



SR003_7: Failed Bank Report

PFF Bank & Trust

399 North Garey Avenue
Pomona, CA 91767

(1/1/1892 – 11/21/2008)

Report Objective

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

FDIC Certificate #	28344
Bank Charter Class	Savings Association
Asset Concentration	Commercial Lending Specialization
Product Specialty	Financial Planning Services including management of stocks, bonds, real estate, and closely held business interests
Number of Branches	38 (as of September 30, 2008)
Number of Employees	700 (as of September 30, 2008)

Executives

CEO/President	Kevin McCarthy
CFO	Gregory C. Talbott
EVP	William G. Standlea

What took place?

The banking operations of PFF Bank and Trust, Pomona, CA was sold to U.S. Bank, National Association, Minneapolis, MN in a transaction facilitated by the Federal Depository Insurance Corporation (FDIC) and the Office of Thrift Supervision on November 21st, 2008. The estimated cost to the FDIC Deposit Insurance Fund is \$700,000,000, compared to the average cost of \$389,206,944. U.S. Bancorp acquired all deposits and some assets.

Bank Financial Snapshot

Financial Data Overlay (thousands)			
	2007 Q3	2008 Q3	Percentage Change
Assets	\$ 4,352,240	\$ 3,715,433	↓ 14.6%
Liabilities	\$ 3,971,816	\$ 3,545,544	↓ 10.7%
Net Income	\$ 8,751	-\$ 170,767	↓ 2,051%

- The average net income change for all FDIC banks was -66.92% in the same period.
- The average net income change for all the commercial lending specialization banks was -73.88% in the same period.
- Compared with the whole industry and other commercial lending specialization banks, PFF Bank & Trust's decline from Net Income is abnormally large (-2052%) during 2008.

Key Performance Indicators


KPI Summary for 2008 Q3	
Normalized Income Rating	Poor
Delinquent Asset Rating	Good
Asset: Liability Rating	Very Poor
Real Estate Asset Rating*	Very Poor
Bankability Composite Score	16.99** (Very 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

	2007Q2	2007Q3	2007Q4	2008Q1 	2008Q2	2008Q3
Normalized Income	0.13%	-0.20%	-0.26%	-2.37%	-0.28%	-1.67%
SD's from Average*	-0.189	-0.982	-0.475	-4.95	-0.477	-1.97
Ranking	Moderate	Moderate	Moderate	Very Poor	Moderate	Poor

- PFF Bank and Trust had a normalized income of -1.67% in the third quarter of 2008, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average normalized income of -0.24%. The standard deviation of the normalized incomes was 1.02%, which means that PFF Bank and Trust was almost 2 SD's below the average.

*Average of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Delinquent Asset Analysis

	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2	2008Q3
Delinquent Asset	0.4406%	1.3532%	0.9129%	1.0096%	0.5788%	1.0007%
SD's from Average*	-0.47	0.07	-0.28	-0.27	-0.44	-0.26
Ranking	Good	Moderate	Good	Good	Good	Good

- PFF Bank & Trust had a delinquent assets out of total assets ratio 1.0% in the third quarter of 2008, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average delinquent asset of 1.4993%. The standard deviation of the delinquent assets was 1.91%, which means that PFF Bank & Trust was about 0.26 SD's below the average.
- Since the second quarter of 2007, PFF Bank & Trust's delinquent assets ratio has been better than the average; from the perspective of delinquent assets ratio, there was no sign of PFF Bank & Trust's failing during 2008 Q4.

*Average of banks of the same asset concentration hierarchy

Real Estate Loan Asset Analysis

	2007Q2 	2007Q3	2007Q4	2008Q1	2008Q2	2008Q3
Real Estate Loan Asset Ratio	84.50%	84.29%	85.07%	85.95%	79.92%	82.46%
SD's from Average*	1.96	1.90	1.93	1.99	1.56	1.73
Ranking	Very Poor	Very Poor	Very Poor	Very Poor	Very Poor	Very Poor

- PPF Bank and Trust had a 82.46% of R/A ratio in 08 Q3, the quarter before it failed.
- In 08 Q3, banks of the same asset concentration hierarchy (commercial lending specialization) had an average R/A ratio of 56.74%. The standard deviation of the R/A ratio was 14.82%, which means that PPF Bank and Trust was 1.73 SD's above the average.

*Average of banks of the same asset concentration hierarchy



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Asset: Liability Analysis

	2007Q2	2007Q3	2007Q4	2008Q1 	2008Q2	2008Q3
Asset: Liability Ratio	109.80%	109.58%	109.46%	107.19%	105.96%	104.79%
Median A/L Ratio*	110.74%	110.97%	110.95%	110.93%	110.69%	110.65%
Ranking	Moderate	Moderate	Poor	Poor	Very Poor	Very Poor

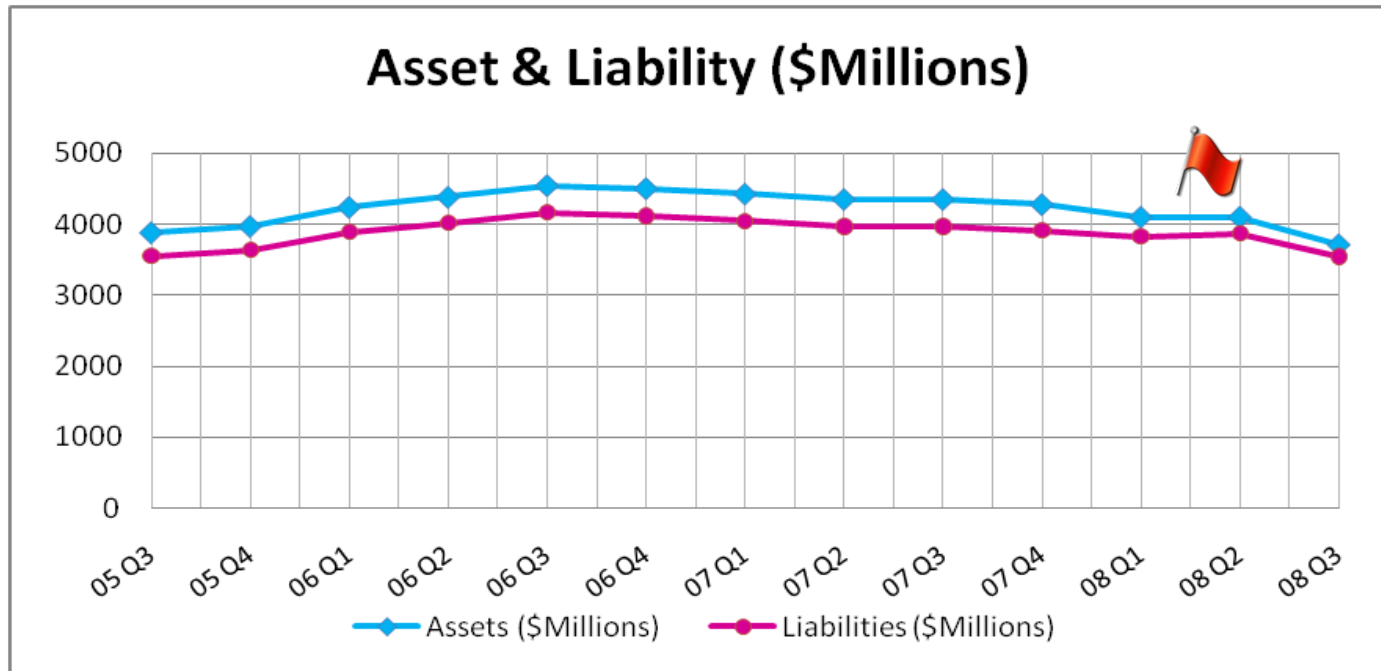
- PPF Bank and Trust's A/L ratio was below average for all 6 quarters prior to failure.
- The bank experienced decreasing A/L ratio in all 6 quarters.
- The bank fell into the worst ranking in 08 Q2.
- Of the banks failed in 08 Q4, 83.33% of them had an A/L ratio under 107%.

*Median of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Asset & Liability History

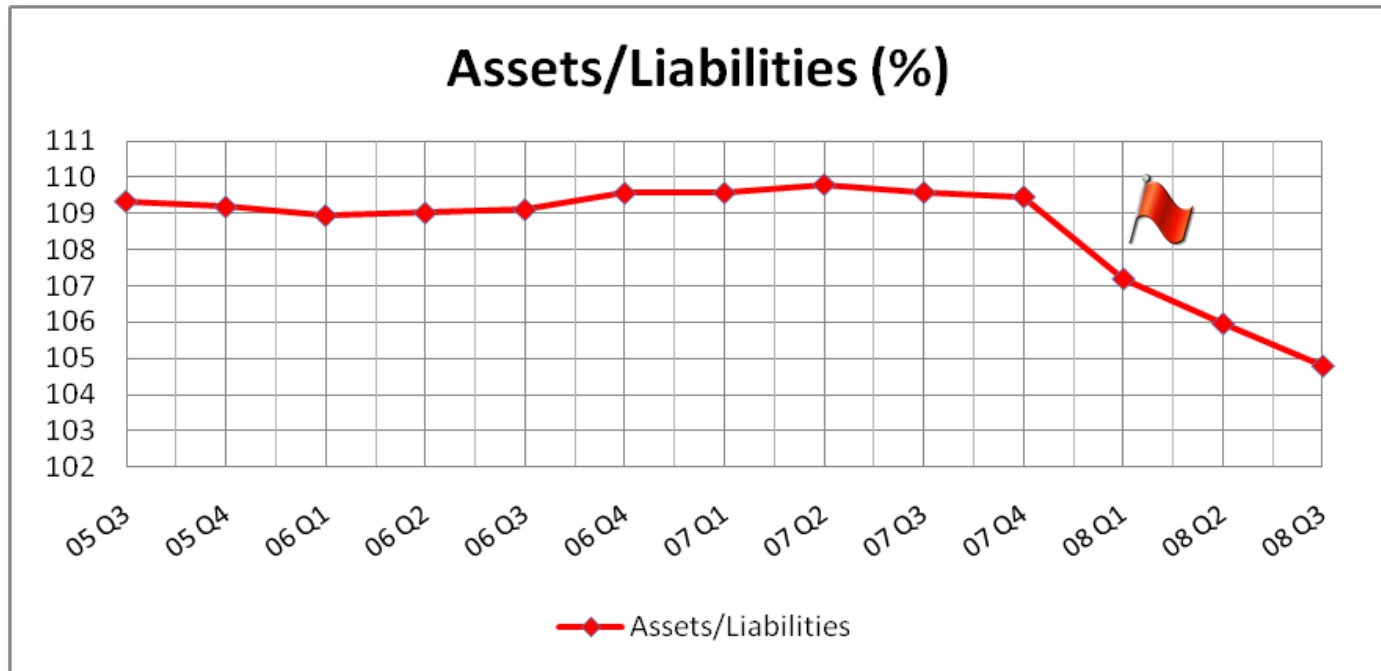


- The difference between asset and liability was getting closer in 08 Q1.



Indicates sign of bank in financial distress

Asset/Liability History

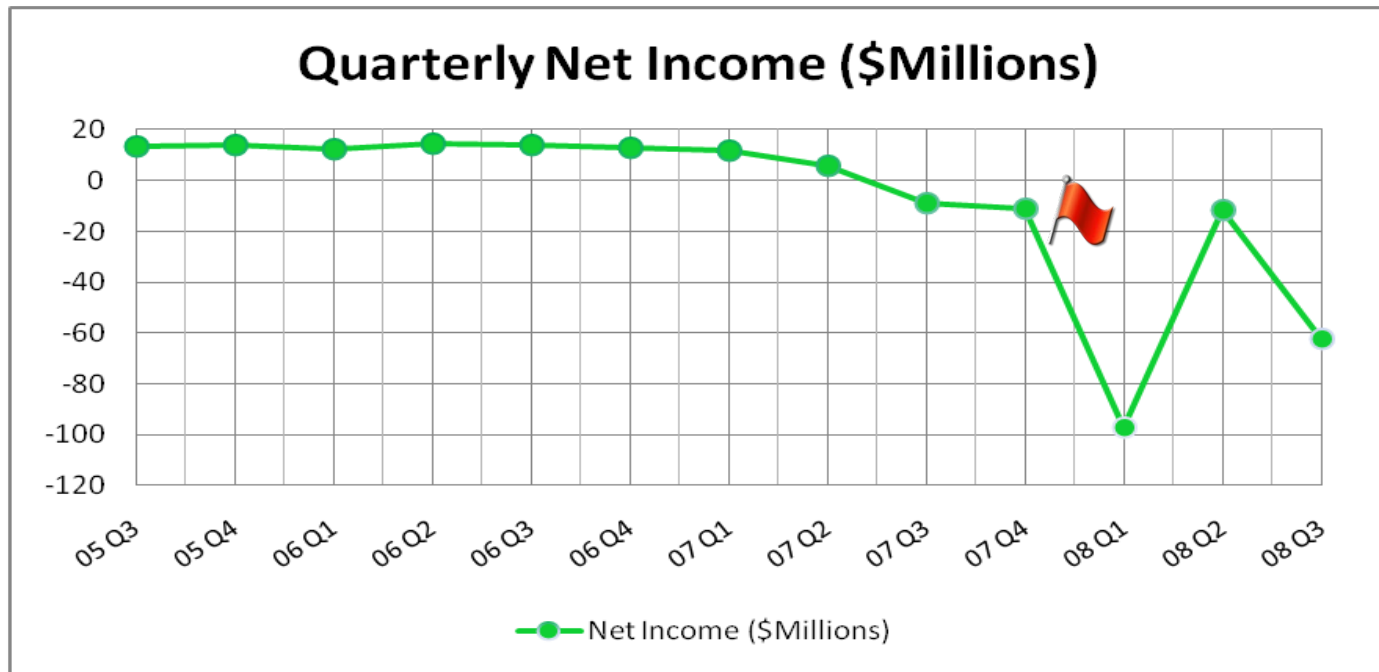


- The A/L ratio was decreasing since 07 Q2.



Indicates sign of bank in financial distress

Net Income History

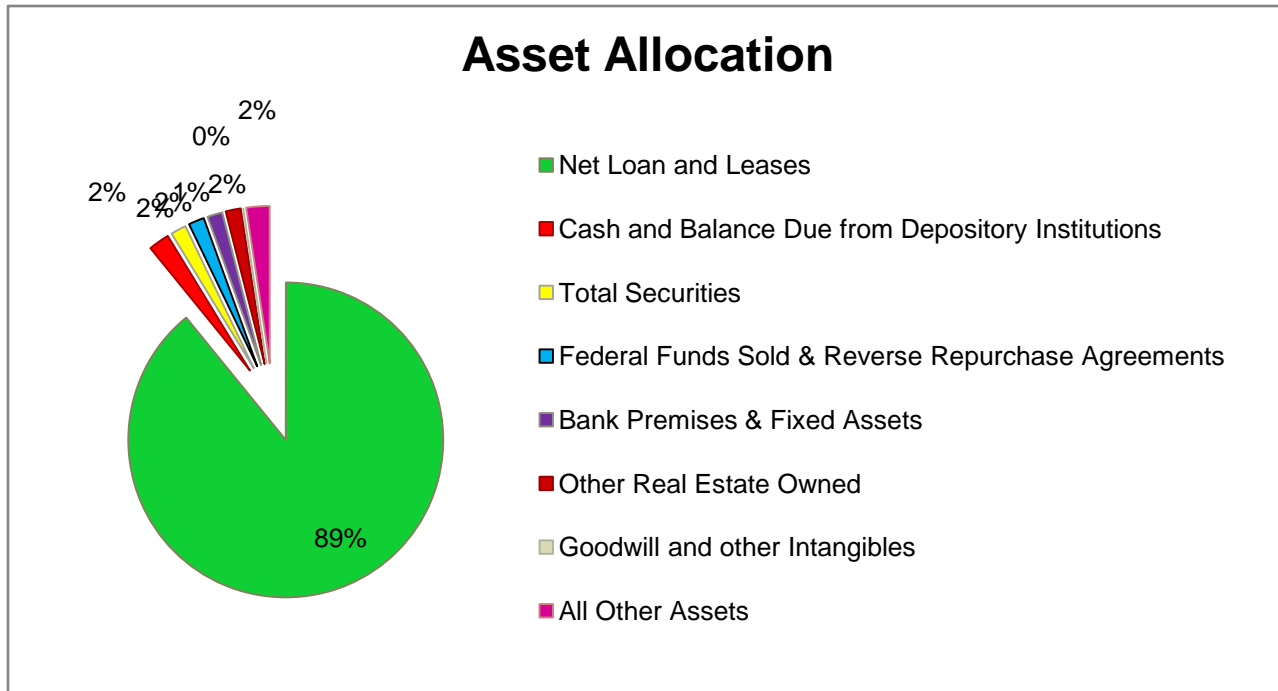


- The bank recorded a big loss in 08 Q1 and 08 Q3.
- The bank reported losses since 07 Q3.



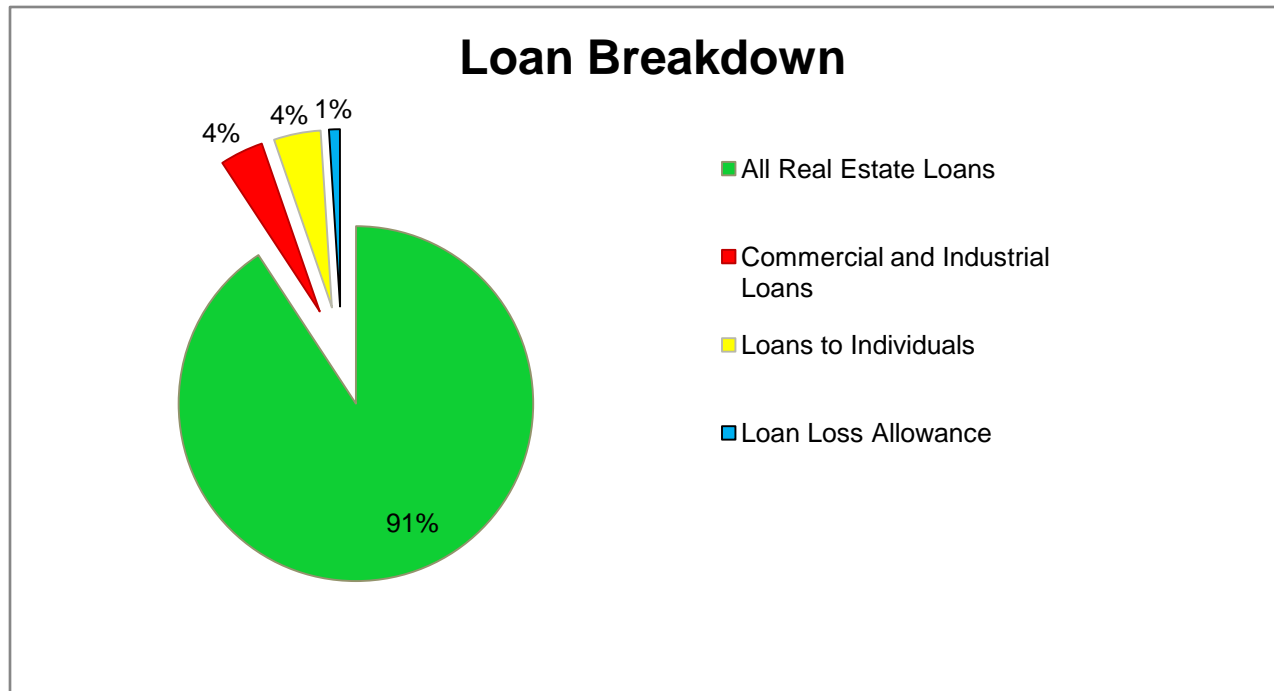
Indicates sign of bank in financial distress

Asset Allocation



- The average percentage of Net Loans for banks of the same Asset Concentration Hierarchy in third quarter of 2008 was 72.85%.
- The average Net Loan percentage of all banks in the third quarter of 2008 was 66.63%.

Loan Breakdown



- The average percentage of Real Estate Loans for banks of the same Asset Concentration Hierarchy in the third quarter of 2008 was 76.31%.
- The average percentage for all banks in the third quarter of 2008 was 70.99%.

Events Timeline

May 30, 07 - PFF Bank opens 3 branch locations in Victor Valley.

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.

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 16, 08 - California National Bank parent agrees to acquire PFF Bancorp.

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.

Events Timeline

- 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.
- Aug. 20, 08** - FDIC's implementation in Loan Modification Program will help to modify troubled IndyMac mortgages loans.
- Aug. 20, 08** - Former employees sue against PFF Bank & Trust over losses in stock plan.
- 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.
- Sept. 20, 08** - Treasury Secretary Hank Paulson releases \$700 billion proposal to purchase troubled mortgage-related assets.
- 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.

Events Timeline

- Nov. 20, 08** - FDIC announces the availability of IndyMac Loan Modification Model.
- Nov. 21, 08** - U.S. Bank will assume the first \$1.6 billion of losses on the asset pools .
- 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.
- 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.

Events Timeline

- 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.

Report Summary – *Surprise?*

Based on the methods with which we analyzed, PFF Bank & Trust, its failure was **not a surprise**.

Although PFF Bank & Trust's delinquent asset analysis was relatively typical of banks with the same asset concentration hierarchy, there are other indications that PFF Bank & Trust should fail:

- 1) **Since 2007 Q3, PFF Bank & Trust's normalized income has become negative and worsen each quarter.**
- 2) **PFF Bank & Trust's real estate loan asset ratio has been more than 80% almost every quarter since 2007 Q2.**
- 3) **PFF Bank & Trust's asset: liability ratio rapidly decreased since 2008 Q1.**
- 4) **Its Bankability Composite Score was 16.99 before its failure, which was considered to be very poor.**

The combination of these four measures being poor shows that the bank could fail anytime.

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