	35.0%
State income taxes, net of Federal income tax benefit	(3,856)	5.7	5,332	6.4
Interest on obligations of state and political subdivisions, which are exempt from Federal taxation	(212)	0.3	(333)	(0.4)
Low income housing tax credit	(8,089)	12.0	(7,123)	(8.5)
Agency preferred stock write-down			4,632	5.5
Other, net	411	(0.6)	(1,619)	(1.9)
Total income tax (benefit)/expense	\$ (35,362)	52.4%	\$ 30,133	36.1%

As previously disclosed, on December 31, 2003, the California Franchise Tax Board (FTB) announced its intent to list certain transactions that in its view constitute potentially abusive tax shelters. Included in the transactions subject to this listing were transactions utilizing regulated investment companies (RICs) and real estate investment trusts (REITs). While the Company continues to believe that the tax benefits recorded in 2000, 2001, and 2002 with respect to its regulated investment company were appropriate and fully defensible under California law, the Company participated in Option 2 of the Voluntary Compliance Initiative of the Franchise Tax Board, and paid all California taxes and interest on these disputed 2000 through 2002 tax benefits, and at the same time filed a claim for refund for these years while avoiding certain potential penalties. The Company expects to resolve the California tax audits of its 2000 through 2002 tax years without any additional accruals.

In May 2009, the Company filed amended California tax returns for tax years 2003 through 2007. The Company paid California income tax of \$5.5 million and interest of \$1.2 million, substantially all of which had previously been recorded as unrecognized tax benefits.

The Company recognizes accrued interest and penalties relating to unrecognized tax benefits as an income tax provision expense. The Company had approximately \$0.3 million of accrued interest and penalties as of September 30, 2009 and \$1.9 million of accrued interest and penalties as of December 31, 2008.

The Company's tax returns are open for audits by the Internal Revenue Service back to 2005 and by the Franchise Tax Board of the State of California back to 2000. The Company is currently under audit by the California Franchise Tax Board for the years 2000 to 2004.

Table of Contents

15. Sales of Common Stock

On September 9, 2009, the Company commenced a \$75 million at-the-market common stock offering. Through September 30, 2009, the Company raised \$31.4 million in additional capital through the sale of 3,490,000 shares of common stock from its at-the-market common stock offering.

16. Fair Value Measurements

ASC Topic 820 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Company adopted ASC Topic 820 on January 1, 2008, and determined the fair values of our financial instruments based on the following:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Observable prices in active markets for similar assets or liabilities; prices for identical or similar assets or liabilities in markets that are not active; directly observable market inputs for substantially the full term of the asset and liability; market inputs that are not directly observable but are derived from or corroborated by observable market data.

Level 3 - Unobservable inputs based on the Company's own judgments about the assumptions that a market participant would use. The Company uses the following methodologies to measure the fair value of its financial assets on a recurring basis:

Securities available for sale. For certain actively traded agency preferred stocks and U.S. Treasury securities, the Company measures the fair value based on quoted market prices in active exchange markets at the reporting date, a Level 1 measurement. The Company also measures securities by using quoted market prices for similar securities or dealer quotes, a Level 2 measurement. This category generally includes U.S. Government agency securities, state and municipal securities, mortgage-backed securities (MBS), commercial MBS, collateralized mortgage obligations, asset-backed securities and corporate bonds.

Trading securities. The Company measures the fair value of trading securities based on quoted market prices in active exchange markets at the reporting date, a Level 1 measurement.

Impaired loans. The Company does not record loans at fair value on a recurring basis. However, from time to time, nonrecurring fair value adjustments to collateral dependent impaired loans are recorded based on either current appraised value of the collateral, a Level 2 measurement, or management's judgment and estimation of value reported on old appraisals which are then adjusted based on recent market trends, a Level 3 measurement.

Other real estate owned. Real estate acquired in the settlement of loans is initially recorded at fair value, less estimated costs to sell. The Company records other real estate owned at fair value on a non-recurring basis. However, from time to time, nonrecurring fair value adjustments to other real estate owned are recorded based on current appraised value of the property, a Level 2 measurement, or management's judgment and estimation based on reported appraisal value, a Level 3 measurement.

Table of Contents

Equity investments. The Company records equity investments at fair value on a nonrecurring basis. However, from time to time, nonrecurring fair value adjustments to equity investments are recorded based on quoted market prices in active exchange market at the reporting date, a Level 1 measurement.

Warrants. The Company measures the fair value of warrants based on unobservable inputs based on assumption and management judgment, a Level 3 measurement.

Currency Option Contracts and Foreign Exchange Contracts. The Company measures the fair value of currency option and foreign exchange contracts based on dealer quotes on a recurring basis, a Level 2 measurement.

Interest Rate Swaps. Fair value of interest rate swaps was derived from observable market prices for similar assets on a recurring basis, a level 2 measurement.

Table of Contents

The following table presents the Company's hierarchy for its assets and liabilities measured at fair value on a recurring and non-recurring basis at September 30, 2009:

	Fair Value Measurements Using			Total at Fair Value
	Level 1	Level 2	Level 3	
(In thousands)				
Assets				
<u>On a Recurring Basis</u>				
Securities available-for-sale				
U.S. government sponsored entities	\$	\$ 807,779	\$	\$ 807,779
State and municipal securities		15,982		15,982
Mortgage-backed securities		2,325,538		2,325,538
Collateralized mortgage obligations		125,835		125,835
Asset-backed securities		248		248
Corporate bonds		9,570		9,570
Preferred stock of government sponsored entities		2,322		2,322
Other foreign securities		6,451		6,451
Other equity securities	1,083			1,083
Total securities available-for-sale	1,083	3,293,725		3,294,808
Trading securities	12			12
Warrants			103	103
Option contracts		156		156
Foreign exchange contracts		11,766		11,766
<u>On a Nonrecurring Basis</u>				
Impaired loans		99,773	36,139	135,912
Other real estate owned (1)		86,653	6,117	92,770