PROVIDENT FINANCIAL HOLDINGS INC
Form 10-Q
November 13, 2009

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended …………………………………….... September 30, 2009

[ ] 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 X . No .

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See 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 [ ]   Non-accelerated filer [ ]
Smaller reporting company [X]

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

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 November 12, 2009
Common stock, $ 0.01 par value, per share	6,220,454 shares

PROVIDENT FINANCIAL HOLDINGS, INC.

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PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Financial Condition
(Unaudited)
Dollars in Thousands

	September 30, 2009	June 30, 2009
Assets		
Cash and cash equivalents	$ 98,416	$ 56,903
Investment securities – available for sale, at fair value	54,502	125,279
Loans held for investment, net of allowance for loan losses of $58,013 and $45,445, respectively	1,108,536	1,165,529
Loans held for sale, at fair value	130,088	135,490
Loans held for sale, at lower of cost or market	-	10,555
Accrued interest receivable	5,560	6,158
Real estate owned, net	12,693	16,439
Federal Home Loan Bank (“FHLB”) – San Francisco stock	33,023	33,023
Premises and equipment, net	6,190	6,348
Prepaid expenses and other assets	30,730	23,889
Total assets	$ 1,479,738	$ 1,579,613
Liabilities and Stockholders’ Equity		
Liabilities:		
Non interest-bearing deposits	$ 43,476	$ 41,974
Interest-bearing deposits	888,445	947,271
Total deposits	931,921	989,245
Borrowings	416,681	456,692
Accounts payable, accrued interest and other liabilities	22,233	18,766
Total liabilities	1,370,835	1,464,703
Commitments and Contingencies		
Stockholders’ equity:		
Preferred stock, $.01 par value (2,000,000 shares authorized; none issued and outstanding)	-	-
Common stock, $.01 par value (15,000,000 shares authorized; 12,435,865 and 12,435,865 shares issued, respectively; 6,220,454 and 6,219,654 shares outstanding, respectively)	124	124
Additional paid-in capital	72,978	72,709
Retained earnings	129,542	134,620
Treasury stock at cost (6,215,411 and 6,216,211 shares, respectively)	(93,942)	(93,942)
Unearned stock compensation	(406)	(473)
Accumulated other comprehensive income, net of tax	607	1,872
Total stockholders’ equity	108,903	114,910

Total liabilities and stockholders’ equity	$ 1,479,738	$ 1,579,613

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

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PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Operations
(Unaudited)
Dollars in Thousands, Except (Loss) Earnings Per Share

	Quarter Ended	
	September 30, 2009	September 30, 2008
Interest income:		
Loans receivable, net	$ 18,148	$ 20,658
Investment securities	1,095	1,905
FHLB – San Francisco stock	69	449
Interest-earning deposits	54	1
Total interest income	19,366	23,013
Interest expense:		
Checking and money market deposits	326	330
Savings deposits	521	569
Time deposits	3,904	6,127
Borrowings	4,509	4,694
Total interest expense	9,260	11,720
Net interest income, before provision for loan losses	10,106	11,293
Provision for loan losses	17,206	5,732
Net interest (expense) income, after provision for loan losses	(7,100)	5,561
Non-interest income:		
Loan servicing and other fees	235	248
Gain on sale of loans, net	3,143	1,191
Deposit account fees	763	758
Gain on sale of investment securities, net	1,949	356
Gain (loss) on sale and operations of real estate owned acquired in the settlement of loans, net	438	(390)
Other	478	313
Total non-interest income	7,006	2,476
Non-interest expense:		
Salaries and employee benefits	4,930	4,625
Premises and occupancy	788	716
Equipment	357	360
Professional expenses	387	360
Sales and marketing expenses	112	181
Deposit insurance premiums and regulatory assessments	716	322
Other	1,261	800

Total non-interest expense	8,551	7,364
(Loss) income before income taxes	(8,645)	673
(Benefit) provision for income taxes	(3,629)	344
Net (loss) income	$ (5,016)	$ 329
Basic (loss) earnings per share	$ (0.82)	$ 0.05
Diluted (loss) earnings per share	$ (0.82)	$ 0.05
Cash dividends per share	$ 0.01	$ 0.05

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

PROVIDENT FINANCIAL HOLDINGS, INC.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)
Dollars in Thousands
For the Quarters Ended September 30, 2009 and 2008

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Unearned Stock Compensation	Accumulated Other Comprehensive Income, Net of Tax	Total
Balance at July 1, 2009	6,219,654	$ 124	$ 72,709	$ 134,620	$ (93,942)	$ (473)	$ 1,872	$ 114,910
Comprehensive loss:								
Net loss				(5,016)				(5,016)
Unrealized holding loss on securities available for sale, net of tax benefit of $(916)							(1,265)	(1,265)
Total comprehensive loss								(6,281)
Distribution of restricted stock	800							-
Amortization of restricted stock			106					106
Stock options expense			117					117
Allocations of contribution to ESOP (1)			46			67		113
Cash dividends				(62)				(62)
Balance at September 30, 2009	6,220,454	$ 124	$ 72,978	$ 129,542	$ (93,942)	$ (406)	$ 607	$ 108,903

(1) Employee Stock Ownership Plan ("ESOP").

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Unearned Stock Compensation	Accumulated Other Compre-hensive Income	Total
Balance at July 1, 2008	6,207,719	$ 124	$ 75,164	$ 143,053	$ (94,798)	$ (102)	$ 539	$ 123,980

Comprehensive income:								
Net income				329				329
Unrealized holding gain on securities available for sale, net of tax expense of $60							83	83
Total comprehensive income								412
Awards of restricted stock			(868)		868			-
Distribution of restricted stock	800							-
Amortization of restricted stock			95					95
Stock options expense			183					183
Allocations of contribution to ESOP			61			80		141
Cash dividends				(310)				(310)
Balance at September 30, 2008	6,208,519	$ 124	$ 74,635	$ 143,072	$ (93,930)	$ (22)	$ 622	$ 124,501

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)

	Three Months Ended September 30, 2009	2008
Cash flows from operating activities:		
Net (loss) income	$ (5,016)	$ 329
Adjustments to reconcile net (loss) income to net cash provided by (used for) operating activities:		
Depreciation and amortization	433	504
Provision for loan losses	17,206	5,732
Recovery of losses on real estate owned	(252)	(186)
Gain on sale of loans, net	(3,143)	(1,191)
Net gain on sale of investment securities	(1,949)	(356)
Net (gain) loss on sale of real estate owned	(634)	133
Stock-based compensation	335	395
FHLB – San Francisco stock dividend	-	(491)
(Decrease) increase in accounts payable and other liabilities	(935)	2,055
Increase in prepaid expense and other assets	(6,102)	(76)
Loans originated for sale	(491,575)	(166,002)
Proceeds from sale of loans and net change in receivable from sale of loans	515,835	157,173
Net cash provided by (used for) operating activities	24,203	(1,981)
Cash flows from investing activities:		
Net decrease in loans held for investment	32,107	32,414
Principal payments from investment securities	13,384	8,315
Purchase of investment securities available for sale	-	(8,135)
Proceeds from sale of investment securities available for sale	57,080	480
Proceeds from sale of real estate owned	12,215	8,410
Purchase of premises and equipment	(80)	(380)
Net cash provided by investing activities	114,706	41,104
Cash flows from financing activities:		
Net decrease in deposits	(57,324)	(56,613)
Repayments of short-term borrowings, net	-	(60,200)
Proceeds from long-term borrowings	-	80,000
Repayments of long-term borrowings	(40,011)	(5,011)
ESOP loan payment	1	5
Cash dividends	(62)	(310)
Net cash used for financing activities	(97,396)	(42,129)
Net increase (decrease) in cash and cash equivalents	41,513	(3,006)
Cash and cash equivalents at beginning of period	56,903	15,114
Cash and cash equivalents at end of period	$ 98,416	$ 12,108

Supplemental information:		
Cash paid for interest	$ 9,298	$ 11,302
Cash paid for income taxes	$ 125	$ 874
Transfer of loans held for sale to loans held for investment	$ -	$ 611
Real estate acquired in the settlement of loans	$ 11,847	$ 10,473

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

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

September 30, 2009

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 financial statements at June 30, 2009 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 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, 2009. The results of operations for the quarter ended September 30, 2009 are not necessarily indicative of results that may be expected for the entire fiscal year ending June 30, 2010.

Note 2: Recent Accounting Pronouncements

Accounting Standards Update No. 2009-1:
In June 2009, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2009-1, Topic 105, "Generally Accepted Accounting Principles amendments based on Statement of Financial Standards ("SFAS") No. 168 - the FASB Accounting Standard Codification and the Hierarchy of Generally Accepted Accounting Principles." This Accounting Standards Update amends the FASB Accounting Standards Codification for the issuance of FASB Statement No. 168, "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles." This Accounting Standards Update includes Statement No. 168 in its entirety, including the accounting standards update instructions contained in Appendix B of the Statement. The Corporation adopted the FASB Codification on July 1, 2009, which did not have a material impact on the Corporation's consolidated financial statements.

ASC 105:
In June 2009, the FASB issued ASC 105, "Generally Accepted Accounting Principles," a replacement of previous statement, "The Hierarchy of Generally Accepted Accounting Principles." The FASB Accounting Standards Codification ("Codification") is the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of this ASC, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other non-grandfathered non-SEC accounting literature not included in the Codification will become non-authoritative. ASC 105 is effective for interim and annual financial statements issued after September 15, 2009. The Corporation adopted this Statement on July 1, 2009, which did not have a material impact on the Corporation's consolidated financial statements in terms of Codification references.

SFAS No. 167:

In June 2009, the FASB issued SFAS No. 167, “Amendments to FASB Interpretation No. 46 (R),” to improve financial reporting by enterprises involved with variable interest entities (“VIEs”). SFAS No. 167 addresses: (1) the effects on certain provisions of FASB Interpretation No. (“FIN”) 46R, “Consolidation of Variable Interest Entities,” as a result of the elimination of the qualifying SPE concept in SFAS No. 166, and (2) constituent concerns about the application of certain key provisions of FIN 46R, including those in which the accounting and disclosures under FIN 46R do not always provide timely and useful information about an enterprise’s involvement in a VIE. SFAS No. 167 is effective at the beginning of each reporting entity’s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual periods thereafter.

Early adoption is prohibited. The Corporation will be required to adopt SFAS 167 on July 1, 2010, and has not yet assessed the impact of the adoption of this standard on the Corporation's consolidated financial statements.

SFAS No. 166:
In June 2009, the FASB issued SFAS No. 166, "Accounting for Transfers of Financial Assets," an amendment of ASC 860, "Transfers and Servicing." This statement is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. SFAS No. 166 addresses (1) practices that have developed since the issuance of SFAS No. 140 that are not consistent with the original intent and key requirements of that statement, and (2) concerns of financial statement users that many of the financial assets (and related obligations) that have been derecognized should continue to be reported in the financial statements of transferors. SFAS No. 166 is effective at the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual periods thereafter. Early adoption is prohibited. This statement must be applied to transfers occurring on or after the effective date. However, the disclosure provisions of this statement should be applied to transfers that occurred both before and after the effective date. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity ("SPE") is no longer relevant for accounting purposes. Therefore, formerly qualifying SPEs, as defined under previous accounting standards, should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. The Corporation will be required to adopt SFAS 167 on July 1, 2010, and has not yet assessed the impact of the adoption of this standard on the Corporation's consolidated financial statements.

ASC 715-20-65-2:
In December 2008, the FASB issued ASC 715-20-65-2, "Employer's Disclosures about Postretirement Benefit Plan Asset," which amends ASC 715-20, "Employer's Disclosures about Pensions and Other Postretirement Benefits," to provide guidance on employers' disclosures about plan assets of a defined benefit pension or other postretirement plan. The objectives of the disclosures are to provide users of financial statements with an understanding of the plan investment policies and strategies regarding investment allocation, major categories of plan assets, use of fair valuation inputs and techniques, effect of fair value measurements using significant unobservable inputs (i.e., level 3 inputs), and significant concentrations of risk within plan assets. ASC 715-20-65-2 is effective for financial statements issued for fiscal years beginning after December 15, 2009, with early adoption permitted. This ASC does not require comparative disclosures for earlier periods. Management has not determined the impact of this ASC on the Corporation's consolidated financial statements.

Note 3: Earnings (Loss) Per Share and Stock-Based Compensation

Earnings (Loss) Per Share:
Basic earnings per share ("EPS") excludes dilution and is computed by dividing income or loss 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 September 30, 2009 and 2008, there were outstanding options to purchase 905,500 shares and 907,700 shares of the Corporation's common stock, respectively, of which 905,500 shares and 658,200 shares, respectively, were excluded from the diluted EPS computation as their effect was anti-dilutive. As of September 30, 2009 and 2008, there was outstanding unvested restricted stock of 135,500 shares and 148,900 shares, respectively, also excluded from the diluted EPS computation as their effect was anti-dilutive.

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The following table provides the basic and diluted EPS computations for the quarters ended September 30, 2009 and 2008, respectively.

(In Thousands, Except (Loss) Earnings Per Share)	For the Quarter Ended September 30, 2009	2008
Numerator:		
Net (loss) income – numerator for basic (loss) earnings per share and diluted (loss) earnings per share - available to common stockholders	$ (5,016)	$ 329
Denominator:		
Denominator for basic (loss) earnings per share:		
Weighted-average shares	6,114	6,186
Effect of dilutive securities:		
Stock option dilution	-	-
Restricted stock dilution	-	-
Denominator for diluted (loss) earnings per share:		
Adjusted weighted-average shares and assumed conversions	6,114	6,186
Basic (loss) earnings per share	$ (0.82)	$ 0.05
Diluted (loss) earnings per share	$ (0.82)	$ 0.05

ASC 718, "Compensation – Stock Compensation," requires companies to recognize in the statement of operations the grant-date fair value of stock options and other equity-based compensation issued to employees and directors. Effective July 1, 2005, the Corporation adopted ASC 718 using the modified prospective method under which the provisions of ASC 718 are applied to new awards and to awards modified, repurchased or cancelled after June 30, 2005 and to awards outstanding on June 30, 2005 for which requisite service has not yet been rendered. The adoption of ASC 718 resulted in incremental stock-based compensation expense and is solely related to issued and unvested stock option grants.

For the first three months of fiscal 2010 and 2009, there was no cash provided by operating activities and financing activities related to excess tax benefits from stock-based payment arrangements.

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 September 30, 2009 and 2008, respectively (in thousands).

	For the Quarter Ended September 30, 2009		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income, before provision for loan losses	$ 9,290	$ 816	$ 10,106
Provision for loan losses	16,713	493	17,206
Net interest (expense) income, after provision for loan losses	(7,423)	323	(7,100)
Non-interest income:			
Loan servicing and other fees	224	11	235
Gain on sale of loans, net	4	3,139	3,143
Deposit account fees	763	-	763
Gain on sale of investment securities	1,949	-	1,949
Gain (loss) on sale and operations of real estate owned acquired in the settlement of loans, net	468	(30)	438
Other	478	-	478
Total non-interest income	3,886	3,120	7,006
Non-interest expense:			
Salaries and employee benefits	2,699	2,231	4,930
Premises and occupancy	619	169	788
Operating and administrative expenses	1,740	1,093	2,833
Total non-interest expense	5,058	3,493	8,551
Loss before income taxes	(8,595)	(50)	(8,645)
Benefit for income taxes	(3,608)	(21)	(3,629)
Net loss	$ (4,987)	$ (29)	$ (5,016)
Total assets, end of period	$ 1,350,724	$ 129,014	$ 1,479,738

	For the Quarter Ended September 30, 2008		
	Provident Bank	Provident Bank Mortgage	Consolidated Totals
Net interest income before provision for loan losses	$ 11,182	$ 111	$ 11,293
Provision for loan losses	4,878	854	5,732
Net interest income (expense), after provision for loan losses	6,304	(743)	5,561
Non-interest income:			
Loan servicing and other fees (1)	105	143	248
Gain on sale of loans, net	3	1,188	1,191
Deposit account fees	758	-	758
Gain on sale of investment securities	356	-	356
Loss on sale and operations of real estate owned acquired in the settlement of loans, net	(313)	(77)	(390)
Other	312	1	313
Total non-interest income	1,221	1,255	2,476
Non-interest expense:			
Salaries and employee benefits	3,390	1,235	4,625
Premises and occupancy	592	124	716
Operating and administrative expenses	1,130	893	2,023
Total non-interest expense	5,112	2,252	7,364
Income (loss) before income taxes	2,413	(1,740)	673
Provision (benefit) for income taxes	1,076	(732)	344
Net income (loss)	$ 1,337	$ (1,008)	$ 329
Total assets, end of period	$ 1,552,213	$ 41,687	$ 1,593,900

(1) Includes an inter-company charge of $102 credited to PBM by the Bank during the period to compensate PBM for originating loans held for investment.

Note 5: 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, and loan sale commitments to third parties. 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 September 30, 2009 and June 30, 2009, the Corporation had commitments to extend credit (on loans to be held for investment and loans to be

held for sale) of $131.5 million and $105.7 million, respectively. The following table provides information regarding undisbursed funds to borrowers on existing loans and lines of credit with the Bank as well as commitments to originate loans to be held for investment.

Commitments	September 30, 2009	June 30, 2009
(In Thousands)		
Undisbursed loan funds – Construction loans	$ 75	$ 305
Undisbursed lines of credit – Mortgage loans	1,782	2,171
Undisbursed lines of credit – Commercial business loans	3,570	4,148
Undisbursed lines of credit – Consumer loans	1,320	1,617
Commitments to extend credit on loans to be held for investment	350	1,053
Total	$ 7,097	$ 9,294

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, commitments to purchase mortgage-backed securities ("MBS"), put option contracts and call option contracts are recorded at fair value on the Condensed Consolidated Statements of Financial Condition , and are included in other assets or 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 net impact of derivative financial instruments on the Condensed Consolidated Statements of Operations during the quarters ended September 30, 2009 and 2008 were a loss of $(2.6) million and a loss of $(152,000), respectively.

	September 30, 2009		June 30, 2009		September 30, 2008	
Derivative Financial Instruments	Amount	Fair Value	Amount	Fair Value	Amount	Fair Value
(In Thousands)						
Commitments to extend credit on loans to be held for sale (1)	$ 131,149	$ 2,231	$ 104,630	$ 1,316	$ 32,253	$ (456)
Best efforts loan sale commitments	(2,051)	-	(12,834)	-	(71,363)	-
Mandatory loan sale commitments	(259,529)	(2,835)	(207,239)	656	-	-
Total	$ (130,431)	$ (604)	$ (115,443)	$ 1,972	$ (39,110)	$ (456)

(1) Net of 36.4 percent at September 30, 2009, 34.5 percent at June 30, 2009 and 41.0 percent at September 30, 2008 of commitments, which may not fund.

Note 6: 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, and none are anticipated during the fiscal year ending June 30, 2010.

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 Corporation's tax asset has increased during the first three months of fiscal 2010 due to an increase in its loan loss allowances. The deferred tax asset related to loan loss allowances will be realized when actual charge-offs are made against the loan loss allowances. Based on the availability of loss carry-backs and projected taxable income during the periods for which loss carry-forwards are available, management does believes it is more likely than not the Corporation will realize the deferred tax asset. As of

September 30, 2009, the Corporation has estimated the deferred tax asset of $16.6 million and current tax receivables of $3.6 million.

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. The Internal Revenue Service also completed a review of the Corporation's income tax returns for fiscal 2006 and 2007. Tax years subsequent to 2007 remain subject to federal examination, while the California state tax returns for years subsequent to 2004 are subject to examination by taxing authorities. It is the Corporation's policy to record any penalties or interest arising from federal or state taxes as a component of income tax expense. There were no penalties or interest included in the Condensed Consolidated Statements of Operations for the quarter ended September 30, 2009.

Note 7: Fair Value of Financial Instruments

The Corporation adopted ASC 820, "Fair Value Measurements and Disclosures," on July 1, 2008 and elected the fair value option (ASC 825, "Financial Instruments") on May 28, 2009 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 statement is to provide entities with the opportunity to mitigate volatility in earnings caused by measuring related assets and liabilities differently without having to apply complex accounting provisions.

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

(Dollars In Thousands)	Aggregate Fair Value	Aggregate Unpaid Principal Balance	Difference or Gain
As of September 30, 2009:			
Single-family loans measured at fair value	$ 130,088	$ 126,527	$ 3,561

On April 9, 2009, the FASB issued 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." This ASC 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 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 and real estate owned are measured at fair value on a nonrecurring basis.

Investment securities are primarily comprised of U.S. government sponsored enterprise debt securities, U.S. government agency mortgage-backed securities, U.S. government sponsored enterprise mortgage-backed securities and private issue collateralized mortgage obligations. The Corporation utilizes unadjusted quoted prices in active markets for identical securities (Level 1) for its fair value measurement of debt securities, quoted prices in active and less than active markets for similar securities (Level 2) for its fair value measurement of mortgage-backed securities and broker price indications for similar securities in non-active markets (Level 3) for its fair value measurement of collateralized mortgage obligations ("CMO").

Derivative financial instruments are comprised of commitments to extend credit on loans to be held for sale and mandatory loan sale commitments. The fair value is determined, when possible, using quoted secondary-market prices. If no such quoted price exists, the fair value of a commitment is determined by quoted prices for a similar commitment or commitments, adjusted for the specific attributes of each commitment.

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.

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 Bank will sustain some loss if the deficiencies are not corrected. The fair value of an impaired loan is determined based on an observable market price or current appraised value of the underlying collateral, less selling costs. 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 also restructured loans, the fair value is derived from discounted cash flow analysis, except those which are in the process of foreclosure, the fair value is derived from the appraisal value of its collateral, less selling costs. Non-performing loans are reviewed and evaluated on at least a quarterly basis for additional impairment 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, but rather as a component in determining the overall adequacy of the allowance for losses on loans. These adjustments to the estimated fair value of non-performing loans may result in increases or decreases to the provision for losses on loans recorded in current earnings.

The Corporation uses the amortization method for its mortgage servicing assets, which amortizes servicing assets in proportion to and over the period of estimated net servicing income and assesses servicing assets for impairment based on fair value at each reporting date. The fair value of mortgage servicing assets are 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.

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 are calculated using the same assumptions that are used to value the related servicing assets.

The fair value of real estate owned is derived from the lower of the appraisal value at the time of foreclosure, less selling costs or the list price provided by an independent realtor, less selling costs.

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 about the Corporation's assets measured at fair value on a recurring basis:

	Fair Value Measurement at September 30, 2009 Using:			
(Dollars in Thousands)	Level 1	Level 2	Level 3	Total
Investment securities	$ 5,369	$ 47,618	$ 1,515	$ 54,502
Loans held for sale, at fair value	-	130,088	-	130,088
Interest-only strips	-	-	298	298
Derivative financial instruments	-	(1,511)	907	(604)
Total	$ 5,369	$ 176,195	$ 2,720	$ 184,284

	Fair Value Measurement at June 30, 2009 Using:			
(Dollars in Thousands)	Level 1	Level 2	Level 3	Total
Investment securities	$ 5,353	$ 118,500	$ 1,426	$ 125,279
Loans held for sale, at fair value	-	135,490	-	135,490
Interest-only strips	-	-	294	294
Derivative financial instruments	-	(97)	2,069	1,972
Total	$ 5,353	$ 253,893	$ 3,789	$ 263,035

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

	Fair Value Measurement Using Significant Other Unobservable Inputs (Level 3)			
(Dollars in Thousands)	CMO	Interest-Only Strips	Derivative Financial Instruments	Total
Beginning balance at July 1, 2009	$ 1,426	$ 294	$ 2,069	$ 3,789
Total gains or losses (realized/unrealized):				
Included in earnings	-	(19)	(2,069)	(2,088)
Included in other comprehensive income	170	23	-	193
Purchases, issuances, and settlements	(81)	-	907	826
Transfers in and/or out of Level 3	-	-	-	-
Ending balance at September 30, 2009	$ 1,515	$ 298	$ 907	$ 2,720

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

	Fair Value Measurement at September 30, 2009 Using:			
(Dollars in Thousands)	Level 1	Level 2	Level 3	Total
Non-performing loans	$ -	$ 46,498	$ 28,123	$ 74,621
Mortgage servicing assets	-	-	73	73
Real estate owned	-	12,693	-	12,693
Total	$ -	$ 59,191	$ 28,196	$ 87,387

Note 8: Subsequent Events

Management has evaluated events through November 16, 2009, which is the date that the financial statements were issued. No material subsequent events have occurred since September 30, 2009 that would require recognition or disclosure in these condensed consolidated financial statements, except for the following:

On October 9, 2009, the Corporation filed a registration statement with the Securities and Exchange Commission for a proposed public offering of up to $46.0 million of the Corporation's common stock in an underwritten public offering.

On October 29, 2009, the Corporation announced a cash dividend of $0.01 per share on the Corporation's outstanding shares of common stock for shareholders of record as of the close of business on November 20, 2009, payable on December 16, 2009.

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. At September 30, 2009, the Corporation had total assets of $1.48 billion, total deposits of $931.9 million and total stockholders' equity of $108.9 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.

The Bank, founded in 1956, is a federally chartered stock savings bank headquartered in Riverside, California. The Bank is regulated by the Office of Thrift Supervision ("OTS"), 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 Bank's business consists of community banking activities and mortgage banking activities, operated by 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 and sale of mortgage and consumer loans secured primarily by single-family residences. The Bank currently operates 14 retail/business banking offices in Riverside County and San Bernardino County (commonly known as the Inland Empire), including the newly opened Iris Plaza office in Moreno Valley, California. Provident Bank Mortgage operates wholesale loan production offices in Pleasanton and Rancho Cucamonga, California and retail loan production offices in Glendora and Riverside, California. The Bank'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 Bank'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 for sale of loans, competitive conditions, legislative and regulatory changes, fraud and other risks.

The Corporation, from time to time, may repurchase its common stock. The Corporation evaluates the repurchase of its common stock when the market price of the stock is lower than its book value and/or the Corporation believes that the current market price is not commensurate with its current and future earnings potential. Consideration is also given to the Corporation's liquidity, regulatory capital requirements and future capital needs based on the Corporation's current business plan. The Corporation's Board of Directors authorizes each stock repurchase program, the duration of which is typically one year. Once the stock repurchase program is authorized, management may repurchase the Corporation's common stock from time to time in the open market or in privately negotiated transactions, depending upon market conditions and the factors described above. See Part II, Item 2 – "Unregistered Sales of Equity Securities and Use of Proceeds" on page 47.

The Corporation began to distribute quarterly cash dividends in the quarter ended September 30, 2002. On July 23, 2009, the Corporation declared a quarterly cash dividend of $0.01 per share for the Corporation's shareholders of record at the close of business on August 17, 2009, which was paid on September 11, 2009. On October 29, 2009, the Corporation announced a cash dividend of $0.01 per share on the Corporation's outstanding shares of common stock for shareholders of record as of the close of business on November 20, 2009, payable on December 16, 2009. 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

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. The Corporation does not undertake and specifically disclaims any obligation to revise any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements. These risks could cause our actual results for fiscal 2010 and beyond to differ materially from those expressed in any forward-looking statements by, or on behalf of, us, and could negatively affect the Corporation's operating and stock price performance. Factors which could cause actual results to differ materially include, but are not limited to the Corporation's ability to raise common capital and the amount of capital it intends to raise, and the credit risks of lending activities, including changes in the level and trend of loan delinquencies and write-offs and changes in our allowance for loan losses and provision for loan losses that may be impacted by deterioration in the housing and commercial real estate markets; 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 us by the OTS or other regulatory authorities, including the possibility that any such regulatory authority may, among other things, require us to increase our reserve for loan losses, write-down assets, change our regulatory capital position or affect our ability to borrow funds or maintain or increase deposits, which could adversely affect our liquidity and earnings; legislative or regulatory changes that adversely affect our business including changes in regulatory policies and principles, or the interpretation of regulatory capital or other rules; our ability to attract and retain deposits; further 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 retain key members of our senior management team; costs and effects of litigation, including settlements and judgments; 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; 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; 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 FASB, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting

methods; and other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services and the other risks described detailed in the Corporation's reports filed with the SEC, including its Annual Report on Form 10-K for the fiscal year ended June 30, 2009.

Critical Accounting Policies

The discussion and analysis of the Corporation's financial condition and results of operations is based upon the Corporation's condensed 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 have a material impact on the carrying value of net loans. Management considers this accounting policy to be a critical accounting policy. 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," which require that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance. The allowance has two components: a formula allowance for groups of homogeneous loans and a specific valuation allowance for identified problem loans. Each of these components is based upon estimates that can change over time. The formula allowance is based primarily on historical experience and as a result can differ from actual losses incurred in the future. The history is reviewed at least quarterly and adjustments are made as needed. Various techniques are used to arrive at specific loss estimates, including historical loss information, discounted cash flows and the fair market value of collateral. The use of these techniques is inherently subjective and the actual losses could be greater or less than the estimates.

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-accrual 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.

ASC 815 requires that derivatives of the Corporation be recorded in the consolidated financial statements at fair value. Management considers this accounting policy to be a critical accounting policy. The Bank's derivatives are primarily the result of its mortgage banking activities in the form of commitments to extend credit, commitments to sell loans, commitments to sell MBS 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 consolidated statements of operations with offsets to other assets or other liabilities in the 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. Management's judgment is required in determining the amount and timing of recognition of the resulting deferred tax assets and liabilities, including projections of future taxable income. 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 Bank's full service offices and investing those funds in single-family, multi-family, commercial real estate, construction, commercial business, consumer and other loans. 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, and wire transfer fees, among others. 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. During the next three years, although not immediately given the uncertain environment, the Corporation intends to improve the 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 multi-family, commercial real estate, construction and commercial business loans (which are sometimes referred to in this report as "preferred loans"). In addition, over time, 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 has determined that deleveraging the balance sheet is the most prudent short-term strategy in response to current weaknesses in general economic conditions. Deleveraging the balance sheet improves capital ratios and mitigates credit and liquidity risk.

Mortgage banking operations primarily consist of the origination 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, 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, regulation and 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 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 inhibit the Corporation's ability to recover on defaulted loans by selling the underlying real estate. For further details on risk factors, see the "Safe-Harbor Statement" on page 15 and "Item 1A – Risk Factors" on page 39.

Off-Balance Sheet Financing Arrangements and Contractual Obligations

The following table summarizes the Corporation's contractual obligations at September 30, 2009 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				
	1 year or less	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years	Total
Operating obligations	$ 787	$ 1,235	$ 283	$ -	$ 2,305

Pension benefits	182	396	396	5,844	6,818
Time deposits	432,148	80,105	56,693	3,470	572,416
FHLB – San Francisco advances	91,674	247,054	93,794	18,816	451,338
FHLB – San Francisco letter of credit	5,000	-	-	-	5,000
FHLB – San Francisco MPF credit enhancement	3,147	-	-	-	3,147
Total	$ 532,938	$ 328,790	$ 151,166	$ 28,130	$ 1,041,024

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 5 of the Notes to Unaudited Interim Consolidated Financial Statements on page 9.

Comparison of Financial Condition at September 30, 2009 and June 30, 2009

Total assets decreased $99.9 million, or six percent, to $1.48 billion at September 30, 2009 from $1.58 billion at June 30, 2009. The decrease was primarily attributable to decreases in investment securities and loans held for investment, partly offset by an increase in cash and cash equivalents. The decline in total assets and the increase in cash and cash equivalents are consistent with the Corporation strategy of deleveraging the balance sheet to improve capital ratios and to mitigate credit and liquidity risk.

Total cash and cash equivalents, primarily excess cash at the Federal Reserve Bank of San Francisco, increased $41.5 million, or 73 percent, to $98.4 million at September 30, 2009 from $56.9 million at June 30, 2009.

Total investment securities decreased $70.8 million, or 57 percent, to $54.5 million at September 30, 2009 from $125.3 million at June 30, 2009. The decrease was primarily the result of the sale of $55.0 million of investment securities for a net gain of $1.9 million as well as the scheduled and accelerated principal payments on mortgage-backed securities. The Bank evaluates individual investment securities quarterly for other-than-temporary declines in market value. The Bank does not believe that there are any other-than-temporary impairments at September 30, 2009; therefore, no impairment losses have been recorded as of September 30, 2009.

Loans held for investment decreased $57.0 million, or five percent, to $1.11 billion at September 30, 2009 from $1.17 billion at June 30, 2009. Total loan principal payments during the first three months of fiscal 2010 were $37.6 million, compared to $50.9 million during the comparable period in fiscal 2009. During the first three months of fiscal 2010, the Bank originated $105,000 of loans held for investment, all of which were single-family loans. The Bank did not purchase any loans for investment in the first three months of fiscal 2010 and 2009, given the economic uncertainty of the current banking environment. The balance of preferred loans decreased to $491.2 million, or 42 percent of loans held for investment at September 30, 2009, as compared to $508.7 million, or 42 percent of loans held for investment at June 30, 2009. Purchased loans serviced by others at September 30, 2009 were $24.0 million, or two percent of loans held for investment, compared to $125.4 million, or 11 percent of loans held for investment at June 30, 2009. The decrease in the purchased loans serviced by others was primarily attributable to the Bank's decision to acquire approximately $95.3 million of loan servicing from one of its loan servicers who no longer meets its contractual loan servicing covenants, resulting in a 25 basis point increase to the loan yield of the impacted loans.

The table below describes the geographic dispersion of real estate secured loans held for investment at September 30, 2009, as a percentage of the total dollar amount outstanding:

	Inland Empire		Southern California (1)		Other California (2)		Other States		Total	
Loan Category	Balance	%	Balance	%	Balance	%	Balance	%	Balance	%
Single-family	$204,070	30%	$365,062	55%	$ 90,964	14%	$ 8,363	1%	$668,459	100%
Multi-family	33,323	9%	259,086	72%	62,801	18%	3,669	1%	358,879	100%
Commercial real estate	61,116	51%	54,611	46%	2,352	2%	1,640	1%	119,719	100%
Construction	3,939	91%	400	9%	-	0%	-	0%	4,339	100%

Other	1,532	100%	-	0%	-	0%	-	0%	1,532	100%
Total	$303,980	26%	$679,159	59%	$156,117	14%	$13,672	1%	$1,152,928	100%

(1) Other than the Inland Empire.
(2) Other than the Inland Empire and Southern California.

Total deposits decreased $57.3 million, or six percent, to $931.9 million at September 30, 2009 from $989.2 million at June 30, 2009. The decrease was primarily attributable to the strategic decision to compete less aggressively on time deposit interest rates, partly offset by the Bank's marketing strategy to promote transaction accounts.

Borrowings, consisting of FHLB – San Francisco advances, decreased $40.0 million, or nine percent, to $416.7 million at September 30, 2009 from $456.7 million at June 30, 2009. The decrease was due to scheduled maturities and $20.0 million of prepayments due to excess liquidity. The weighted-average maturity of the Bank's FHLB – San Francisco advances was approximately 27 months (25 months, if put options are exercised by the FHLB – San Francisco) at September 30, 2009, as compared to the weighted-average maturity of 28 months (26 months, if put options were exercised by the FHLB – San Francisco) at June 30, 2009.

Total stockholders' equity decreased $6.0 million, or five percent, to $108.9 million at September 30, 2009, from $114.9 million at June 30, 2009, primarily as a result of the net loss and the quarterly cash dividends paid during the first three months of fiscal 2010. During the first three months of fiscal 2010, no stock options were exercised and no common stock was repurchased. The total cash dividend paid to the Corporation's shareholders in the first three months of fiscal 2010 was $62,000.

Comparison of Operating Results for the Quarters Ended September 30, 2009 and 2008

The Corporation's net loss for the quarter ended September 30, 2009 was $(5.0) million, compared to net income of $329,000 during the same quarter of fiscal 2009. The decrease in net earnings was primarily a result of an increase in the provision for loan losses, partly offset by an increase in non-interest income.

The Corporation's efficiency ratio, defined as non-interest expense divided by the sum of net interest income (before provision for loan losses) and non-interest income, improved to 50 percent in the first quarter of fiscal 2010 from 53 percent in the same period of fiscal 2009. The improvement in the efficiency ratio was a result of an increase in non-interest income, partly offset by a decrease in net interest income (before provision for loan losses) and an increase in non-interest expense.

(Loss) return on average assets for the quarter ended September 30, 2009 decreased 136 basis points to (1.28) percent from 0.08 percent in the same period last year. (Loss) return on average equity for the quarter ended September 30, 2009 decreased to (17.68) percent from 1.06 percent for the same period last year. Diluted (loss) earnings per share for the quarter ended September 30, 2009 were $(0.82), compared to $0.05 for the quarter ended September 30, 2008.

Net Interest Income:
Net interest income (before the provision for loan losses) decreased $1.2 million, or 11 percent, to $10.1 million for the quarter ended September 30, 2009 from $11.3 million in the comparable period in fiscal 2009 due primarily to declines in the net interest margin and average earning assets. The net interest margin was 2.69 percent in the first quarter of fiscal 2010, down 20 basis points from 2.89 percent for the same period of fiscal 2009. The decrease in the net interest margin during the first quarter of fiscal 2010 was primarily attributable to a decrease in the average yield on earning assets which declined more than the average cost of funds. The average balance of earning assets decreased $58.3 million to $1.51 billion in the first quarter of fiscal 2010 from $1.56 billion in the comparable period of fiscal 2009.

Interest Income:
Total interest income decreased by $3.6 million, or 16 percent, to $19.4 million for the first quarter of fiscal 2010 from $23.0 million in the same quarter of fiscal 2009. This decrease was primarily the result of a lower average earning asset yield and a lower average balance of earning assets. The average yield on earning assets during the first quarter of fiscal 2010 was 5.15 percent, 74 basis points lower than the average yield of 5.89 percent during the same period of fiscal 2009. The average balance of earning assets decreased $58.3 million to $1.51 billion in the first quarter of fiscal 2010 from $1.56 billion in the comparable period of fiscal 2009.

Loans receivable interest income decreased $2.6 million, or 13 percent, to $18.1 million in the quarter ended September 30, 2009 from $20.7 million for the same quarter of fiscal 2009. This decrease was attributable to a lower average loan yield and a lower average loan balance. The average loan yield during the first quarter of fiscal 2010 decreased 36 basis points to 5.65 percent from 6.01 percent during the same quarter last year. The decrease in the average loan yield was primarily attributable to accrued interest income reversals from newly classified non-accrual loans, the repricing of adjustable rate loans to lower interest rates and loan payoffs on loans which carried a higher average yield than the average yield of loans receivable. The average balance of loans outstanding, including loans held for sale, decreased $90.5 million, or seven percent, to $1.28 billion during the first quarter of fiscal 2010 from $1.38 billion in the same quarter of fiscal 2009.

Interest income from investment securities decreased $810,000, or 43 percent, to $1.1 million during the quarter ended September 30, 2009 from $1.9 million in the same quarter of fiscal 2009. This decrease was primarily a result of a decrease in the average balance and a decrease in average yield. The average balance of investment securities decreased $51.8 million, or 33 percent, to $103.0 million in the first quarter of fiscal 2010 from $154.8 million in the same quarter of fiscal 2009. The decrease in the average balance was primarily due to the sale of investment securities as well as the scheduled and accelerated principal payments on mortgage-backed securities. The average yield on investment securities decreased 67 basis points to 4.25 percent during the quarter ended September 30, 2009 from 4.92 percent during the quarter ended September 30, 2008. The decrease in the average yield of investment securities was primarily attributable to the sale of investment securities with a higher average yield, the repricing of mortgage-backed securities to lower interest rates and a higher net premium amortization ($58,000 in the first quarter of fiscal 2010 as compared to $23,000 in the comparable quarter of fiscal 2009). During the first quarter of fiscal 2010, the Bank did not purchase any investment securities, while $13.4 million of principal payments were received on mortgage-backed securities.

The FHLB – San Francisco declared a $69,000 cash dividend on its stock in the first quarter of fiscal 2010 as compared to the stock dividend of $449,000 in the same quarter last year. However, the FHLB – San Francisco has not allowed the redemption of excess capital stock because of its desire to strengthen its capital ratios.

Interest Expense:
Total interest expense for the quarter ended September 30, 2009 was $9.3 million as compared to $11.7 million for the same period of fiscal 2009, a decrease of $2.4 million, or 21 percent. This decrease was primarily attributable to a lower average cost of interest-bearing liabilities, particularly deposits, and to a much lesser extent, a lower average balance of interest-bearing liabilities. The average cost of interest-bearing liabilities, principally deposits and borrowings, was 2.57 percent during the quarter ended September 30, 2009, down 62 basis points from 3.19 percent during the same period of fiscal 2009. The average balance of interest-bearing liabilities, principally deposits and borrowings, decreased $28.1 million, or two percent, to $1.43 billion during the first quarter of fiscal 2010 from $1.46 billion during the same period of fiscal 2009.

Interest expense on deposits for the quarter ended September 30, 2009 was $4.8 million as compared to $7.0 million for the same period of fiscal 2009, a decrease of $2.2 million, or 31 percent. The decrease in interest expense on deposits was primarily attributable to a lower average cost and a slightly lower average balance. The average cost of deposits decreased to 1.93 percent during the quarter ended September 30, 2009 from 2.85 percent during the same quarter of fiscal 2009, a decrease of 92 basis points. The decrease in the average cost of deposits was attributable primarily to new time deposits with a lower average cost replacing maturing time deposits with a higher average cost, consistent with declining short-term interest rates. The average balance of deposits decreased $3.5 million to $977.5 million during the quarter ended September 30, 2009 from $981.0 million during the same period of fiscal 2009. The decline in the average balance was primarily in time deposits, the result of the Bank’s strategic decision to compete less aggressively for this product, partly offset by an increase in transaction (core) deposits. The average balance of transaction deposits to total deposits in the first quarter of fiscal 2010 was 38 percent, compared to 35 percent in the same period of fiscal 2009.

Interest expense on borrowings, consisting of FHLB – San Francisco advances, for the quarter ended September 30, 2009 decreased $185,000, or four percent, to $4.5 million from $4.7 million for the same period of fiscal 2009. The decrease in interest expense on borrowings was primarily a result of a lower average balance, partly offset by a higher average cost. The average balance of borrowings decreased $24.6 million, or five percent, to $454.3 million during the quarter ended September 30, 2009 from $478.9 million during the same period of fiscal 2009, consistent with the Corporation’s short-term deleveraging strategy. The average cost of borrowings increased to 3.94 percent for the quarter ended September 30, 2009 from 3.90 percent in the same quarter of fiscal 2009, an increase of four basis points. The increase in the average cost of borrowings was primarily the result of a lower average balance of short-term advances. Short-term advance interest rates remained at relatively low levels as a result of U.S. Treasury

and Federal Reserve Board actions.

The following table depicts the average balance sheets for the quarters ended September 30, 2009 and 2008, respectively:

Average Balance Sheets
(Dollars in thousands)

	Quarter Ended September 30, 2009			Quarter Ended September 30, 2008		
	Average Balance	Interest	Yield/ Cost	Average Balance	Interest	Yield/ Cost
Interest-earning assets:						
Loans receivable, net (1)	$ 1,284,747	$ 18,148	5.65%	$ 1,375,224	$ 20,658	6.01%
Investment securities	103,022	1,095	4.25%	154,759	1,905	4.92%
FHLB – San Francisco stock	33,023	69	0.84%	32,376	449	5.55%
Interest-earning deposits	84,610	54	0.26%	1,296	1	0.31%
Total interest-earning assets	1,505,402	19,366	5.15%	1,563,655	23,013	5.89%
Non interest-earning assets	60,539			41,338		
Total assets	$ 1,565,941			$ 1,604,993		
Interest-bearing liabilities:						
Checking and money market accounts (2)	$ 202,209	326	0.64%	$ 198,304	330	0.66%
Savings accounts	165,308	521	1.25%	141,098	569	1.60%
Time deposits	609,957	3,904	2.54%	641,562	6,127	3.80%
Total deposits	977,474	4,751	1.93%			