



# SR003\_7: Failed Bank Report

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## Washington Mutual Bank

2273 North Green Valley Parkway  
Henderson, NV 89014

(12/27/1988 – 9/25/2008)

# Report Objective

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This report has **two** objectives, using the bank's **data**\*:

1. To examine the bank finances in the quarters prior to its failure.
2. To analyze the bank finances using our Key Performance Indicator (KPI) scoring approach to determine if the bank's failure is something we could have predicted.

\*Data source: FDIC and company filings.

# Bank Background

<b>FDIC Certificate #</b>	<b>32633</b>
<b>Bank Charter Class</b>	Savings Association
<b>Asset Concentration</b>	Mortgage Lending Specialization
<b>Product Specialty</b>	Retail Banking and Financial Services, Home Loans, Commercial Banking, and Card Services
<b>Number of Branches</b>	2239 (as of June 30, 2008)
<b>Number of Employees</b>	41,360 (as of June 30, 2008)

<b>Executives</b>	
<b>CEO</b>	Alan H. Fishman
<b>Chairman</b>	Stephen E. Frank
<b>President</b>	Robert J. Williams Jr.

# What took place?

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**T**he banking operations of Washington Mutual, Inc - Washington Mutual Bank, Henderson, NV and Washington Mutual Bank, FSB, Park City, UT (Washington Mutual Bank) were sold in a transaction facilitated by the Office of Thrift Supervision (OTS) and FDIC on September 25<sup>th</sup>, 2008. The estimated cost to the FDIC Deposit Insurance Fund was \$0, as all deposits, branches, and some assets were acquired by JPMorgan Chase.

# Bank Financial Snapshot

Financial Data Overlay (thousands)			
	2007 Q2	2008 Q2	Percentage Change
<b>Assets</b>	\$ 311,053,133	\$ 307,021,614	↓ 1.30%
<b>Liabilities</b>	\$ 283,352,363	\$ 282,641,867	↓ 0.25%
<b>Net Income</b>	\$ 1,839,425	-\$ 4,272,651	↓ 332%

- The average net income change for all FDIC banks was -65.89% in the same period.
- The average net income change for all the mortgage lending specialization banks was -178% in the same period.
- Compared with the whole industry and other mortgage lending specialization banks, Washington Mutual Bank's decline from Net Income is almost twice as large (-332%) during 2008.

# Key Performance Indicators


KPI Summary for 2008 Q2	
Normalized Income Rating	Very Poor
Delinquent Asset Rating	Moderate
Asset: Liability Rating	Poor
Real Estate Asset Rating*	Poor
Bankability Composite Score	35.99** (Poor)

Possible ratings: *Excellent, Good, Moderate, Poor, Very Poor.*

\*This rating is relevant to the current “financial crisis” fueled by mortgage security backed loans.


\*\*This is out of 100.

# Normalized Income Analysis

	2007Q1	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2 
Normalized Income	0.29%	0.30%	-0.07%	-0.55%	-0.34%	-1.04%
SD's from Average*	0.196	0.309	-0.0493	-1.08	-1.00	-2.89
Ranking	Moderate	Moderate	Moderate	Poor	Poor	Very Poor

- Washington Mutual had a normalized income of -1.04% in the second quarter of 2008, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average normalized income of 0.09%. The standard deviation of the normalized incomes was 0.39%, which means that Washington Mutual was 2.89 SD's below the average.

\* Average of banks of the same asset concentration hierarchy

 Indicates sign of bank in financial distress

# Delinquent Asset Analysis

	2007Q1	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2
Delinquent Asset	0.9922%	1.1252%	1.3067%	1.6839%	1.8872%	2.0503%
SD's from Average*	-0.07	-0.04	-0.01	0.09	0.27	0.32
Ranking	Moderate	Moderate	Moderate	Moderate	Moderate	Moderate

- Washington Mutual Bank had a delinquent assets out of total assets ratio 2.05% in the second quarter of 2008, the quarter before it failed.
- Banks of the same asset concentration hierarchy (mortgage lending specialization) had an average delinquent asset of 1.4079%. The standard deviation of the delinquent assets was 2.01%, which means that Washington Mutual Bank was about 0.32 SD's above the average.
- Since the first quarter of 2007, Washington Mutual Bank 's delinquent assets ratio has been around the average in relation to banks of the same asset concentration hierarchy; even during the quarter prior to its failure, its delinquent asset ratio seems stable and normal.

\*Average of banks of the same asset concentration hierarchy

# Real Estate Loan Asset Analysis

	2007Q1	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2
Real Estate Loan Asset Ratio	72.86%	71.37%	70.69%	72.99%	74.43%	74.50%
SD's from Average*	0.59	0.51	0.47	0.59	0.74	0.74
Ranking	Moderate	Moderate	Moderate	Moderate	Poor	Poor

- Washington Mutual Bank had a 74.50% of R/A ratio in 08 Q2, the quarter before it failed.
- In 08 Q2, banks of the same asset concentration hierarchy (mortgage lending specialization) had an average R/A ratio of 58.54%. The standard deviation of the R/A ratio was 21.54%, which means that Washington Mutual Bank was 0.74 SD's above the average.

\*Average of banks of the same asset concentration hierarchy

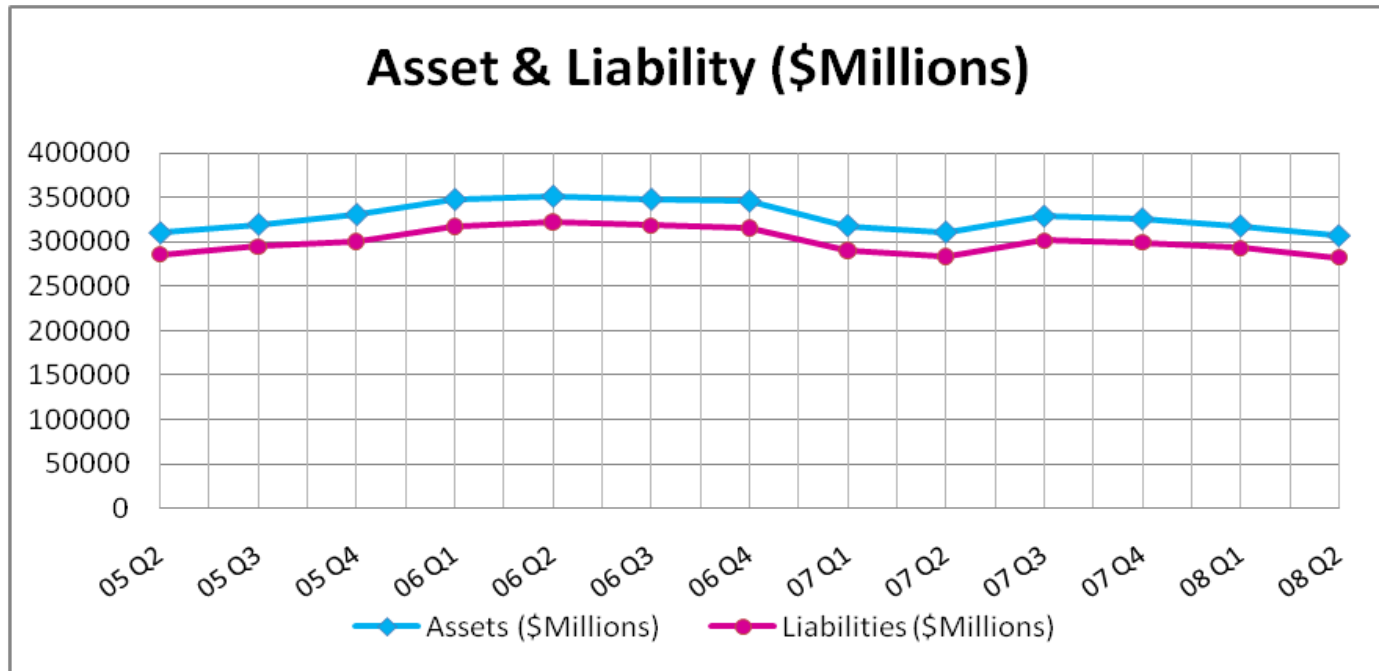
# Asset: Liability Analysis

	2007Q1	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2
Asset: Liability Ratio	109.62%	109.78%	108.99%	108.81%	108.36%	108.63%
Median A/L Ratio*	111.98%	112.03%	112.21%	112.01%	112.04%	111.72%
Ranking	Moderate	Moderate	Poor	Poor	Poor	Poor

- Washington Mutual Bank's A/L ratio was below average for all 6 quarters prior to failure.
- The bank's A/L ratio was slightly decreasing from 07 Q3 to 08 Q1.

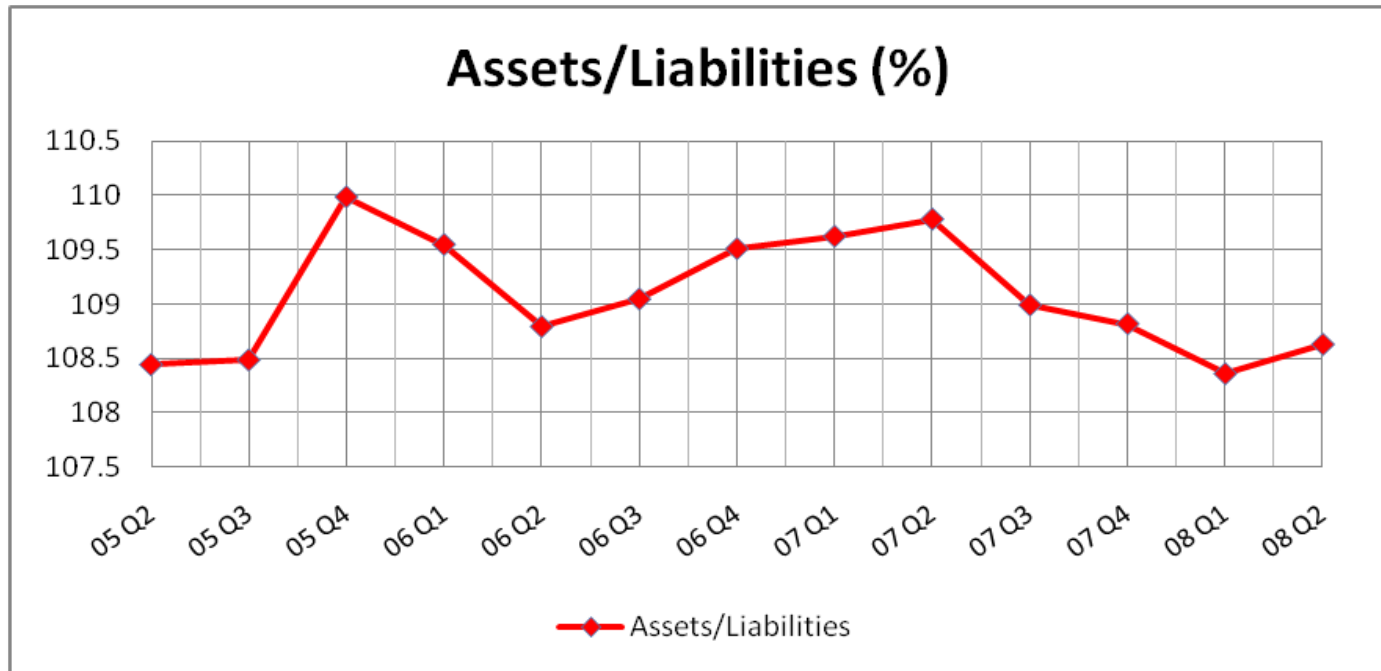
\*Average of banks of the same asset concentration hierarchy

# Asset & Liability History



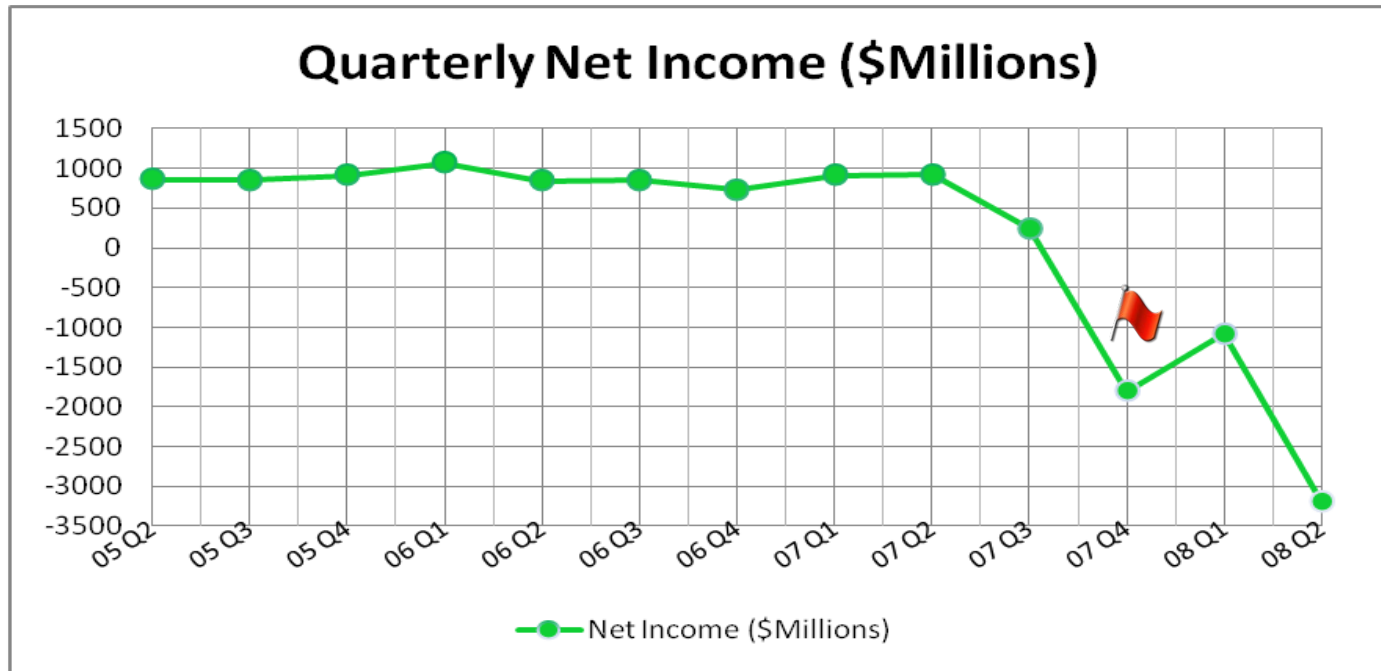
- The difference between asset and liability was consistent along all these quarters.

# Asset/Liability History




- The A/L ratio was decreasing since 07 Q2.

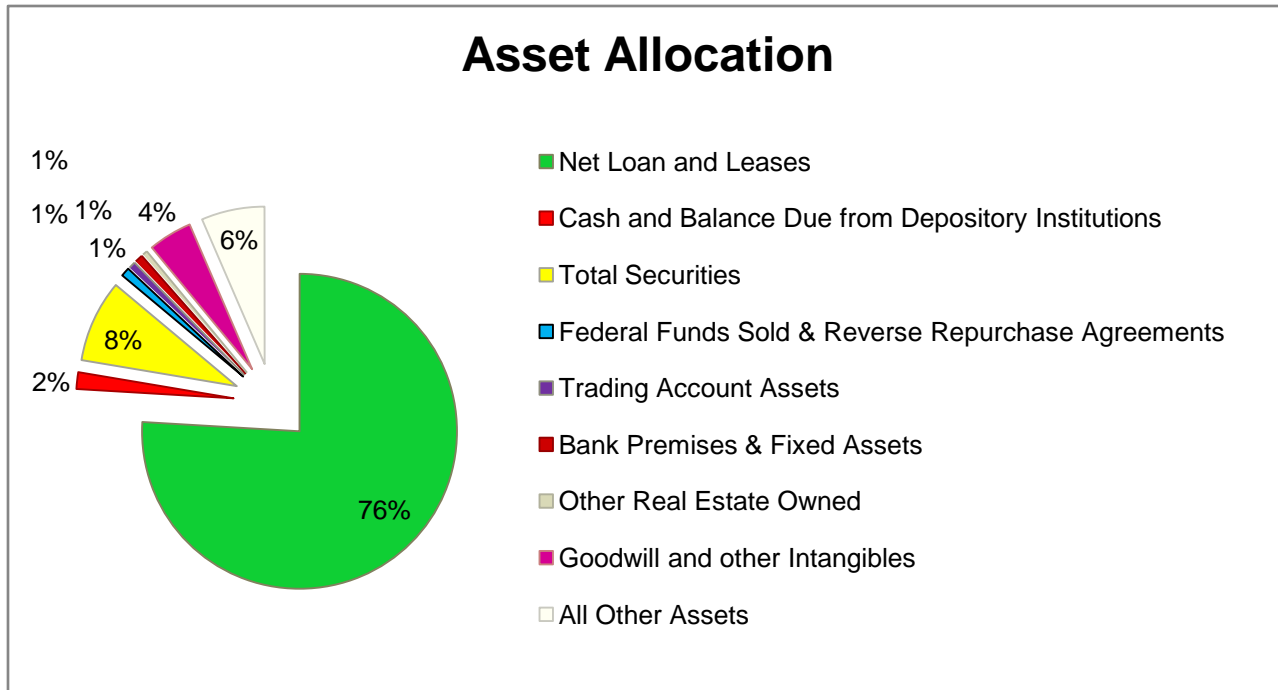
# Net Income History



- The bank recorded big losses in the last 3 quarters prior to failure.

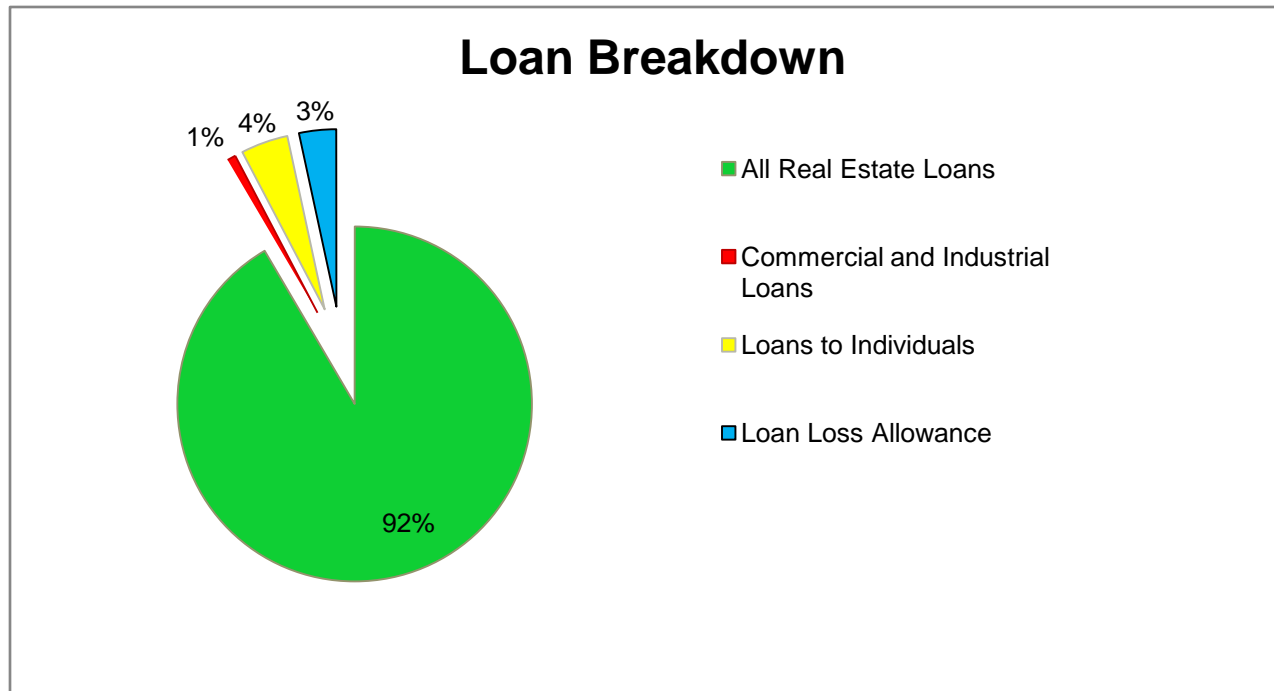
 Indicates sign of bank in financial distress

# Asset Allocation



- The average percentage of Net Loans for banks of the same Asset Concentration Hierarchy in the second quarter of 2008 was 63.20%.
- The average Net Loan percentage of all banks in the second quarter of 2008 was 66.00%.

# Loan Breakdown



- The average percentage of Real Estate Loans for banks of the same Asset Concentration Hierarchy in the second quarter of 2008 was 90.53%.
- The average percentage for all banks in the second quarter of 2008 was 70.68%.

# Events Timeline

- Nov. 7, 07** - 2007 credit losses could amount to between \$2.7 billion to \$2.9 billion, nearly doubling the forecasts made in July.
- Dec. 11, 07** - WaMu will write down the value of its home lending unit by as much as \$1.6 billion in the fourth quarter and cut 3,150 jobs.
- Jan. 15, 08** -The Seattle-based bank planned to sell \$3 billion in stock to raise cash, cut its dividend by 73%, and set aside \$1.5 billion to \$1.6 billion to cover bad loans in the 4Q.
- Mar. 4, 08** - SEC voted to disclose information for the secondary market ETF investors in Form N-1A.
- Mar. 7, 08** - The Fed will initiate a series of term repurchase transactions that are expected to cumulate to \$100 billion.
- Mar. 19, 08** - Fannie Mae and Freddie Mac is expected to provide support to the U.S. mortgage market, up to \$200 billion immediate liquidity.
- Apr. 8, 08** - WaMu obtained \$7 billion capital injection from private investors.
- Apr. 8, 08** - WaMu cuts quarterly dividend to 1 cents/share from 15 cents/share.
- May 29, 08** - U.S.-Canada mutual recognition arrangement: U.S. Securities markets and certain U.S. financial service firms could gain greater freedom to operate in Canada under SEC.
- June 10, 08** - FDIC releases a supervisory letter to all banks on interest reserves that examines the risks that this underwriting practice presents.
- June 11, 08** - SEC voted on a comprehensive series of credit rating agency reforms to bring increased transparency to credit rating process.
- June 11, 08** - The stock hit a low of \$5.75 in intraday trading.

# Events Timeline

- June 17, 08** - New HOPE NOW guidelines to deal with issues surrounding second mortgages and short sales.
- June. 26, 08** - FDIC adopts Basel II-Based Standardized Approach as an alternative risk-based capital framework available to all banks except the largest and most complex banks
- June. 26, 08** - FRS, FDIC, and OCC issued the host state loan-to-deposit ratios, which help indicate branches outside of the home state that were established or acquired for the purpose of deposit production.
- Jul. 13, 08** - Paulson Announces a three-part plan for GSEs: a temporary increase in the line of credit, a temporary authority for Treasury to purchase equity, and an advisory role is given to the Fed.
- Jul. 22, 08** - WaMu reports 2Q loss of \$3.3 billion.
- Jul. 24, 08** - WaMu lost more than 30% of its market value.
- Aug. 20, 08** - FDIC's implementation in Loan Modification Program will help to modify troubled IndyMac mortgages loans.
- Sept. 11, 08** – WaMU shares sink below \$2 on the NYSE.
- Sept. 17, 08** - SEC clarified that bank support of money market mutual funds generally are not required to present the fund on-balance sheet, but disclosure of the nature of the support provided is expected.
- Sept. 18, 08** - SEC requires that certain institutional money managers report their new short sales of certain publicly traded securities.
- Sept. 19, 08** - SEC prohibited short selling in 779 financial institutions.

# Events Timeline

- Sept. 20, 08** - Treasury Secretary Hank Paulson releases \$700 billion proposal to purchase troubled mortgage-related assets.
- Sept. 25, 08** – WaMu was sold to JP Morgan Chase & Co. for \$1.9 billion.
- Oct. 7, 08** - Emergency Economic Stabilization Act of 2008 Temporarily Increases Basic FDIC Insurance Coverage from \$100,000 to \$250,000 per Depositor.
- Oct. 14, 08** - FDIC creates new program to guarantee bank debts and fully insure non-interest bearing deposit transaction accounts.
- Oct. 14, 08** - The Treasury Department will invest up to \$250 billion in the nation's banks via the Capital Purchase Program.
- Nov. 20, 08** - FDIC announces the availability of IndyMac Loan Modification Model.
- Nov. 25, 08** - Created the Term Asset-Backed Securities Loan Facility to support the issuance of asset-backed securities collateralized by loans.
- Dec. 3, 08** - SEC approved measures to strengthen oversight of credit rating agencies.
- Dec. 16, 08** - Troubled banks have to provide certain position level and counterparty level data and QFC counterparty and portfolio identifiers to FDIC in a timely manner.
- Dec. 23, 08** - Treasury provides TARP funds to focal Banks by purchasing \$2.8 billion investment from 49 banks.
- Dec. 30, 08** - The Fed announced that it will purchase mortgage-backed securities.
- Jan. 15, 09** - The Senate voted to allow access to the remaining bailout funds of \$350 billion.
- Jan. 27, 09** - As part of the Capital Purchase Program, Treasury announced investments of \$386 million in 23 healthy banks.

# Events Timeline

- Feb. 10, 09** – Geithner rolls out the Financial Stability Plan, promises to perform “stress tests” on big banks, and commit \$100 billion to boost the TALF.
- Feb. 10, 09** - A Capital Assistance Program to help ensure banks hold sufficient capital, produce a more consistent and forward-looking assessment of risks on banks' balance and their potential capital needs.
- Feb. 10, 09** - A Public-Private Investment Fund will combine public and private capital with government financing to help free up capital to support new lending.
- Feb. 10, 09** - Treasury and Fed expanded the Term Asset-Backed Securities Lending facility up to \$1 trillion.
- Feb. 18, 09** - President Obama signs the American Recovery and Reinvestment Act of 2009, which limits bonuses of the highest earning executives.
- Mar. 4, 09** - Treasury announced loan modification guidelines under the Administration's Homeowner Affordability and Stability Plan.
- Mar. 23, 09** - Using TARP capital and capital from private investors, the Public-Private Investment Program will generate \$500 billion in purchasing power to buy legacy assets.
- May 29, 09** - FDIC tightens the deposit interest rates paid by banks that are less than well capitalized. Generally, such banks will be permitted to offer to "national rate" plus 75 basis points.
- June 9, 09** - 10 Of the largest U.S financial institutions are expected to make CPP repayments to Treasury.
- Jul. 2, 09** - FDIC proposed guidelines require private equity firms to hold bank purchases for 3yrs and maintain capital levels.

# Report Summary – *Surprise?*

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Based on the methods with which we analyzed Washington Mutual, its failure was ***not a surprise***.

Here are the indications that Washington Mutual should fail:

- 1) **Washington Mutual had a poor normalized income the three quarters before it failed.**
- 2) **Washington Mutual's delinquent asset percentage consistently increased each quarter for the past six quarters.**
- 3) **Washington Mutual's bankability composite score was 35.99 the quarter before it failed and 38.96 the quarter before. Although these scores are poor, its BCS's are relatively high compared to other banks that failed.**

# References

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