PROVIDENT FINANCIAL HOLDINGS INC
Form 10-Q
February 08, 2013

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 ……………………………………..... December 31, 2012

[ ] 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 000-28304

PROVIDENT FINANCIAL HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware	33-0704889
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3756 Central Avenue, Riverside, California 92506
(Address of principal executive offices and zip code)

(951) 686-6060
(Registrant's telephone number, including area code)

.
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes Ö . 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 the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer [ ]	Accelerated filer [Ö]
Non-accelerated filer [ ]	Smaller reporting company [ ]

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

APPLICABLE ONLY TO CORPORATE ISSUERS

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

Title of class:	As of February 1, 2013
Common stock, $ 0.01 par value, per share	10,605,355 shares

PROVIDENT FINANCIAL HOLDINGS, INC.

Table of Contents

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Financial Condition
(Unaudited)
In Thousands, Except Share Information

	December 31, 2012	June 30, 2012
Assets		
Cash and cash equivalents	$ 99,634	$ 145,136
Investment securities – available for sale, at fair value	21,184	22,898
Loans held for investment, net of allowance for loan losses of $18,530 and $21,483, respectively	772,057	796,836
Loans held for sale, at fair value	294,434	231,639
Accrued interest receivable	3,032	3,277
Real estate owned, net	2,435	5,489
Federal Home Loan Bank ("FHLB") – San Francisco stock	19,149	22,255
Premises and equipment, net	6,528	6,600
Prepaid expenses and other assets	29,877	26,787
Total assets	$ 1,248,330	$ 1,260,917
Liabilities and Stockholders' Equity		
Liabilities:		
Non interest-bearing deposits	$ 51,121	$ 55,688
Interest-bearing deposits	884,085	905,723
Total deposits	935,206	961,411
Borrowings	126,519	126,546
Accounts payable, accrued interest and other liabilities	30,749	28,183
Total liabilities	1,092,474	1,116,140
Commitments and Contingencies		
Stockholders' equity:		
Preferred stock, $.01 par value (2,000,000 shares authorized; none issued and outstanding)	-	-
Common stock, $.01 par value (40,000,000 shares authorized; 17,647,865 and 17,619,865 shares issued; 10,597,005 and 10,856,027 shares outstanding, respectively)	176	176
Additional paid-in capital	87,278	86,758
Retained earnings	171,155	156,560
Treasury stock at cost (7,050,860 and 6,763,838 shares, respectively)	(103,352)	(99,343)
Accumulated other comprehensive income, net of tax	599	626

Total stockholders’ equity	155,856	144,777
Total liabilities and stockholders’ equity	$ 1,248,330	$ 1,260,917

The accompanying notes are an integral part of these condensed consolidated financial statements.

1

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Operations
(Unaudited)
In Thousands, Except Per Share Information

	Quarter Ended December 31,		Six Months Ended December 31,	
	2012	2011	2012	2011
Interest income:				
Loans receivable, net	$ 11,286	$ 13,261	$ 22,919	$ 26,010
Investment securities	110	134	224	281
FHLB – San Francisco stock	137	20	164	38
Interest-earning deposits	84	37	157	134
Total interest income	11,617	13,452	23,464	26,463
Interest expense:				
Checking and money market deposits	112	176	210	376
Savings deposits	144	191	292	416
Time deposits	1,449	1,824	2,973	3,730
Borrowings	1,140	1,755	2,281	3,637
Total interest expense	2,845	3,946	5,756	8,159
Net interest income, before provision for loan losses	8,772	9,506	17,708	18,304
Provision for loan losses	23	1,132	556	2,104
Net interest income, after provision for loan losses	8,749	8,374	17,152	16,200
Non-interest income:				
Loan servicing and other fees	382	176	720	308
Gain on sale of loans, net	17,878	5,897	38,473	13,173
Deposit account fees	617	626	1,240	1,229
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	595	77	668	109
Card and processing fees	315	309	636	640
Other	248	228	457	402
Total non-interest income	20,035	7,313	42,194	15,861
Non-interest expense:				
Salaries and employee benefits	12,671	8,380	25,856	17,234
Premises and occupancy	1,100	956	2,250	1,828
Equipment	422	410	863	724
Professional expenses	453	455	806	888
Sales and marketing expenses	416	178	836	377
Deposit insurance premiums and regulatory assessments	303	461	642	632
Other	1,404	1,634	2,842	3,094
Total non-interest expense	16,769	12,474	34,095	24,777
Income before income taxes	12,015	3,213	25,251	7,284
Provision for income taxes	5,075	1,359	9,581	3,112

Net income	$ 6,940	$ 1,854	$ 15,670	$ 4,172
Basic earnings per share	$ 0.65	$ 0.16	$ 1.46	$ 0.37
Diluted earnings per share	$ 0.64	$ 0.16	$ 1.43	$ 0.36
Cash dividends per share	$ 0.05	$ 0.03	$ 0.10	$ 0.06

The accompanying notes are an integral part of these condensed consolidated financial statements.

2

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(Unaudited)
In Thousands
For the Quarters and Six Months Ended December 31, 2012 and 2011

	For the Quarters Ended December 31,		For the Six Months Ended December 31,	
	2012	2011	2012	2011
Net income	$ 6,940	$ 1,854	$ 15,670	$ 4,172
Change in unrealized holding loss on securities available for sale	(45)	(72)	(47)	(147)
Reclassification of (gains) losses to net income	-	-	-	-
Other comprehensive loss, before income tax benefit	(45)	(72)	(47)	(147)
Income tax benefit	19	30	20	62
Other comprehensive loss	(26)	(42)	(27)	(85)
Total comprehensive income	$ 6,914	$ 1,812	$ 15,643	$ 4,087

The accompanying notes are an integral part of these condensed consolidated financial statements.

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)
In Thousands, Except Share Information
For the Quarters Ended December 31, 2012 and 2011

	Common Stock Shares	Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income, Net of Tax	Total
Balance at October 1, 2012	10,690,585	$ 176	$ 87,173	$ 164,748	$ (101,904)	$ 625	$ 150,818
Net income				6,940			6,940
Other comprehensive loss						(26)	(26)
Purchase of treasury stock	(93,580)				(1,448)		(1,448)
Amortization of restricted stock			52				52
Stock options expense			53				53
Cash dividends				(533)			(533)
Balance at December 31, 2012	10,597,005	$ 176	$ 87,278	$ 171,155	$ (103,352)	$ 599	$ 155,856

	Common Stock Shares	Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income, Net of Tax	Total
Balance at October 1, 2011	11,439,264	$ 176	$ 86,021	$ 149,295	$ (93,316)	$ 595	$ 142,771
Net income				1,854			1,854
Other comprehensive loss						(42)	(42)
Purchase of treasury stock (1)	(263,503)				(2,441)		(2,441)
Amortization of restricted stock			115				115
Stock options expense			129				129
Cash dividends				(341)			(341)
Balance at December 31, 2011	11,175,761	$ 176	$ 86,265	$ 150,808	$ (95,757)	$ 553	$ 142,045

The accompanying notes are an integral part of these condensed consolidated financial statements.

4

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)
In Thousands, Except Share Information
For the Six Months Ended December 31, 2012 and 2011

	Common Stock Shares	Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income, Net of Tax	Total
Balance at July 1, 2012	10,856,027	$ 176	$ 86,758	$ 156,560	$ (99,343)	$ 626	$ 144,777
Net income				15,670			15,670
Other comprehensive loss						(27)	(27)
Purchase of treasury stock	(287,822)				(3,996)		(3,996)
Exercise of stock options	28,000		197				197
Distribution of restricted stock	800						-
Amortization of restricted stock			105				105
Forfeitures of restricted stock			13		(13)		-
Stock options expense			134				134
Tax benefit from non-qualified equity compensation			71				71
Cash dividends				(1,075)			(1,075)
Balance at December 31, 2012	10,597,005	$ 176	$ 87,278	$ 171,155	$ (103,352)	$ 599	$ 155,856

	Common Stock Shares	Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income, Net of Tax	Total
Balance at July 1, 2011	11,418,654	$ 176	$ 85,432	$ 147,322	$) (92,650	$ 638	$ 140,918
Net income				4,172			4,172
Other comprehensive loss						(85)	(85)
Purchase of treasury stock (1)	(343,193)				(3,107)		(3,107)
Distribution of restricted stock	100,300						-
Amortization of restricted stock			417				417
Stock options expense			416				416

Cash dividends				(686)			(686)
Balance at December 31, 2011	11,175,761	$ 176	$ 86,265	$ 150,808	$ (95,757)	$ 553	$ 142,045

(1) Includes the repurchase of 11,523 shares of distributed restricted stock.

The accompanying notes are an integral part of these condensed consolidated financial statements.

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited - In Thousands)

	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011
Cash flows from operating activities:		
Net income	$ 15,670	$ 4,172
Adjustments to reconcile net income to net cash used for operating activities:		
Depreciation and amortization	848	792
Provision for loan losses	556	2,104
Recovery of losses on real estate owned	(118)	(673)
Gain on sale of loans, net	(38,473)	(13,173)
(Gain) loss on sale of real estate owned, net	(746)	135
Stock-based compensation	239	833
(Increase) decrease in current and deferred income taxes	(1,835)	2,193
Tax benefit from non-qualified equity compensation	(71)	-
Increase in cash surrender value of the bank owned life insurance	(95)	(95)
Increase in accounts payable and other liabilities	2,684	1,680
(Increase) decrease in prepaid expenses and other assets	(1,177)	524
Loans originated for sale	(1,869,290)	(1,197,004)
Proceeds from sale of loans	1,844,726	1,177,706
Net cash used for operating activities	(47,082)	(20,806)
Cash flows from investing activities:		
Decrease in loans held for investment, net	18,876	25,527
Principal payments from investment securities available for sale	1,667	1,983
Redemption of FHLB – San Francisco stock	3,106	2,391
Proceeds from sale of real estate owned	9,365	9,143
Purchase of premises and equipment	(399)	(1,552)
Net cash provided by investing activities	32,615	37,492
Cash flows from financing activities:		
(Decrease) increase in deposits, net	(26,205)	8,089
Repayments of long-term borrowings	(27)	(30,025)
Exercise of stock options	197	-
Tax benefit from non-qualified equity compensation	71	-
Cash dividends	(1,075)	(686)
Treasury stock purchases	(3,996)	(3,107)
Net cash used for financing activities	(31,035)	(25,729)
Net decrease in cash and cash equivalents	(45,502)	(9,043)
Cash and cash equivalents at beginning of period	145,136	142,550
Cash and cash equivalents at end of period	$ 99,634	$ 133,507
Supplemental information:		
Cash paid for interest	$ 5,750	$ 8,292

Cash paid for income taxes	$ 11,345	$ 900
Transfer of loans held for sale to held for investment	$ 1,881	$ 1,336
Real estate acquired in the settlement of loans	$ 6,776	$ 12,085

The accompanying notes are an integral part of these condensed consolidated financial statements.

6

PROVIDENT FINANCIAL HOLDINGS, INC.
NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2012

Note 1: Basis of Presentation

The unaudited interim condensed consolidated financial statements included herein reflect all adjustments which are, in the opinion of management, necessary to present a fair statement of the results of operations for the interim periods presented. All such adjustments are of a normal, recurring nature. The condensed consolidated statements of financial condition at June 30, 2012 are derived from the audited consolidated financial statements of Provident Financial Holdings, Inc. and its wholly-owned subsidiary, Provident Savings Bank, F.S.B. (the “Bank”) (collectively, the “Corporation”). Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) with respect to interim financial reporting. It is recommended that these unaudited interim condensed consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto included in the Corporation’s Annual Report on Form 10-K for the year ended June 30, 2012. The results of operations for the quarter and six months ended December 31, 2012 are not necessarily indicative of results that may be expected for the entire fiscal year ending June 30, 2013.

Note 2: Accounting Standard Updates (“ASU”)

ASU 2011-11:
In December 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Updates (“ASU”) 2011-11, “Balance Sheet (Topic 210) - Disclosures about Offsetting Assets and Liabilities.” The amendments in this ASU will enhance disclosures required by GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. This information will enable users of an entity’s financial statements to evaluate the effect or potential effect of netting arrangements on an entity’s financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this ASU. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The Corporation has not determined the impact of this ASU on the Corporation’s consolidated financial statements.

Note 3: Earnings Per Share

Basic earnings per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would then share in the earnings of the entity.

As of December 31, 2012 and 2011, there were outstanding options to purchase 1,138,500 shares and 1,187,000 shares of the Corporation's common stock, respectively, of which 586,500 shares and 594,000 shares, respectively, were excluded from the diluted EPS computation as their effect was anti-dilutive.

The following table provides the basic and diluted EPS computations for the quarters and six months ended December 31, 2012 and 2011, respectively.

(In Thousands, Except Earnings Per Share)	For the Quarter Ended December 31,		For the Six Months Ended December 31,	
	2012	2011	2012	2011
Numerator:				
Net income – numerator for basic earnings per share and diluted earnings per share - available to common stockholders	$ 6,940	$ 1,854	$ 15,670	$ 4,172
Denominator:				
Denominator for basic earnings per share:				
Weighted-average shares	10,654	11,353	10,727	11,410
Effect of dilutive securities	211	31	191	39
Denominator for diluted earnings per share:				
Adjusted weighted-average shares and assumed conversions	10,865	11,384	10,918	11,449
Basic earnings per share	$ 0.65	$ 0.16	$ 1.46	$ 0.37
Diluted earnings per share	$ 0.64	$ 0.16	$ 1.43	$ 0.36

Note 4: Operating Segment Reports

The Corporation operates in two business segments: community banking through the Bank and mortgage banking through Provident Bank Mortgage ("PBM"), a division of the Bank.

The following tables set forth condensed consolidated statements of operations and total assets for the Corporation's operating segments for the quarters ended December 31, 2012 and 2011, respectively (in thousands).

	For the Quarter Ended December 31, 2012		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income, before provision for loan losses	$ 7,144	$ 1,628	$ 8,772
(Recovery) provision for loan losses	(35)	58	23
Net interest income, after (recovery) provision for loan losses	7,179	1,570	8,749
Non-interest income:			
Loan servicing and other fees (1)	347	35	382
(Loss) gain on sale of loans, net (2)	(37)	17,915	17,878
Deposit account fees	617	-	617
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	587	8	595
Card and processing fees	315	-	315
Other	248	-	248
Total non-interest income	2,077	17,958	20,035
Non-interest expense:			
Salaries and employee benefits	4,239	8,432	12,671
Premises and occupancy	668	432	1,100
Operating and administrative expenses	1,109	1,889	2,998
Total non-interest expense	6,016	10,753	16,769
Income before income taxes	3,240	8,775	12,015
Provision for income taxes	1,386	3,689	5,075
Net income	$ 1,854	$ 5,086	$ 6,940
Total assets, end of period	$ 959,612	$ 288,718	$ 1,248,330

(1) Includes an inter-company charge of $11 credited to PBM by the Bank during the period to compensate PBM for originating loans held for investment.
(2) Includes an inter-company charge of $25 credited to PBM by the Bank during the period to compensate PBM for servicing fees on loans sold on a servicing retained basis.

	For the Quarter Ended December 31, 2011		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income, before provision for loan losses	$ 7,640	$ 1,866	$ 9,506
Provision for loan losses	1,082	50	1,132
Net interest income after provision for loan losses	6,558	1,816	8,374
Non-interest income:			
Loan servicing and other fees (1)	160	16	176
(Loss) gain on sale of loans, net (2)	(626)	6,523	5,897
Deposit account fees	626	-	626
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	69	8	77
Card and processing fees	309	-	309
Other	228	-	228
Total non-interest income	766	6,547	7,313
Non-interest expense:			
Salaries and employee benefits	3,264	5,116	8,380
Premises and occupancy	676	280	956
Operating and administrative expenses	1,417	1,721	3,138
Total non-interest expense	5,357	7,117	12,474
Income before income taxes	1,967	1,246	3,213
Provision for income taxes	835	524	1,359
Net income	$ 1,132	$ 722	$ 1,854
Total assets, end of period	$ 1,076,170	$ 221,564	$ 1,297,734

(1) There was no inter-company charge credited to PBM by the Bank during the period to compensate PBM for originating loans held for investment.

(2) Includes an inter-company charge of $26 credited to PBM by the Bank during the period to compensate PBM for servicing fees on loans sold on a servicing retained basis.

The following tables set forth condensed consolidated statements of operations and total assets for the Corporation's operating segments for the six months ended December 31, 2012 and 2011, respectively (in thousands).

	For the Six Months Ended December 31, 2012		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income, before provision for loan losses	$ 14,477	$ 3,231	$ 17,708
Provision (recovery) for loan losses	820	(264)	556
Net interest income, after provision (recovery) for loan losses	13,657	3,495	17,152
Non-interest income:			
Loan servicing and other fees (1)	650	70	720
(Loss) gain on sale of loans, net (2)	(8)	38,481	38,473
Deposit account fees	1,240	-	1,240
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	661	7	668
Card and processing fees	636	-	636
Other	457	-	457
Total non-interest income	3,636	38,558	42,194
Non-interest expense:			
Salaries and employee benefits	8,996	16,860	25,856
Premises and occupancy	1,408	842	2,250
Operating and administrative expenses	2,280	3,709	5,989
Total non-interest expense	12,684	21,411	34,095
Income before taxes	4,609	20,642	25,251
Provision for income taxes	902	8,679	9,581
Net income	$ 3,707	$ 11,963	$ 15,670
Total assets, end of period	$ 959,612	$ 288,718	$ 1,248,330

(1) Includes an inter-company charge of $27 credited to PBM by the Bank during the period to compensate PBM for originating loans held for investment.

(2) Includes an inter-company charge of $66 credited to PBM by the Bank during the period to compensate PBM for servicing fees on loans sold on a servicing retained basis.

	For the Six Months Ended December 31, 2011		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income, before provision for loan losses	$ 15,198	$ 3,106	$ 18,304
Provision for loan losses	1,791	313	2,104
Net interest income, after provision for loan losses	13,407	2,793	16,200
Non-interest income:			
Loan servicing and other fees (1)	279	29	308
(Loss) gain on sale of loans, net (2)	(619)	13,792	13,173
Deposit account fees	1,229	-	1,229
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	37	72	109
Card and processing fees	640	-	640
Other	402	-	402
Total non-interest income	1,968	13,893	15,861
Non-interest expense:			
Salaries and employee benefits	7,453	9,781	17,234
Premises and occupancy	1,273	555	1,828
Operating and administrative expenses	2,357	3,358	5,715
Total non-interest expense	11,083	13,694	24,777
Income before taxes	4,292	2,992	7,284
Provision for income taxes	1,854	1,258	3,112
Net income	$ 2,438	$ 1,734	$ 4,172
Total assets, end of period	$ 1,076,170	$ 221,564	$ 1,297,734

(1) There was no inter-company charge credited to PBM by the Bank during the period to compensate PBM for originating loans held for investment.

(2) Includes an inter-company charge of $59 credited to PBM by the Bank during the period to compensate PBM for servicing fees on loans sold on a servicing retained basis.

Note 5: Investment Securities

The amortized cost and estimated fair value of investment securities as of December 31, 2012 and June 30, 2012 were as follows:

December 31, 2012 (In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Carrying Value

Available for sale					
U.S. government agency MBS (1)	$ 11,157	$ 443	$ -	$ 11,600	$ 11,600
U.S. government sponsored enterprise MBS	7,960	468	-	8,428	8,428
Private issue CMO (2)	1,162	-	(6)	1,156	1,156
Total investment securities	$ 20,279	$ 911	$ (6)	$ 21,184	$ 21,184

(1) Mortgage-Backed Securities ("MBS").
(2) Collateralized Mortgage Obligations ("CMO").

June 30, 2012 (In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Carrying Value
Available for sale					
U.S. government agency MBS	$ 11,854	$ 460	$ -	$ 12,314	$ 12,314
U.S. government sponsored enterprise MBS	8,850	492	-	9,342	9,342
Private issue CMO	1,243	4	(5)	1,242	1,242
Total investment securities	$ 21,947	$ 956	$ (5)	$ 22,898	$ 22,898

In the second quarter of fiscal 2013 and 2012, the Corporation received MBS principal payments of $905,000 and $1.1 million, respectively, and did not purchase or sell investment securities. For the first six months of fiscal 2013 and 2012, the Corporation received MBS principal payments of $1.7 million and $2.0 million, respectively, and did not purchase or sell investment securities.

The Corporation evaluates individual investment securities quarterly for other-than-temporary declines in market value. As of December 31, 2012 and June 30, 2012, the gross unrealized holding losses relate to one adjustable rate private issue CMO which has been in an unrealized loss position for more than 12 months. The unrealized holding losses were primarily the result of perceived credit and liquidity concerns of privately issued CMO investment securities. Based on the nature of the investments, management concluded that such unrealized losses were not other than temporary as of December 31, 2012 and June 30, 2012. The Corporation does not believe that there are any other-than-temporary impairments at December 31, 2012 and 2011; therefore, no impairment losses have been recorded for the quarter ended December 31, 2012 and 2011. The Corporation intends and has the ability to hold these CMO investment securities until maturity and will not likely be required to sell the CMO investment securities before realizing a full recovery.

Contractual maturities of investment securities as of December 31, 2012 and June 30, 2012 were as follows:

	December 31, 2012		June 30, 2012	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Available for sale				
Due in one year or less	$ -	$ -	$ -	$ -
Due after one through five years	-	-	-	-
Due after five through ten years	-	-	-	-
Due after ten years	20,279	21,184	21,947	22,898
Total investment securities	$ 20,279	$ 21,184	$ 21,947	$ 22,898

Note 6: Loans Held for Investment

Loans held for investment consisted of the following:

		December 31, 2012	June 30, 2012
Mortgage loans:			
	Single-family	$ 422,457	$ 439,024
	Multi-family	261,580	278,057
	Commercial real estate	101,621	95,302
	Other	390	755
Commercial business loans		2,199	2,580
Consumer loans		383	506
	Total loans held for investment, gross	788,630	816,224
Deferred loan costs, net		1,957	2,095
Allowance for loan losses		(18,530)	(21,483)
	Total loans held for investment, net	$ 772,057	$ 796,836

As of December 31, 2012, the Corporation had $36.4 million in mortgage loans that are subject to negative amortization, consisting of $25.6 million in multi-family loans, $5.8 million in single-family loans and $5.0 million in commercial real estate loans. This compares to $40.2 million of negative amortization mortgage loans at June 30, 2012, consisting of $26.7 million in multi-family loans, $6.5 million in single-family loans and $7.0 million in commercial real estate loans. During the second quarter of fiscal 2013 and 2012, no loan interest income was added to the negative amortization loan balance. For the first six months of fiscal 2013, no loan interest income was added to the negative amortization loan balance, as compared to $13,000 of loan interest income in the comparable period of fiscal 2012. Negative amortization involves a greater risk to the Corporation because the loan principal balance may increase by a range of 110% to 115% of the original loan amount during the period of negative amortization and because the loan payment may increase beyond the means of the borrower when loan principal amortization is required. Also, the Corporation has originated interest-only ARM loans, which typically have a fixed interest rate for the first two to five years coupled with an interest only payment, followed by a periodic adjustable rate and a fully amortizing loan payment. As of December 31, 2012 and June 30, 2012, the interest-only ARM loans were $201.9 million and $214.2 million, or 25.6% and 26.2% of loans held for investment, respectively.

The following table sets forth information at December 31, 2012 regarding the dollar amount of loans held for investment that are contractually repricing during the periods indicated, segregated between adjustable rate loans and fixed rate loans. Fixed-rate loans comprised 5% of loans held for investment at December 31, 2012, unchanged from June 30, 2012. Adjustable rate loans having no stated repricing dates that reprice when the index they are tied to reprices (e.g. prime rate index) and checking account overdrafts are reported as repricing within one year. The table does not include any estimate of prepayments which may cause the Corporation's actual repricing experience to differ materially from that shown.

	Adjustable Rate					
(In Thousands)	Within One Year	After One Year Through 3 Years	After 3 Years Through 5 Years	After 5 Years Through 10 Years	Fixed Rate	Total

Mortgage loans:						
Single-family	$ 382,617	$ 17,907	$ 8,605	$ 1,834	$ 11,494	$ 422,457
Multi-family	162,736	14,039	67,035	6,118	11,652	261,580
Commercial real estate	57,821	2,461	17,991	8,311	15,037	101,621
Other	159	-	-	-	231	390
Commercial business loans	988	-	-	-	1,211	2,199
Consumer loans	363	-	-	-	20	383
Total loans held for investment, gross	$ 604,684	$ 34,407	$ 93,631	$ 16,263	$ 39,645	$ 788,630

The allowance for loan losses is maintained at a level sufficient to provide for estimated losses based on evaluating known and inherent risks in the loans held for investment and upon management's continuing analysis of the factors underlying the quality of the loans held for investment. These factors include changes in the size and composition of the loans held for investment, actual loan loss experience, current economic conditions, detailed analysis of individual loans for which full collectability may not be assured, and determination of the realizable value of the collateral securing the loans. Provisions for loan losses are charged against operations on a quarterly basis, as necessary, to maintain the allowance at appropriate levels. Although management believes it uses the best information available to make such determinations, there can be no assurance that regulators, in reviewing the Corporation's loans held for investment, will not request the Corporation to significantly increase its allowance for loan losses. Future adjustments to the allowance for loan losses may be necessary and results of operations could be significantly and adversely affected as a result of economic, operating, regulatory, and other conditions beyond the Corporation's control.

In compliance with the regulatory reporting requirements of the Office of the Comptroller of the Currency ("OCC"), the Bank's primary federal regulator, non-performing loans are charged-off to their fair market values in the period the loans, or portion thereof, are deemed uncollectible, generally after the loan becomes 150 days delinquent for real estate secured first trust deed loans and 120 days delinquent for commercial business or real estate secured second trust deed loans. For loans that were modified from their original terms, were re-underwritten and identified in the Corporation's asset quality reports as troubled debt restructurings ("restructured loans"), the charge-off occurs when the loan becomes 90 days delinquent; and where borrowers file bankruptcy, the charge-off occurs when the loan becomes 60 days delinquent. The amount of the charge-off is determined by comparing the loan balance to the estimated fair value of the underlying collateral, less disposition costs, with the loan balance in excess of the estimated fair value charged-off against the allowance for loan losses. The allowance for loan losses for non-performing loans is determined by applying Accounting Standards Codification ("ASC") 310, "Receivables,". For restructured loans that are less than 90 days delinquent, the allowance for loan losses are segregated into (a) individually evaluated allowances for those loans with applicable discounted cash flow calculations or (b) collectively evaluated allowances based on the aggregated pooling method. For non-performing loans less than 60 days delinquent where the borrower has filed bankruptcy, the collectively evaluated allowances are assigned based on the aggregated pooling method.

The following tables summarize the Corporation's allowance for loan losses at December 31, 2012 and June 30, 2012:

(In Thousands)	December 31, 2012	June 30, 2012
Collectively evaluated for impairment:		
Mortgage loans:		
Single-family	$ 12,201	$ 15,189
Multi-family	3,660	3,524
Commercial real estate	1,852	1,810
Other	7	7
Commercial business loans	101	169
Consumer loans	13	13
Total collectively evaluated allowance	17,834	20,712
Individually evaluated for impairment:		
Mortgage loans:		
Single-family	503	744
Multi-family	27	27

Other	159	-
Commercial business loans	7	-
Total individually evaluated allowance	696	771
Total loan loss allowance	$ 18,530	$ 21,483

The following table is provided to disclose additional details on the Corporation's allowance for loan losses (dollars in thousands):

(Dollars in Thousands)	For the Quarter Ended December 31, 2012	For the Quarter Ended December 31, 2011	For the Six Months Ended December 31, 2012	For the Six Months Ended December 31, 2011
Allowance at beginning of period	$ 20,118	$ 28,704	$ 21,483	$ 30,482
Provision for loan losses	23	1,132	556	2,104
Recoveries:				
Mortgage loans:				
Single-family	93	191	163	304
Consumer loans	1	-	2	-
Total recoveries	94	191	165	304
Charge-offs:				
Mortgage loans:				
Single-family	(1,704)	(3,101)	(3,671)	(5,962)
Multi-family	-	-	-	-
Consumer loans	(1)	(25)	(3)	(27)
Total charge-offs	(1,705)	(3,126)	(3,674)	(5,989)
Net charge-offs	(1,611)	(2,935)	(3,509)	(5,685)
Balance at end of period	$ 18,530	$ 26,901	$ 18,530	$ 26,901
Allowance for loan losses as a percentage of gross loans held for investment	2.34 %	3.08 %	2.34 %	3.08 %
Net charge-offs as a percentage of average loans outstanding during the period (annualized)	0.62 %	1.02 %	0.67 %	1.03 %
Allowance for loan losses as a percentage of gross non-performing loans at the end of the period	64.40 %	62.71 %	64.40 %	62.71 %

The following tables identify the Corporation's total recorded investment in non-performing loans by type, net of allowance for loan losses at December 31, 2012 and June 30, 2012:

(In Thousands)	Recorded Investment	December 31, 2012 Allowance for Loan Losses (1)	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 12,513	$ (3,078)	$ 9,435
Without a related allowance (2)	8,950	-	8,950
Total single-family loans	21,463	(3,078)	18,385
Multi-family:			
With a related allowance	1,988	(397)	1,591
Total multi-family loans	1,988	(397)	1,591
Commercial real estate:			
With a related allowance	4,958	(744)	4,214
Total commercial real estate loans	4,958	(744)	4,214
Other:			
With a related allowance	159	(159)	-
Total other loans	159	(159)	-
Commercial business loans:			
With a related allowance	204	(29)	175
Total commercial business loans	204	(29)	175
Total non-performing loans	$ 28,772	$ (4,407)	$ 24,365

(1) Consists of collectively and individually evaluated allowances, specifically assigned to the individual loan.
(2) There was no related allowance for loan losses because the loans have been charged-off to their fair value and/or the fair value of the collateral is higher than the loan balance.

(In Thousands)		Recorded Investment	June 30, 2012 Allowance for Loan Losses (1)	Net Investment
Mortgage loans:				
Single-family:				
	With a related allowance	$ 26,214	$ (5,476)	$ 20,738
	Without a related allowance (2)	8,352	-	8,352
Total single-family loans		34,566	(5,476)	29,090
Multi-family:				
	With a related allowance	1,806	(349)	1,457
Total multi-family loans		1,806	(349)	1,457
Commercial real estate:				
	With a related allowance	3,820	(573)	3,247
Total commercial real estate loans		3,820	(573)	3,247
Other:				
	Without a related allowance (2)	522	-	522
Total other loans		522	-	522
Commercial business loans:				
	With a related allowance	246	(74)	172
Total commercial business loans		246	(74)	172
Total non-performing loans		$ 40,960	$ (6,472)	$ 34,488

(1) Consists of collectively and individually evaluated allowances, specifically assigned to the individual loan.
(2) There was no related allowance for loan losses because the loans have been charged-off to their fair value and/or the fair value of the collateral is higher than the loan balance.

At December 31, 2012 and June 30, 2012, there were no commitments to lend additional funds to those borrowers whose loans were classified as non-performing.

The following table describes the aging analysis (length of time on non-performing status) of non-performing loans, net of allowance for loan losses, as of December 31, 2012:

(In Thousands)	3 Months or Less	Over 3 to 6 Months	Over 6 to 12 Months	Over 12 Months	Total
Mortgage loans:					
Single-family	$ 5,406	$ 1,694	$ 3,517	$ 7,768	$ 18,385
Multi-family	194	-	917	480	1,591
Commercial real estate	214	1,271	2,729	-	4,214
Commercial business loans	-	-	150	25	175
Total	$ 5,814	$ 2,965	$ 7,313	$ 8,273	$ 24,365

For the quarters ended December 31, 2012 and 2011, the Corporation's average investment in non-performing loans was $26.2 million and $35.3 million, respectively. The Corporation records payments on non-performing loans utilizing the cash basis or cost recovery method of accounting during the periods when the loans are on non-performing status. For the quarters ended December 31, 2012 and 2011, interest income of $1.5 million and $1.5 million, respectively, was recognized, based on cash receipts from loan payments on non-performing loans. Foregone interest income, which would have been recorded had the non-performing loans been current in accordance with their original terms, amounted to $145,000 and $261,000 for the quarters ended December 31, 2012 and 2011, respectively, and was not included in the results of operations.

For the six months ended December 31, 2012 and 2011, the Corporation's average investment in non-performing loans was $27.7 million and $36.0 million, respectively. For the six months ended December 31, 2012 and 2011, interest income of $3.0 million and $3.1 million, respectively, was recognized, based on cash receipts from loan payments on non-performing loans. Foregone interest income amounted to $246,000 and $574,000 for the quarters ended December 31, 2012 and 2011, respectively, and was not included in the results of operations.

For the quarter ended December 31, 2012, there were no new loans that were modified from their original terms, re-underwritten or identified in the Corporation's asset quality reports as restructured loans. For the quarter ended December 31, 2011, four loans for $1.0 million were re-underwritten and identified as restructured loans during the quarter ended December 31, 2011. During the quarter ended December 31, 2012 and 2011, no restructured loans were in default within a 12-month period subsequent to their original restructuring. Additionally, during the quarter ended December 31, 2012, there was one loan for $131,000 whose modification was extended beyond the initial maturity of the modification. For the quarter ended December 31, 2011, four loans for $3.0 million had their modification extended beyond the initial maturity of the modification.

For the six months ended December 31, 2012, there were no new loans that were modified from their original terms, re-underwritten or identified in the Corporation's asset quality reports as restructured loans. This compares to 16 loans for $5.8 million that were re-underwritten and identified as restructured loans during the six months ended December 31, 2011. During the six months ended December 31, 2012, one restructured loan with a balance of $437,000 was in default within a 12-month period subsequent to its original restructuring and required an additional provision of $226,000. This compares to two restructured loans with a total balance of $771,000 during the six months ended December 31, 2011 that were in default within a 12-month period subsequent to their original restructuring and required an additional provision of $200,000. Additionally, during the six months ended December 31, 2012, there was one loan for $131,000 whose modification was extended beyond the initial maturity of the modification. For the six months ended December 31, 2011, five loans for $3.2 million had their modification extended beyond the initial maturity of the modification.

As of December 31, 2012, the net outstanding balance of the 42 restructured loans was $18.1 million: six were classified in accordance with the Corporation's risk rating system as pass and remain on accrual status ($2.7 million); four were classified as special mention and remain on accrual status ($1.7 million); and 32 were classified as substandard ($13.6 million total, with 31 of the 32 loans or $10.8 million on non-accrual status). Substandard assets have one or more defined weaknesses and are characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. Assets that do not currently expose the Corporation to sufficient risk to warrant adverse classification but possess weaknesses are designated as special mention and are closely monitored by the Corporation. As of December 31, 2012, $9.8 million, or 54 percent, of the restructured loans were current with respect to their payment status.

The Corporation upgrades restructured single-family loans to the pass category if the borrower has demonstrated satisfactory contractual payments for at least six consecutive months; 12 months for those loans that were restructured more than once; and if the borrower has demonstrated satisfactory contractual payments beyond 12 consecutive months, the loan is no longer categorized as a restructured loan for the United States Securities and Exchange Commission ("SEC") reporting purposes. In addition to the payment history described above, multi-family, commercial real estate, construction and commercial business loans (which are sometimes referred to in this report as "preferred loans") must also demonstrate a combination of the following characteristics to be upgraded: satisfactory cash flow, satisfactory guarantor support, and additional collateral support, among others.

To qualify for restructuring, a borrower must provide evidence of their creditworthiness such as, current financial statements, their most recent income tax returns, current paystubs, current W-2s, and most recent bank statements, among other documents, which are then verified by the Corporation. The Corporation re-underwrites the loan with the borrower's updated financial information, new credit report, current loan balance, new interest rate, remaining loan term, updated property value and modified payment schedule, among other considerations, to determine if the borrower qualifies.

The following table summarizes at the dates indicated the restructured loan balances, net of allowance for loan losses, by loan type and non-accrual versus accrual status:

(In Thousands)	December 31, 2012	June 30, 2012
Restructured loans on non-accrual status:		
Mortgage loans:		
Single-family	$ 7,708	$ 11,995
Multi-family	480	490
Commercial real estate	2,477	2,483
Other	-	522
Commercial business loans	168	165
Total	10,833	15,655
Restructured loans on accrual status:		
Mortgage loans:		
Single-family	4,252	6,148
Multi-family	2,755	3,266
Other	232	-
Commercial business loans	-	33
Total	7,239	9,447
Total restructured loans	$ 18,072	$ 25,102

The following table shows the restructured loans by type, net of allowance for loan losses, at December 31, 2012 and June 30, 2012:

	December 31, 2012		
(In Thousands)	Recorded Investment	Allowance for Loan Losses (1)	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 3,466	$ (372)	$ 3,094
Without a related allowance (2)	8,866	-	8,866
Total single-family loans	12,332	(372)	11,960
Multi-family:			
With a related allowance	506	(26)	480
Without a related allowance (2)	2,755	-	2,755
Total multi-family loans	3,261	(26)	3,235
Commercial real estate:			
With a related allowance	2,914	(437)	2,477
Total commercial real estate loans	2,914	(437)	2,477

Other:			
With a related allowance	159	(159)	-
Without a related allowance (2)	232	-	232
Total other loans	391	(159)	232
Commercial business loans:			
With a related allowance	195	(27)	168
Total commercial business loans	195	(27)	168
Total restructured loans	$ 19,093	$ (1,021)	$ 18,072

(1) Consists of collectively and individually evaluated allowances, specifically assigned to the individual loan.

(2) There was no related allowance for loan losses because the loans have been charged-off to their fair value and/or the fair value of the collateral is higher than the loan balance.

(In Thousands)	June 30, 2012 Recorded Investment	Allowance for Loan Losses (1)	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 9,465	$ (486)	$ 8,979
Without a related allowance (2)	9,164	-	9,164
Total single-family loans	18,629	(486)	18,143
Multi-family:			
With a related allowance	517	(27)	490
Without a related allowance (2)	3,266	-	3,266
Total multi-family loans	3,783	(27)	3,756
Commercial real estate:			
With a related allowance	2,921	(438)	2,483
Total commercial real estate loans	2,921	(438)	2,483
Other:			
Without a related allowance (2)	522	-	522
Total other loans	522	-	522
Commercial business loans:			
With a related allowance	236	(71)	165
Without a related allowance (2)	33	-	33
Total commercial business loans	269	(71)	198
Total restructured loans	$ 26,124	$ (1,022)	$ 25,102

(1) Consists of collectively and individually evaluated allowances, specifically assigned to the individual loan.
(2) There was no related allowance for loan losses because the loans have been charged-off to their fair value and/or the fair value of the collateral is higher than the loan balance.

During the quarter ended December 31, 2012, five properties were acquired in the settlement of loans, while 11 previously foreclosed upon properties were sold. For the six months ended December 31, 2012, sixteen properties were acquired in the settlement of loans, while 28 previously foreclosed upon properties were sold. As of December 31, 2012, real estate owned was comprised of 12 properties with a net fair value of $2.4 million, primarily located in Southern California. This compares to 24 real estate owned properties, primarily located in Southern California, with a net fair value of $5.5 million at June 30, 2012. A new appraisal was obtained on each of the properties at the time of foreclosure and fair value was calculated by using the lower of the appraised value or the listing price of the property, net of disposition costs. Any initial loss was recorded as a charge to the allowance for loan losses before being transferred to real estate owned. Subsequently, if there is further deterioration in real estate values, specific real estate owned loss reserves are established and charged to the statement of operations. In addition, the Corporation records costs to carry real estate owned as real estate operating expenses as incurred.

Note 7: Derivative and Other Financial Instruments with Off-Balance Sheet Risks

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit in the form of originating loans or providing funds under existing lines of credit, loan sale commitments to third parties and option contracts. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the accompanying Condensed Consolidated Statements of Financial Condition. The Corporation's exposure to credit loss, in the event of non-performance by the counterparty to these financial instruments, is represented by the contractual amount of these instruments. The Corporation uses the same credit policies in entering into financial instruments with off-balance sheet risk as it does for on-balance sheet instruments. As of December 31, 2012 and June 30, 2012, the Corporation had commitments to extend credit (on loans to be held for investment and loans to be held for sale) of $224.1 million and $222.1 million, respectively.

The following table provides information at the dates indicated regarding undisbursed funds to borrowers on existing lines of credit with the Corporation as well as commitments to originate loans to be held for investment for the quarter ended December 31, 2012 and 2011.

Commitments (In Thousands)	December 31, 2012	June 30, 2012
Undisbursed lines of credit – Mortgage loans	$ 834	$ 1,028
Undisbursed lines of credit – Commercial business loans	1,126	1,340
Undisbursed lines of credit – Consumer loans	793	863
Commitments to extend credit on loans to be held for investment	2,152	1,720
Total	$ 4,905	$ 4,951

In accordance with ASC 815, “Derivatives and Hedging,” and interpretations of the Derivatives Implementation Group of the FASB, the fair value of the commitments to extend credit on loans to be held for sale, loan sale commitments, to be announced (“TBA”) MBS trades, put option contracts and call option contracts are recorded at fair value on the Condensed Consolidated Statements of Financial Condition. At December 31, 2012, $3.3 million was included in other assets and $332,000 was included in other liabilities; at June 30, 2012, $4.0 million was included in other assets and $1.3 million was included in other liabilities. The Corporation does not apply hedge accounting to its derivative financial instruments; therefore, all changes in fair value are recorded in earnings.

The following table provides information regarding the allowance for loan losses for the undisbursed funds and commitments to extend credit on loans to be held for investment for the quarters and six months ended December 31, 2012 and 2011.

	For the Quarters Ended December 31,		For the Six Months Ended December 31,	
(In Thousands)	2012	2011	2012	2011
Balance, beginning of the period	$ 66	$ 93	$ 66	$ 94
Recovery	(3)	(21)	(3)	(22)
Balance, end of the period	$ 63	$ 72	$ 63	$ 72

The net impact of derivative financial instruments on the gain on sale of loans contained in the Condensed Consolidated Statements of Operations during the quarters ended December 31, 2012 and 2011 was as follows:

	For the Quarters Ended December 31,		For the Six Months Ended December 31,	
Derivative Financial Instruments (In Thousands)	2012	2011	2012	2011

Commitments to extend credit on loans to be held for sale	$ (5,132)	$ (1,344)	$ (743)	$ 1,480
Mandatory loan sale commitments and TBA MBS trades	5,642	(25)	984	(2,497)
Option contracts	(179)	(135)	(441)	(289)
Total	$ 331	$ (1,504)	$ (200)	$ (1,306)

The outstanding derivative financial instruments at the dates indicated were as follows:

Derivative Financial Instruments (In Thousands)	December 31, 2012 Amount	December 31, 2012 Fair Value	June 30, 2012 Amount	June 30, 2012 Fair Value
Commitments to extend credit on loans to be held for sale (1)	$ 221,978	$ 3,238	$ 220,357	$ 3,981
Best efforts loan sale commitments	(34,374)	-	(30,498)	-
Mandatory loan sale commitments and TBA MBS trades	(477,671)	(332)	(408,636)	(1,316)
Put option contracts	(20,000)	47	(15,000)	36
Total	$ (310,067)	$ 2,953	$ (233,777)	$ 2,701

(1) Net of 28.4 percent at December 31, 2012 and 33.8 percent at June 30, 2012 of commitments, which management has estimated may not fund.

Note 8: Income Taxes

FASB ASC 740, “Income Taxes,” requires the affirmative evaluation that it is more likely than not, based on the technical merits of a tax position, that an enterprise is entitled to economic benefits resulting from positions taken in income tax returns. If a tax position does not meet the more-likely-than-not recognition threshold, the benefit of that position is not recognized in the financial statements. Management has determined that there are no unrecognized tax benefits to be reported in the Corporation’s financial statements.

ASC 740 requires that when determining the need for a valuation allowance against a deferred tax asset, management must assess both positive and negative evidence with regard to the realizability of the tax losses represented by that asset. To the extent available sources of taxable income are insufficient to absorb tax losses, a valuation allowance is necessary. Sources of taxable income for this analysis include prior years’ tax returns, the expected reversals of taxable temporary differences between book and tax income, prudent and feasible tax-planning strategies, and future taxable income. The deferred tax asset related to the allowance will be realized when actual charge-offs are made against the allowance. Based on the availability of loss carry-backs and projected taxable income during the periods for which loss carry-forwards are available, management believes it is more likely than not the Corporation will realize the deferred tax asset. The Corporation continues to monitor the deferred tax asset on a quarterly basis for a valuation allowance. The future realization of these tax benefits primarily hinges on adequate future earnings to utilize the tax benefit. Prospective earnings or losses, tax law changes or capital changes could prompt the Corporation to reevaluate the assumptions which may be used to establish a valuation allowance. As of December 31, 2012, the estimated deferred tax asset was $9.3 million, a $653,000 or eight percent increase, from $8.6 million at June 30, 2012. The Corporation did not have any liabilities for uncertain tax positions or any known unrecognized tax benefit at December 31, 2012 or June 30, 2012, other than the $825,000 tax liability at June 30, 2012 related to the prior period adjustment for fiscal 2009 established as a result of the Corporation’s overstatement of certain income items for tax reporting purposes from 2006 through 2007, resulting in an overpayment of taxes and an understatement of the deferred tax liability.

On August 2, 2012, the Corporation received a notification from the tax authorities indicating the acceptance of the accounting method change attributable to the Corporation's overstatement of certain income items for tax reporting purposes from 2006 through 2007. As a result, the Corporation reversed the $825,000 tax liability recorded in the quarter ended June 30, 2012, decreasing the provision for income taxes for the quarter ended September 30, 2012.

The Corporation files income tax returns for the United States and state of California jurisdictions. The Internal Revenue Service has audited the Bank's income tax returns through 1996 and the California Franchise Tax Board has audited the Bank through 1990. Also, the Internal Revenue Service completed a review of the Corporation's income tax returns for fiscal 2006 and 2007; and the California Franchise Tax Board completed a review of the Corporation's income tax returns for fiscal 2007 and 2008. Tax years subsequent to fiscal 2009 remain subject to federal examination, while the California state tax returns for years subsequent to fiscal 2008 are subject to examination by state taxing authorities. It is the Corporation's policy to record any penalties or interest charges arising from federal or state taxes as a component of income tax expense. For the quarters ended December 31, 2012 and 2011, there were no tax penalties or interest charges. For the six months ended December 31, 2012, there were no tax penalties or interest charges; while for the six months ended December 31, 2011, a total of $14,000 in interest charges (related to the State of California tax return for fiscal 2007) was paid with no penalties.

Note 9: Fair Value of Financial Instruments

The Corporation adopted ASC 820, “Fair Value Measurements and Disclosures,” and elected the fair value option pursuant to ASC 825, “Financial Instruments” on loans originated for sale by PBM. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 825 permits entities to elect to measure many financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis (the “Fair Value Option”) at specified election dates. At each subsequent reporting date, an entity is required to report unrealized gains and losses on items in earnings for which the fair value option has been elected. The objective of the Fair Value Option is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions.

The following table describes the difference at dates indicated between the aggregate fair value and the aggregate unpaid principal balance of loans held for sale at fair value.

(In Thousands)	Aggregate Fair Value	Aggregate Unpaid Principal Balance	Net Unrealized Gain
As of December 31, 2012:			
Loans held for sale, measured at fair value	$ 294,434	$ 283,240	$ 11,194
As of June 30, 2012:			
Loans held for sale, measured at fair value	$ 231,639	$ 220,849	$ 10,790

ASC 820-10-65-4, “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,” provides additional guidance for estimating fair value in accordance with ASC 820, “Fair Value Measurements,” when the volume and level of activity for the asset or liability have significantly decreased.

ASC 820 establishes a three-level valuation hierarchy that prioritizes inputs to valuation techniques used in fair value calculations. The three levels of inputs are defined as follows:

Level-1 Unadjusted quoted prices in active markets for identical assets or liabilities that the Corporation has the ability to access at the measurement date.

Level-2 Observable inputs other than Level 1 such as: quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated to observable market data for substantially the full term of the asset or liability.

Level-3 Unobservable inputs for the asset or liability that use significant assumptions, including assumptions of risks. These unobservable assumptions reflect the Corporation’s estimate of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of pricing models, discounted cash flow models and similar techniques.

ASC 820 requires the Corporation to maximize the use of observable inputs and minimize the use of unobservable inputs. If a financial instrument uses inputs that fall in different levels of the hierarchy, the instrument will be categorized based upon the lowest level of input that is significant to the fair value calculation.

The Corporation's financial assets and liabilities measured at fair value on a recurring basis consist of investment securities, loans held for sale at fair value, interest-only strips and derivative financial instruments; while non-performing loans, mortgage servicing assets ("MSA") and real estate owned are measured at fair value on a nonrecurring basis.

Investment securities are primarily comprised of U.S. government agency MBS, U.S. government sponsored enterprise MBS and private issue CMO. The Corporation utilizes unadjusted quoted prices in active markets for identical securities for its fair value measurement of debt securities, quoted prices in active and less than active markets for similar securities for its fair value measurement of MBS and debt securities (Level 2), and broker price indications for similar securities in non-active markets for its fair value measurement of CMO (Level 3).

Derivative financial instruments are comprised of commitments to extend credit on loans to be held for sale, mandatory loan sale commitments, TBA-MBS trades and option contracts. The fair value of TBA-MBS trades is determined using quoted secondary-market prices (Level 2). The fair values of other derivative financial instruments are determined by quoted prices for a similar commitment or commitments, adjusted for the specific attributes of each commitment (Level 3).

Loans held for sale at fair value are primarily single-family loans. The fair value is determined, when possible, using quoted secondary-market prices such as mandatory loan sale commitments. If no such quoted price exists, the fair value of a loan is determined by quoted prices for a similar loan or loans, adjusted for the specific attributes of each loan (Level 2).

Non-performing loans are loans which are inadequately protected by the current net worth and paying capacity of the borrowers or of the collateral pledged. The non-performing loans are characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. The fair value of a non-performing loan is determined based on an observable market price or current appraised value of the underlying collateral. Appraised and reported values may be discounted based on management’s historical knowledge, changes in market conditions from the time of valuation, and/or management’s expertise and knowledge of the borrower. For non-performing loans which are restructured loans, the fair value is derived from discounted cash flow analysis (Level 3), except those which are in the process of foreclosure or 90 days delinquent for which the fair value is derived from the appraised value of its collateral (Level 2). For other non-performing loans which are not restructured loans, the fair value is derived from historical experience and management estimates by loan type for which collectively evaluated allowances are assigned (Level 3), or the appraised value of its collateral for loans which are in the process of foreclosure or where borrowers file bankruptcy, for which the charge-off will occur when the loan becomes 60 days delinquent (Level 2). Non-performing loans are reviewed and evaluated on at least a quarterly basis for additional allowance and adjusted accordingly, based on the same factors identified above. This loss is not recorded directly as an adjustment to current earnings or other comprehensive income (loss), but rather as a component in determining the overall adequacy of the allowance for loan losses. These adjustments to the estimated fair value of non-performing loans may result in increases or decreases to the provision for loan losses recorded in current earnings.

The Corporation uses the amortization method for its MSA, which amortizes the MSA in proportion to and over the period of estimated net servicing income and assesses the MSA for impairment based on fair value at each reporting date. The fair value of MSA is calculated using the present value method; which includes a third party’s prepayment projections of similar instruments, weighted-average coupon rates and the estimated average life (Level 3).

The rights to future income from serviced loans that exceed contractually specified servicing fees are recorded as interest-only strips. The fair value of interest-only strips is calculated using the same assumptions that are used to value the related MSA (Level 3).

The fair value of real estate owned is derived from the lower of the appraised value at the time of foreclosure or the listing price, net of estimated selling costs (Level 2).

The Corporation’s valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Corporation’s valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The following fair value hierarchy table presents information at the dates indicated about the Corporation's assets measured at fair value on a recurring basis:

	Fair Value Measurement at December 31, 2012 Using:			
(In Thousands)	Level 1	Level 2	Level 3	Total
Assets:				
Investment securities:				
U.S. government agency MBS	$ -	$ 11,600	$ -	$ 11,600
U.S. government sponsored enterprise MBS	-	8,428	-	8,428
Private issue CMO	-	-	1,156	1,156
Investment securities	-	20,028	1,156	21,184
Loans held for sale, at fair value	-	294,434	-	294,434
Interest-only strips	-	-	130	130
Derivative assets:				
Commitments to extend credit on loans to be held for sale	-	-	3,273	3,273
Mandatory loan sale commitments	-	-	45	45
TBA MBS trades	-	247	-	247
Option contracts	-	-	47	47
Derivative assets	-	247	3,365	3,612
Total assets	$ -	$ 314,709	$ 4,651	$ 319,360
Liabilities:				
Derivative liabilities:				
Commitments to extend credit on loans to be held for sale	$ -	$ -	$ 35	$ 35
Mandatory loan sale commitments	-	-	116	116
TBA MBS trades	-	508	-	508
Derivative liabilities	-	508	151	659
Total liabilities	$ -	$ 508	$ 151	$ 659

	Fair Value Measurement at June 30, 2012 Using:			
(In Thousands)	Level 1	Level 2	Level 3	Total
Assets:				
Investment securities:				
U.S. government agency MBS	$ -	$ 12,314	$ -	$ 12,314
U.S. government sponsored enterprise MBS	-	9,342	-	9,342
Private issue CMO	-	-	1,242	1,242
Investment securities	-	21,656	1,242	22,898
Loans held for sale, at fair value	-	231,639	-	231,639
Interest-only strips	-	-	130	130
Derivative assets:				
Commitments to extend credit on loans to be held for sale	-	-	3,998	3,998
Mandatory loan sale commitments	-	-	38	38
TBA MBS trades	-	121	-	121
Option contracts	-	-	36	36
Derivative assets	-	121	4,072	4,193
Total assets	$ -	$ 253,416	$ 5,444	$ 258,860
Liabilities:				
Derivative liabilities:				
Commitments to extend credit on loans to be held for sale	$ -	$ -	$ 17	$ 17
Mandatory loan sale commitments	-	-	201	201
TBA MBS trades	-	1,274	-	1,274
Derivative liabilities	-	1,274	218	1,492
Total liabilities	$ -	$ 1,274	$ 218	$ 1,492

The following is a reconciliation of the beginning and ending balances during the periods shown of recurring fair value measurements recognized in the Condensed Consolidated Statements of Financial Condition using Level 3 inputs:

	Fair Value Measurement Using Significant Other Unobservable Inputs (Level 3)					
(In Thousands)	Private Issue CMO	Interest-Only Strips	Loan Commit-ments to originate (1)	Manda-tory Commit-ments (2)	Option Contracts	Total
Beginning balance at October 1, 2012	$ 1,198	$ 117	$ 8,370	$ (1,114)	$ 65	$ 8,636
Total gains or losses (realized/unrealized):						

Included in earnings	-	-	(8,370)	1,114	(65)	(7,321)
Included in other comprehensive loss	(7)	13	-	-	-	6
Purchases	-	-	-	(71)	47	(24)
Issuances	-	-	3,238	-	-	3,238
Settlements	(35)	-	-	-	-	(35)
Transfers in and/or out of Level 3	-	-	-	-	-	-
Ending balance at December 31, 2012	$ 1,156	$ 130	$ 3,238	$ (71)	$ 47	$ 4,500

(1) Consists of commitments to extend credit on loans to be held for sale.
(2) Consists of mandatory loan sale commitments.

	Fair Value Measurement Using Significant Other Unobservable Inputs (Level 3)					
(In Thousands)	Private Issue CMO	Interest-Only Strips	Loan Commit-ments to originate (1)	Manda-tory Commit-ments (2)	Option Contracts	Total
Beginning balance at October 1, 2011	$ 1,288	$ 167	$ 3,462	$ (130)	$ 142	$ 4,929
Total gains or losses (realized/unrealized):						
Included in earnings	-	-	(3,462)	130	(142)	(3,474)
Included in other comprehensive loss	1	(11)	-	-	-	(10)
Purchases	-	-	-	(2)	-	(2)
Issuances	-	-	2,118	-	-	2,118
Settlements	(45)	-	-	-	-	(45)
Transfers in and/or out of Level 3	-	-	-	-	-	-
Ending balance at December 31, 2011	$ 1,244	$ 156	$ 2,118	$ (2)	$ -	$ 3,516

(1) Consists of commitments to extend credit on loans to be held for sale.
(2) Consists of mandatory loan sale commitments.

	Fair Value Measurement Using Significant Other Unobservable Inputs (Level 3)					
(In Thousands)	Private Issue CMO	Interest-Only Strips	Loan Commit-ments to originate (1)	Manda-tory Commit-ments (2)	Option Contracts	Total
Beginning balance at July 1, 2012	$ 1,242	$ 130	$ 3,981	$ (163)	$ 36	$ 5,226
Total gains or losses (realized/unrealized):						
Included in earnings	-	-	(12,351)	1,277	(101)	(11,175)
Included in other comprehensive loss	(6)	-	-	-	-	(6)
Purchases	-	-	-	(1,185)	112	(1,073)
Issuances	-	-	11,608	-	-	11,608
Settlements	(80)	-	-	-	-	(80)
Transfers in and/or out of Level 3	-	-	-	-	-	-
Ending balance at December 31, 2012	$ 1,156	$ 130	$ 3,238	$ (71)	$ 47	$ 4,500

(1) Consists of commitments to extend credit on loans to be held for sale.
(2) Consists of mandatory loan sale commitments.

	Fair Value Measurement Using Significant Other Unobservable Inputs (Level 3)					
(In Thousands)	Private Issue CMO	Interest-Only Strips	Loan Commit-ments to originate (1)	Manda-tory Commit-ments (2)	Option Contracts	Total
Beginning balance at July 1, 2011	$ 1,367	$ 200	$ 638	$ 403	$ 99	$ 2,707
Total gains or losses (realized/unrealized):						
Included in earnings	-	-	(4,101)	(273)	(241)	(4,615)
Included in other comprehensive loss	(41)	(44)	-	-	-	(85)
Purchases	-	-	-	(132)	142	10
Issuances	-	-	5,581	-	-	5,581
Settlements	(82)	-	-	-	-	(82)
Transfers in and/or out of Level 3	-	-	-	-	-	-
Ending balance at December 31, 2011	$ 1,244	$ 156	$ 2,118	$ (2)	$ -	$ 3,516

(1) Consists of commitments to extend credit on loans to be held for sale.
(2) Consists of mandatory loan sale commitments.

The following fair value hierarchy table presents information about the Corporation's assets measured at fair value at the dates indicated on a nonrecurring basis:

	Fair Value Measurement at December 31, 2012 Using:			
(In Thousands)	Level 1	Level 2	Level 3	Total
Non-performing loans	$ -	$ 10,508	$ 14,754	$ 25,262
Mortgage servicing assets	-	-	331	331
Real estate owned, net	-	2,435	-	2,435
Total	$ -	$ 12,943	$ 15,085	$ 28,028

	Fair Value Measurement at June 30, 2012 Using:			
(In Thousands)	Level 1	Level 2	Level 3	Total
Non-performing loans	$ -	$ 10,335	$ 25,006	$ 35,341
Mortgage servicing assets	-	-	227	227
Real estate owned, net	-	5,489	-	5,489
Total	$ -	$ 15,824	$ 25,233	$ 41,057

The following table presents additional information about valuation techniques and inputs used for assets and liabilities, including derivative financial instruments, which are measured at fair value and categorized within Level 3 as of December 31, 2012 (dollars in thousands):

	Fair Value As of December 31, 2012	Valuation Techniques	Unobservable Inputs	Range (1) (Weighted Average)	Impact to Valuation from an Increase in Inputs (2)
Assets:					
Securities available-for sale: Private issue CMO	$ 1,156	Discounted cash flow	Probability of default Loss severity Prepayment speed	0.4% – 1.2% (0.9%) 15.6% - 37.7% (36.5%) 3.4% – 9.5% (5.4%)	Decrease Decrease Decrease
Non-performing loans	$ 14,754	Discounted cash flow or aggregated pooling method	Default rates Loss severity	26.9% 7.2%	Decrease Decrease
MSA	$ 331	Discounted cash flow	Prepayment speed (CPR) Discount rate	0.0% - 60.0% (29.4%) 9.0% - 10.5% (8.8%)	Decrease Decrease
Interest-only strips	$ 130	Discounted cash flow	Prepayment speed (CPR) Discount rate	0.0% - 43.6% (16.8%) 9.0%	Decrease Decrease
Commitments to extend credit on loans to be held for sale	$ 3,273	Relative value analysis	TBA-MBS broker quotes Fall-out ratio (3)	98.1% – 104.5% (102.2%) of par 24.4% - 28.7% (28.4%)	Decrease Decrease
Mandatory loan sale commitments	$ 45	Relative value analysis	Investor quotes TBA-MBS broker quotes Roll-forward costs (4)	102.1% – 104.3% (103.5%) of par 104.5% – 108.7% (105.9%) of par 0.00%	Decrease Decrease Decrease
Put options	$ 47		Broker quotes		Increase

		Relative value analysis		106.4% – 106.7% (106.5%) of par	
Liabilities:					
Commitments to extend credit on loans to be held for sale	$ 35	Relative value analysis	TBA-MBS broker quotes	100.5% – 104.4% (102.6%) of par	Decrease
			Fall-out ratio (3)	24.4% - 28.7% (28.4%)	Decrease
Mandatory loan sale commitments	$ 116	Relative value analysis	Investor quotes	102.1% – 103.9% (102.7%) of par	Decrease
			TBA-MBS broker quotes	104.5% – 108.6% (106.2%) of par	Decrease
			Roll-forward costs (4)	0.00%	Decrease

(1) The range is based on the historical estimated fair values and management estimates.

(2) Unless otherwise noted, this column represents the directional change in the fair value of the Level 3 investments that would result from an increase to the corresponding unobservable input. A decrease to the unobservable input would have the opposite effect. Significant changes in these inputs in isolation could result in significantly higher or lower fair value measurements.

(3) The percentage of commitments to extend credit on loans to be held for sale which management has estimated may not fund.

(4) An estimated cost to roll forward the mandatory loan sale commitments which management has estimated may not be delivered to the corresponding investors in a timely manner.

The significant unobservable inputs used in the fair value measurement of the Corporation's assets and liabilities include the followings: CMO offered quotes, prepayment speeds, discount rates, MBS – TBA quotes, fallout ratios, investor quotes and roll-forward costs, among others. Significant increases or decreases in any of these inputs in isolation could result in significantly lower or higher fair value measurement. The various unobservable inputs used to determine valuations may have similar or diverging impacts on valuation.

The carrying amount and fair value of the Corporation's other financial instruments as of December 31, 2012 and June 30, 2012 were as follows (dollars in thousands):

	December 31, 2012				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial assets:					
Loans held for investment, net	$ 772,057	$ 771,334	-	-	$ 771,334
FHLB – San Francisco stock	$ 19,149	$ 19,149	-	$ 19,149	-
Financial liabilities:					
Deposits	$ 935,206	$ 920,984	-	-	$ 920,984
Borrowings	$ 126,519	$ 134,714	-	-	$ 134,714

	June 30, 2012				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial assets:					
Loans held for investment, net	$ 796,836	$ 801,081	-	-	$ 801,081
FHLB – San Francisco stock	$ 22,255	$ 22,255	-	$ 22,255	-
Financial liabilities:					
Deposits	$ 961,411	$ 948,985	-	-	$ 948,985
Borrowings	$ 126,546	$ 134,936	-	-	$ 134,936

Cash and cash equivalents: The carrying amount of these financial assets approximates the fair value.

Loans held for investment: For loans that reprice frequently at market rates, the carrying amount approximates the fair value. For fixed-rate loans, the fair value is determined by either (i) discounting the estimated future cash flows of such loans over their estimated remaining contractual maturities using a current interest rate at which such loans would be made to borrowers, or (ii) quoted market prices. The allowance for loan losses is subtracted as an estimate of the underlying credit risk.

FHLB – San Francisco stock: The carrying amount reported for FHLB – San Francisco stock approximates fair value. When redeemed, the Corporation will receive an amount equal to the par value of the stock.

Deposits: The fair value of time deposits is estimated using a discounted cash flow calculation. The discount rate is based upon rates currently offered for deposits of similar remaining maturities. The fair value of transaction accounts (checking, money market and savings accounts) is based on management estimates, consistent with current market conditions.

Borrowings: The fair value of borrowings has been estimated using a discounted cash flow calculation. The discount rate on such borrowings is based upon rates currently offered for borrowings of similar remaining maturities.

The Corporation has various processes and controls in place to ensure that fair value is reasonably estimated. The Corporation generally determines fair value of their Level 3 assets and liabilities by using internally developed models which primarily utilize discounted cash flow techniques and prices obtained from independent management services or brokers. The Corporation performs due diligence procedures over third-party pricing service providers in order to support their use in the valuation process. The fair values of investment securities, commitments to extend credit on loans held for sale, mandatory commitments and option contracts are determined from the independent management services or brokers; while the fair value of MSA and interest only strips are determined using the internally developed models which are based on discounted cash flow analysis. The fair value of non-performing loans is determined by calculating discounted cash flows, collectively evaluated allowances or collateral value, less selling costs.

While the Corporation believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. During the quarter ended December 31, 2012, there were no significant changes to the Corporation's valuation techniques that had, or are expected to have, a material impact on its consolidated financial position or results of operations.

Note 10: Incentive Plans

As of December 31, 2012, the Corporation had four share-based compensation plans, which are described below. These plans are the 2010 Equity Incentive Plan ("2010 Plan"), the 2006 Equity Incentive Plan ("2006 Plan"), the 2003 Stock Option Plan and the 1996 Stock Option Plan.

For the quarters ended December 31, 2012 and 2011, the compensation cost for these plans was $105,000 and $244,000, respectively. No income tax benefit was recognized in the quarters ended December 31, 2012 and 2011.

For the six months ended December 31, 2012 and 2011, the compensation cost for these plans was $239,000 and $833,000, respectively. The income tax benefit recognized in the Condensed Consolidated Statements of Operations for share-based compensation plans was $71,000 for the six months ended December 31, 2012 and no income tax benefit was recognized in the six months ended December 31, 2011.

Equity Incentive Plan. The Corporation established and the shareholders approved the 2010 Plan and the 2006 Plan for directors, advisory directors, directors emeriti, officers and employees of the Corporation and its subsidiary. The 2010 Plan authorizes 586,250 stock options and 288,750 shares of restricted stock. The 2010 Plan also provides that no person may be granted more than 117,250 stock options or 43,312 shares of restricted stock in any one year. The 2006 Plan authorizes 365,000 stock options and 185,000 shares of restricted stock. The 2006 Plan also provides that no person may be granted more than 73,000 stock options or 27,750 shares of restricted stock in any one year.

Equity Incentive Plan - Stock Options. Under the 2010 Plan and 2006 Plan (collectively, "the Plans"), options may not be granted at a price less than the fair market value at the date of the grant. Options typically vest over a five-year or shorter period as long as the director, advisory director, director emeritus, officer or employee remains in service to the Corporation. The options are exercisable after vesting for up to the remaining term of the original grant. The maximum term of the options granted is 10 years.

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option valuation model with the following assumptions. The expected volatility is based on implied volatility from historical common stock closing prices for the prior 84 months. The expected dividend yield is based on the most recent quarterly dividend on an annualized basis. The expected term is based on the historical experience of all fully vested stock option grants and is reviewed annually. The risk-free interest rate is based on the U.S. Treasury note rate with a term similar to the underlying stock option on the particular grant date.

There was no activity under the Plans in the second quarter of either fiscal 2013 or 2012, other than the grant of 20,000 options and forfeiture of 20,000 options in the second quarter of fiscal 2013. For the first six months of fiscal 2013 and 2012, there was no activity under the Plans, other than the grant of 20,000 options, the exercise of 28,000 options and the forfeiture of 24,000 options in the first six months of fiscal 2013. As of December 31, 2012 and 2011, there were 188,450 stock options and 184,450 stock options available for future grants under the Plans, respectively.

The following table summarizes the stock option activity in the Plans for the quarter and six months ended December 31, 2012.

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at October 1, 2012	725,800	$ 12.35		
Granted	20,000	$ 16.47		
Exercised	-	$ -		
Forfeited	(20,000)	$ 7.43		
Outstanding at December 31, 2012	725,800	$ 12.60	6.90	$ 5,435
Vested and expected to vest at December 31, 2012	644,000	$ 13.20	6.69	$ 4,647
Exercisable at December 31, 2012	316,800	$ 18.70	4.78	$ 1,497

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at July 1, 2012	757,800	$ 12.13		
Granted	20,000	$ 16.47		
Exercised	(28,000)	$ 7.03		
Forfeited	(24,000)	$ 7.41		
Outstanding at December 31, 2012	725,800	$ 12.60	6.90	$ 5,435
Vested and expected to vest at December 31, 2012	644,000	$ 13.20	6.69	$ 4,647
Exercisable at December 31, 2012	316,800	$ 18.70	4.78	$ 1,497

As of December 31, 2012 and 2011, there was $1.1 million and $1.4 million of unrecognized compensation expense, respectively, related to unvested share-based compensation arrangements under the Plans. The expense is expected to be recognized over a weighted-average period of 2.7 years and 3.3 years, respectively. The forfeiture rate during the first six months of fiscal 2013 and 2012 was 20 percent for both periods, and was calculated by using the historical forfeiture experience of all fully vested stock option grants and is reviewed annually.

Equity Incentive Plan – Restricted Stock. The Corporation used 288,750 shares and 185,000 shares of its treasury stock to fund the 2010 Plan and the 2006 Plan, respectively. Awarded shares typically vest over a five-year or shorter period as long as the director, advisory director, director emeriti, officer or employee remains in service to the Corporation. Once vested, a recipient of restricted stock will have all rights of a shareholder, including the power to vote and the right to receive dividends. The Corporation recognizes compensation expense for the restricted stock awards based on the fair value of the shares at the award date.

There was no restricted stock activity for either the second quarter of fiscal 2013 and 2012. For the first six months of fiscal 2013, there was no restricted stock activity, other than the vesting and distribution of 800 shares and the forfeiture of 1,500 shares. This compares to the vesting and distribution of 100,300 shares of restricted stock in the first six months of fiscal 2012. As of December 31, 2012 and 2011, there were 169,600 shares and 168,100 shares of restricted stock available for future awards under the Plans, respectively.

The following table summarizes the unvested restricted stock activity in the quarter and six months ended December 31, 2012.

Unvested Shares	Shares	Weighted-Average Award Date Fair Value
Unvested at October 1, 2012	144,500	$ 7.07
Granted	-	$ -
Vested	-	$ -
Forfeited	-	$ -
Unvested at December 31, 2012	144,500	$ 7.07
Expected to vest at December 31, 2012	115,600	$ 7.07

Unvested Shares	Shares	Weighted-Average Award Date Fair Value
Unvested at July 1, 2012	146,800	$ 7.13
Granted	-	$ -
Vested	(800)	$ 18.09
Forfeited	(1,500)	$ 7.07
Unvested at December 31, 2012	144,500	$ 7.07
Expected to vest at December 31, 2012	115,600	$ 7.07

As of December 31, 2012 and 2011, the unrecognized compensation expense was $708,000 and $1.0 million, respectively, related to unvested share-based compensation arrangements under the Plans, and reported as a reduction to stockholders' equity. This expense is expected to be recognized over a weighted-average period of 2.5 years and 3.2 years, respectively. Similar to stock options, a forfeiture rate of 20 percent has been applied for the restricted stock compensation expense calculations in the first six months of fiscal 2013 and 2012, for both periods. For the six months ended December 31, 2012 and 2011, the fair value of shares vested and distributed was $9,000 and $814,000, respectively.

Stock Option Plans. The Corporation established the 2003 Stock Option Plan and the 1996 Stock Option Plan (collectively, the "Stock Option Plans") for key employees and eligible directors under which options to acquire up to 352,500 shares and 1.15 million shares of common stock, respectively, may be granted. Under the Stock Option Plans, stock options may not be granted at a price less than the fair market value at the date of the grant. Stock options typically vest over a five-year period on a pro-rata basis as long as the employee or director remains in service to the Corporation. The stock options are exercisable after vesting for up to the remaining term of the original grant. The maximum term of the stock options granted is 10 years. As of December 31, 2012 and 2011, the number of stock options available for future grants under the 2003 Stock Option Plan was 14,900 stock options. No stock options remain available for future grant under the 1996 Stock Option Plan, which expired in January 2007.

The fair value of each stock option grant is estimated on the date of the grant using the Black-Scholes option valuation model with the following assumptions. The expected volatility is based on implied volatility from historical common stock closing prices for the prior 84 months. The expected dividend yield is based on the most recent quarterly dividend on an annualized basis. The expected term is based on the historical experience of all fully vested stock option grants and is reviewed annually. The risk-free interest rate is based on the U.S. Treasury note rate with a term similar to the underlying stock option on the particular grant date.

For the second quarter of fiscal 2013 and 2012, there was no activity in the Stock Option Plans, except forfeitures of 62,700 shares in the second quarter of fiscal 2012. For the first six months of fiscal 2013 and 2012, there was no activity in the Stock Option Plans, except forfeitures of 7,500 shares and 62,700 shares, respectively. As of December 31, 2012 and 2011, there were 14,900 stock options and 14,900 stock options available for future grants under the Stock Option Plans, respectively.

The following is a summary of the activity in the Stock Option Plans for the quarter and six months ended December 31, 2012.

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at October 1, 2012	412,700	$ 24.30		
Granted	-	$ -		
Exercised	-	$ -		
Forfeited	-	$ -		
Outstanding at December 31, 2012	412,700	$ 24.30	2.01	$ -
Vested and expected to vest at December 31, 2012	412,700	$ 24.30	2.01	$ -
Exercisable at December 31, 2012	412,700	$ 24.30	2.01	$ -

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at July 1, 2012	420,200	$ 24.11		
Granted	-	$ -		
Exercised	-	$ -		
Forfeited	(7,500)	$ 13.67		
Outstanding at December 31, 2012	412,700	$ 24.30	2.01	$ -
Vested and expected to vest at December 31, 2012	412,700	$ 24.30	2.01	$ -
Exercisable at December 31, 2012	412,700	$ 24.30	2.01	$ -

As of December 31, 2012, there was no unrecognized compensation expense. This compares to unrecognized compensation expense of $26,000 at December 31, 2011, related to unvested share-based compensation arrangements under the Stock Option Plans. This expense is expected to be recognized over a weighted-average period of 0.6 years. The forfeiture rate during the first six months of fiscal 2012 was 20 percent, and was calculated by using the historical forfeiture experience of all fully vested stock option grants and is reviewed annually.

Note 11: Subsequent Events

On January 24, 2013, the Corporation announced that the Corporation’s Board of Directors declared a quarterly cash dividend of $0.07 per share, reflecting a 40 percent increase from the $0.05 per share paid on December 11, 2012. Shareholders of the Corporation’s common stock at the close of business on February 13, 2013 will be entitled to receive the cash dividend. The cash dividend will be payable on March 5, 2013.

ITEM 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

General

Provident Financial Holdings, Inc., a Delaware corporation, was organized in January 1996 for the purpose of becoming the holding company of Provident Savings Bank, F.S.B. upon the Bank's conversion from a federal mutual to a federal stock savings bank ("Conversion"). The Conversion was completed on June 27, 1996. The Corporation is regulated by the Federal Reserve Board ("FRB"). At December 31, 2012, the Corporation had total assets of $1.25 billion, total deposits of $935.2 million and total stockholders' equity of $155.9 million. The Corporation has not engaged in any significant activity other than holding the stock of the Bank. Accordingly, the information set forth in this report, including financial statements and related data, relates primarily to the Bank and its subsidiaries. As used in this report, the terms "we," "our," "us," and "Corporation" refer to Provident Financial Holdings, Inc. and its consolidated subsidiaries, unless the context indicates otherwise.

The Bank, founded in 1956, is a federally chartered stock savings bank headquartered in Riverside, California. The Bank is regulated by the Office of the Comptroller of the Currency ("OCC"), its primary federal regulator, and the Federal Deposit Insurance Corporation ("FDIC"), the insurer of its deposits. The Bank's deposits are federally insured up to applicable limits by the FDIC. The Bank has been a member of the Federal Home Loan Bank System since 1956.

The Corporation's business consists of community banking activities and mortgage banking activities, conducted by Provident Bank and Provident Bank Mortgage, a division of the Bank. Community banking activities primarily consist of accepting deposits from customers within the communities surrounding the Bank's full service offices and investing those funds in single-family loans, multi-family loans, commercial real estate loans, construction loans, commercial business loans, consumer loans and other real estate loans. The Bank also offers business checking accounts, other business banking services, and services loans for others. Mortgage banking activities consist of the origination, purchase and sale of mortgage loans secured primarily by single-family residences. The Bank currently operates 15 retail/business banking offices in Riverside County and San Bernardino County (commonly known as the Inland Empire). Provident Bank Mortgage operates two wholesale loan production offices: one in Pleasanton and one in Rancho Cucamonga, California; and 16 retail loan production offices in City of Industry, Escondido, Fairfield, Glendora, Hermosa Beach, Pleasanton, Rancho Cucamonga (2), Riverside (4), Roseville, San Diego, San Rafael and Stockton, California. The Corporation's revenues are derived principally from interest on its loans and investment securities and fees generated through its community banking and mortgage banking activities. There are various risks inherent in the Corporation's business including, among others, the general business environment, interest rates, the California real estate market, the demand for loans, the prepayment of loans, the repurchase of loans previously sold to investors, the secondary market conditions to sell loans, competitive conditions, legislative and regulatory changes, fraud and other risks.

The Corporation began to distribute quarterly cash dividends in the quarter ended September 30, 2002. On October 30, 2012, the Corporation declared a quarterly cash dividend of $0.05 per share for the Corporation's shareholders of record at the close of business on November 21, 2012, which was paid on December 11, 2012. Future declarations or payments of dividends will be subject to the consideration of the Corporation's Board of Directors, which will take into account the Corporation's financial condition, results of operations, tax considerations, capital requirements, industry standards, legal restrictions, economic conditions and other factors, including the regulatory restrictions which affect the payment of dividends by the Bank to the Corporation. Under Delaware law, dividends may be paid either out of surplus or, if there is no surplus, out of net profits for the current fiscal year and/or the preceding fiscal year in which the dividend is declared.

Management's Discussion and Analysis of Financial Condition and Results of Operations is intended to assist in understanding the financial condition and results of operations of the Corporation. The information contained in this section should be read in conjunction with the Unaudited Interim Condensed Consolidated Financial Statements and accompanying selected Notes to Unaudited Interim Condensed Consolidated Financial Statements.

Safe-Harbor Statement

Certain matters in this Form 10-Q constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. This Form 10-Q contains statements that the Corporation believes are "forward-looking statements." These statements relate to the Corporation's financial condition, results of operations, plans, objectives, future performance or business. You should not place undue reliance on these statements, as they are subject to risks and uncertainties. When considering these forward-looking statements, you should keep in mind these risks and uncertainties, as well as any cautionary statements the Corporation may make. Moreover, you should treat these statements as speaking only as of the date they are made and based only on information then actually known to the Corporation. There are a number of important factors that could cause future results to differ materially from historical performance and these forward-looking statements. Factors which could cause actual results to differ materially include, but are not limited to, the credit risks of lending activities, including changes in the level and trend of loan delinquencies and charge-offs and changes in our allowance for loan losses and provision for loan losses that may be impacted by deterioration in the residential and commercial real estate markets and may lead to increased losses and non-performing assets and may result in our allowance for loan losses not being adequate to cover actual losses and require us to materially increase our reserve; changes in general economic conditions, either nationally or in our market areas; changes in the levels of general interest rates, and the relative differences between short and long term interest rates, deposit interest rates, our net interest margin and funding sources; fluctuations in the demand for loans, the number of unsold homes, land and other properties and fluctuations in real estate values in our market areas; secondary market conditions for loans and our ability to sell loans in the secondary market; results of examinations of the Corporation by the FRB or of the Bank by the OCC or other regulatory authorities, including the possibility that any such regulatory authority may, among other things, require us to enter into a formal enforcement action or to increase our allowance for loan losses, write-down assets, change our regulatory capital position or affect our ability to borrow funds or maintain or increase deposits, or impose additional requirements and restrictions on us, any of which could adversely affect our liquidity and earnings; legislative or regulatory changes, such as the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and its implementing regulations, that adversely affect our business, as well as changes in regulatory policies and principles or the interpretation of regulatory capital or other rules, including changes related to Basel III; our ability to attract and retain deposits; increases in premiums for deposit insurance; our ability to control operating costs and expenses; the use of estimates in determining fair value of certain of our assets, which estimates may prove to be incorrect and result in significant declines in valuation; difficulties in reducing risk associated with the loans on our balance sheet; staffing fluctuations in response to product demand or the implementation of corporate strategies that affect our workforce and potential associated charges; computer systems on which we depend could fail or experience a security breach; our ability to implement our branch expansion strategy; our ability to successfully integrate any assets, liabilities, customers, systems, and management personnel we have acquired or may in the future acquire into our operations and our ability to realize related revenue synergies and cost savings within expected time frames and any goodwill charges related thereto; our ability to manage loan delinquency rates; our ability to retain key members of our senior management team; costs and effects of litigation, including settlements and judgments; increased competitive pressures among financial services companies; changes in consumer spending, borrowing and savings habits; the availability of resources to address changes in laws, rules, or regulations or to respond to regulatory actions; our ability to pay dividends on our common stock; adverse changes in the securities markets; the inability of key third-party providers to perform their obligations to us; changes in accounting policies and practices, as may be adopted by the financial institution regulatory agencies or the Financial Accounting Standards Board, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods; war or terrorist activities; and other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services and other risks detailed in this report and in the Corporation's other reports filed with or furnished to the SEC, including its Annual Report on Form 10-K for the fiscal year ended June 30, 2012 and subsequently filed Quarterly Reports on Form 10-Q.

Critical Accounting Policies

The discussion and analysis of the Corporation's financial condition and results of operations is based upon the Corporation's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions.

The allowance for loan losses involves significant judgment and assumptions by management, which has a material impact on the carrying value of net loans. Management considers the accounting estimate related to the allowance for loan losses a critical accounting estimate because it is highly susceptible to change from period to period, requiring management to make assumptions about probable incurred losses inherent in the loan portfolio at the balance sheet date. The impact of a sudden large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings.

The allowance is based on two principles of accounting: (i) ASC 450, "Contingencies," which requires that losses be accrued when they are probable of occurring and can be estimated; and (ii) ASC 310, "Receivables." The allowance has two components: collectively evaluated allowances and individually evaluated allowances on substandard non-performing loans. Each of these components is based upon estimates that can change over time. The allowance is based on historical experience and as a result can differ from actual losses incurred in the future. Additionally, differences may result from qualitative factors such as unemployment data, gross domestic product, interest rates, retail sales, the value of real estate and real estate market conditions. The historical data is reviewed at least quarterly and adjustments are made as needed. Various techniques are used to arrive at an individually evaluated allowance, including discounted cash flows and the fair market value of collateral. Management considers, based on currently available information, the allowance for loan losses sufficient to absorb probable losses inherent in loans held for investment. The use of these techniques is inherently subjective and the actual losses could be greater or less than the estimates, which, can materially affect amounts recognized in the Condensed Consolidated Statements of Financial Condition and Condensed Consolidated Statements of Operations.

The Corporation assesses loans individually and classifies loans when the accrual of interest has been discontinued, loans have been restructured or management has serious doubts about the future collectibility of principal and interest, even though the loans may currently be performing. Factors considered in determining classification include, but are not limited to, expected future cash flows, the financial condition of the borrower and current economic conditions. The Corporation measures each non-performing loan based on the fair value of its collateral, less selling costs, or discounted cash flow and charges off those loans or portions of loans deemed uncollectible.

In compliance with the OCC's regulatory reporting requirements, non-performing loans are charged-off to their fair values in the period the loans, or portion thereof, are deemed uncollectible, generally after the loan becomes 150 days delinquent for real estate secured first trust deed loans and 120 days delinquent for commercial business or real estate secured second trust deed loans. For restructured loans, the charge-off occurs when the loans becomes 90 days delinquent; and where borrowers file bankruptcy, the charge-off occurs when the loan becomes 60 days delinquent. The amount of the charge-off is determined by comparing the loan balance to the estimated fair value of the underlying collateral, less disposition costs, with the loan balance in excess of the estimated fair value charged-off against the allowance for loan losses. The allowance for loan losses for non-performing loans is determined by applying ASC 310. For restructured loans that are less than 90 days delinquent, the allowance for loan losses are segregated into (a) individually evaluated allowances for those loans with applicable discounted cash flow calculations or (b) collectively evaluated allowances based on the aggregated pooling method. For non-performing loans less than 60 days delinquent where the borrower has filed bankruptcy, the collectively evaluated allowances are assigned based on the aggregated pooling method.

A troubled debt restructuring ("restructured loan") is a loan which the Corporation, for reasons related to a borrower's financial difficulties, grants a concession to the borrower that the Corporation would not otherwise consider.

The loan terms which have been modified or restructured due to a borrower's financial difficulty, include but are not limited to:

a) A reduction in the stated interest rate.
b) An extension of the maturity at an interest rate below market.
c) A reduction in the accrued interest.
d) Extensions, deferrals, renewals and rewrites.

The Corporation measures the allowance for loan losses of restructured loans based on the difference between the original loan's carrying amount and the present value of expected future cash flows discounted at the original effective yield of the loan. Based on published guidance with respect to restructured loans from certain banking regulators and to conform to general practices within the banking industry, the Corporation determined it was appropriate to maintain certain restructured loans on accrual status because there is reasonable assurance of repayment and performance, consistent with the modified terms based upon a current, well-documented credit evaluation.

Other restructured loans are classified as "Substandard" and placed on non-performing status. The loans may be upgraded and placed on accrual status once there is a sustained period of payment performance (usually six months or, for loans that have been restructured more than once, 12 months) and there is a reasonable assurance that the payments will continue; and if the borrower has demonstrated satisfactory contractual payments beyond 12 consecutive months, the loan is no longer categorized as a restructured loan for the SEC reporting purposes. In addition to the payment history described above; multi-family, commercial real estate, construction and commercial business loans must also demonstrate a combination of corroborating characteristics to be upgraded, such as: satisfactory cash flow, satisfactory guarantor support, and additional collateral support, among others.

To qualify for restructuring, a borrower must provide evidence of their creditworthiness such as, current financial statements, their most recent income tax returns, current paystubs, current W-2s, and most recent bank statements, among other documents, which are then verified by the Corporation. The Corporation re-underwrites the loan with the borrower's updated financial information, new credit report, current loan balance, new interest rate, remaining loan term, updated property value and modified payment schedule, among other considerations, to determine if the borrower qualifies.

Interest is not accrued on any loan when its contractual payments are more than 90 days delinquent or if the loan is deemed impaired. In addition, interest is not recognized on any loan where management has determined that collection is not reasonably assured. A non-performing loan may be restored to accrual status when delinquent principal and interest payments are brought current and future monthly principal and interest payments are expected to be collected.

When a loan is categorized as non-performing, all previously accrued but uncollected interest is reversed in the current operating results. When a full recovery of the outstanding principal loan balance is in doubt, subsequent payments received are first applied to unpaid principal and then to uncollected interest. This is referred to as the cost recovery method. A loan may be returned to accrual status at such time as the loan is brought fully current as to both principal and interest, and, in management's judgment, such loan is considered to be fully collectible on timely basis. However, the Corporation's policy also allows management to continue the recognition of interest income on certain non-performing loans. This is referred to as the cash basis method under which the accrual of interest is suspended and interest income is recognized only when collected. This policy applies to non-performing loans that are considered to be fully collectible but the timely collection of payments is in doubt.

ASC 815, "Derivatives and Hedging," requires that derivatives of the Corporation be recorded in the consolidated financial statements at fair value. Management considers its accounting policy for derivatives to be a critical accounting policy because these instruments have certain interest rate risk characteristics that change in value based upon changes in the capital markets. The Corporation's derivatives are primarily the result of its mortgage banking activities in the form of commitments to extend credit, commitments to sell loans, TBA MBS trades and option contracts to mitigate the risk of the commitments to extend credit. Estimates of the percentage of commitments to extend credit on loans to be held for sale that may not fund are based upon historical data and current market trends. The fair value adjustments of the derivatives are recorded in the Condensed Consolidated Statements of Operations with offsets to other assets or other liabilities in the Condensed Consolidated Statements of Financial Condition.

Management accounts for income taxes by estimating future tax effects of temporary differences between the tax and book basis of assets and liabilities considering the provisions of enacted tax laws. These differences result in deferred tax assets and liabilities, which are included in the Corporation's Condensed Consolidated Statements of Financial Condition. The application of income tax law is inherently complex. Laws and regulations in this area are voluminous and are often ambiguous. As such, management is required to make many subjective assumptions and judgments regarding the Corporation's income tax exposures, including judgments in determining the amount and timing of recognition of the resulting deferred tax assets and liabilities, including projections of future taxable income. Interpretations of and guidance surrounding income tax laws and regulations change over time. As such, changes in management's subjective assumptions and judgments can materially affect amounts recognized in the Condensed Consolidated Statements of Financial Condition and Condensed Consolidated Statements of Operations. Therefore, management considers its accounting for income taxes a critical accounting policy.

Executive Summary and Operating Strategy

Provident Savings Bank, F.S.B., established in 1956, is a financial services company committed to serving consumers and small to mid-sized businesses in the Inland Empire region of Southern California. The Bank conducts its business operations as Provident Bank, Provident Bank Mortgage, a division of the Bank, and through its subsidiary, Provident Financial Corp. The business activities of the Corporation, primarily through the Bank and its subsidiary, consist of community banking, mortgage banking and, to a lesser degree, investment services for customers and trustee services on behalf of the Bank.

Community banking operations primarily consist of accepting deposits from customers within the communities surrounding the Corporation's full service offices and investing those funds in single-family, multi-family and commercial real estate loans. Also, to a lesser extent, the Corporation makes construction, commercial business, consumer and other loans. The primary source of income in community banking is net interest income, which is the difference between the interest income earned on loans and investment securities, and the interest expense paid on interest-bearing deposits and borrowed funds. Additionally, certain fees are collected from depositors, such as returned check fees, deposit account service charges, ATM fees, IRA/KEOGH fees, safe deposit box fees, travelers check fees, wire transfer fees and overdraft protection fees, among others.

During the next three years, subject to market conditions, the Corporation intends to improve its community banking business by moderately growing total assets; by decreasing the concentration of single-family mortgage loans within loans held for investment; and by increasing the concentration of higher yielding preferred loans (i.e., multi-family, commercial real estate, construction and commercial business loans). In addition, the Corporation intends to decrease the percentage of time deposits in its deposit base and to increase the percentage of lower cost checking and savings accounts. This strategy is intended to improve core revenue through a higher net interest margin and ultimately, coupled with the growth of the Corporation, an increase in net interest income. While the Corporation's long-term strategy is for moderate growth, management recognizes that the total balance sheet may decline or stabilize in response to current weaknesses in general economic conditions, which may improve capital ratios and mitigate credit and liquidity risk.

Mortgage banking operations primarily consist of the origination, purchase and sale of mortgage loans secured by single-family residences. The primary sources of income in mortgage banking are gain on sale of loans and certain fees collected from borrowers in connection with the loan origination process. The Corporation will continue to modify its operations in response to the rapidly changing mortgage banking environment. Most recently, the Corporation has been increasing the number of mortgage banking personnel to capitalize on the increasing loan demand which is the result of significantly lower mortgage interest rates. Changes may also include a different product mix, further tightening of underwriting standards, variations in its operating expenses or a combination of these and other changes.

Provident Financial Corp performs trustee services for the Bank's real estate secured loan transactions and has in the past held, and may in the future hold real estate for investment. Investment services operations primarily consist of selling alternative investment products such as annuities and mutual funds to the Bank's depositors. Investment services and trustee services contribute a very small percentage of gross revenue.

There are a number of risks associated with the business activities of the Corporation, many of which are beyond the Corporation's control, including: changes in accounting principles, laws, regulation, interest rates and the economy, among others. The Corporation attempts to mitigate many of these risks through prudent banking practices, such as interest rate risk management, credit risk management, operational risk management, and liquidity risk management. The current economic environment presents heightened risk for the Corporation primarily with respect to falling real estate values and higher loan delinquencies. Declining real estate values may lead to higher loan losses since the majority of the Corporation's loans are secured by real estate located within California. Significant declines in the value of California real estate may also inhibit the Corporation's ability to recover on defaulted loans by selling the underlying real estate. The Corporation's operating costs may increase significantly as a result of the Dodd-Frank Act. Many aspects of the Dodd-Frank Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on the Corporation. For further details on risk factors, see "Safe-Harbor Statement" and "Item 1A – Risk Factors."

Off-Balance Sheet Financing Arrangements and Contractual Obligations

The following table summarizes the Corporation's contractual obligations at December 31, 2012 and the effect these obligations are expected to have on the Corporation's liquidity and cash flows in future periods (in thousands):

	Payments Due by Period				
	Less than 1 year	1 to less than 3 years	3 to 5 years	Over 5 years	Total
Operating obligations	$ 1,778	$ 1,718	$ 927	$ 572	$ 4,995
Pension benefits	-	209	419	7,182	7,810
Time deposits	237,607	175,040	19,539	1,704	433,890
	77,990	12,740	2,753	44,285	137,768

FHLB – San Francisco advances					
FHLB – San Francisco letter of credit	10,000	-	-	-	10,000
FHLB – San Francisco MPF credit enhancement (1)	2,854	-	-	-	2,854
Total	$ 330,229	$ 189,707	$ 23,638	$ 53,743	$ 597,317

(1) Represents the recourse provision for loans previously sold by the Bank to the FHLB – San Francisco under its Mortgage Partnership Finance ("MPF") program. The FHLB – San Francisco discontinued the MPF program on October 6, 2006. As of December 31, 2012, the Bank serviced $59.9 million of loans under this program.

The expected obligation for time deposits and FHLB – San Francisco advances include anticipated interest accruals based on the respective contractual terms.

In addition to the off-balance sheet financing arrangements and contractual obligations mentioned above, the Corporation has derivatives and other financial instruments with off-balance sheet risks as described in Note 7 of the Notes to Unaudited Interim Condensed Consolidated Financial Statements.

Comparison of Financial Condition at December 31, 2012 and June 30, 2012

Total assets decreased $12.6 million to $1.25 billion at December 31, 2012 from $1.26 billion at June 30, 2012. The decrease was primarily attributable to decreases in cash and cash equivalents and loans held for investment, partly offset by an increase in loans held for sale.

Total cash and cash equivalents, primarily excess cash deposited with the Federal Reserve Bank of San Francisco, decreased $45.5 million, or 31 percent, to $99.6 million at December 31, 2012 from $145.1 million at June 30, 2012. The decrease was primarily attributable to the increase in loans held for sale, partly offset by a decrease in loans held for investment. The relatively high balance in cash and cash equivalents were consistent with the Corporation's strategy of managing credit and liquidity risk.

Total investment securities decreased $1.7 million, or seven percent, to $21.2 million at December 31, 2012 from $22.9 million at June 30, 2012. The decrease was primarily the result of scheduled and accelerated principal payments on mortgage-backed securities. For further analysis on investment securities, see Note 5 of the Notes to Unaudited Interim Condensed Consolidated Financial Statements.

Loans held for investment decreased $24.7 million, or three percent, to $772.1 million at December 31, 2012 from $796.8 million at June 30, 2012. Total loan principal payments during the first six months of fiscal 2013 were $70.4 million, a three percent increase from $68.4 million in the comparable period in fiscal 2012. In addition, real estate owned acquired in the settlement of loans in the first six months of fiscal 2013 was $6.8 million, a 44 percent decline from $12.1 million in the same period last year. During the first six months of fiscal 2013, the Corporation originated $45.1 million of loans held for investment, consisting primarily of multi-family and commercial real estate loans, compared to $29.1 million, primarily in multi-family loans, for the same period last year. During the first six months of fiscal 2013, the Corporation did not purchase any loans to be held for investment. This compares to the same period in fiscal 2012 when the Corporation purchased $7.1 million of loans to be held for investment, consisting primarily of multi-family loans. The balance of preferred loans decreased to $365.4 million at December 31, 2012, compared to $375.9 million at June 30, 2012, and represented 46 percent of loans held for investment at both dates. There were no construction loans outstanding at December 31, 2012 and June 30, 2012. The balance of single-family loans held for investment decreased four percent to $422.5 million at December 31, 2012, compared to $439.0 million at June 30, 2012, and represented approximately 54 percent of loans held for investment at both dates.

The table below describes the geographic dispersion of real estate secured loans held for investment at December 31, 2012 and June 30, 2012, as a percentage of the total dollar amount outstanding (dollars in thousands):

As of December 31, 2012

	Inland Empire		Southern California (1)		Other California		Other States		Total	
Loan Category	Balance	%	Balance	%	Balance	%	Balance	%	Balance	%
Single-family	$ 126,866	30%	$ 230,302	54%	$ 61,696	15%	$ 3,593	1%	$ 422,457	100%
Multi-family	39,321	15%	164,648	63%	54,129	21%	3,482	1%	261,580	100%

Commercial real estate	54,783	54%	45,022	44%	1,816	2%	-	-%	101,621	100%
Other	390	100%	-	-%	-	-%	-	-%	390	100%
Total	$ 221,360	28%	$ 439,972	56%	$ 117,641	15%	$ 7,075	1%	$ 786,048	100%

(1) Other than the Inland Empire.

As of June 30, 2012

Loan Category	Inland Empire Balance	%	Southern California (1) Balance	%	Other California Balance	%	Other States Balance	%	Total Balance	%
Single-family	$ 133,874	31%	$ 237,715	54%	$ 63,432	14%				