

## Update: United States Economy: Third Quarter 2011

*The economy continued to expand in the third quarter, while inflation remained contained. High rates of joblessness influenced fiscal and monetary policy, while debt issues were major concerns moving interest rates.*



### National Economy

Fifteen quarters after the start of the 2007 recession, real gross domestic product (GDP) finally exceeded its previous peak. For the ten business cycles from the end of World War II until the recession of 2007, the steepest downturn in real growth had been the 1973-75 business cycle, when output declined 3.2%. The decline in total output for the 2007 recession equaled 5.1%.

For the ten recessions prior to 2007, the longest quarterly span between the prior peak to a new peak in GDP equaled eight quarters, which was during the 1973-75 cycle. For the 2007 recession, the peak-to-peak period extended for 15 quarters. Typically, economic growth would snap back once a recession ended. The period from the end of the recession to

**Postwar Business Cycles  
Cyclical Performance of GDP  
(Based upon 2005 \$)**

Business Cycle	Growth Rates		Qtrs to Next Peak	Growth Performance During Recession		
	Peak to Trough	Trough to Next Peak		Qtrs Down	Qtrs Regain Pk	Qtrs Trough to New Peak
	1948-49	-1.6%	28.7%	13	3	5
1953-54	-2.6%	13.4%	12	3	6	1
1957-58	-3.1%	11.7%	7	2	5	2
1960-61	-0.5%	51.2%	34	2	5	1
1969-70	-0.2%	0.2%	11	3	6	1
1973-75	-3.2%	23.2%	19	5	8	3
1980-80	-2.2%	4.4%	3	2	4	1
1981-82	-2.6%	37.3%	30	3	7	2
1990-91	-1.4%	38.9%	39	3	6	3
2001-01	0.7%	17.2%	23	0	NA	NA
2007-09	-5.1%	NA	NA	5	15	9
Average Recession	-2.0%			2.8	6.7	2.4
Avg w/o 2007	-1.7%			2.6	5.8	1.7
Mildest Recession	0.7%			0	0	0
Worst Recession	-5.1%			5	15	9
Worst before 2007	-3.2%			5	8	3

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December 2011  
Volume 3, Issue 3

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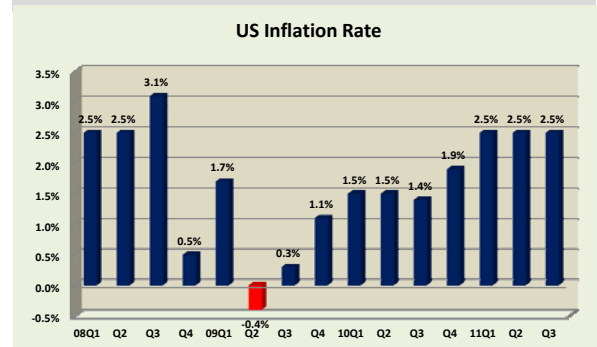
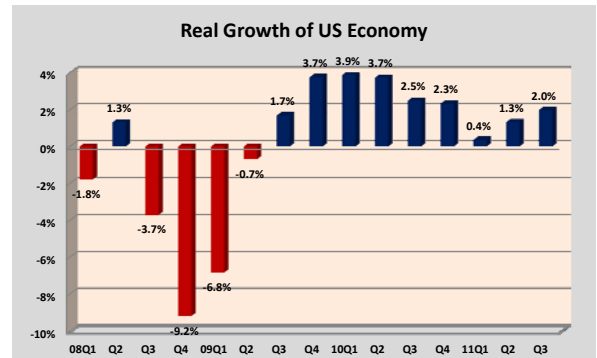
the new peak in output averaged about two quarters. The 2007 recession required nine quarters from the end of the recession for the economy to regain its prior peak. From the third quarter of 2009 through the third quarter of 2011, real GDP grew by a total of 8.1%, compared with the average two-year growth of 19.1% for the prior postwar recoveries.

Economic growth in the third quarter equaled 2.0%, compared with 0.8% growth in the first half of this year. The tepid growth during the first half partially was attributed to transitory factors of sharply higher oil prices and global supply disruptions caused by the earthquake in Japan. Disruptions in the supply chain, notably for automotive parts, eased going into the fourth quarter. Commodity prices declined from the high levels earlier this year. The rate of inflation, as measured by the GDP price deflator, equaled 2.5%, unchanged from the prior two quarters.

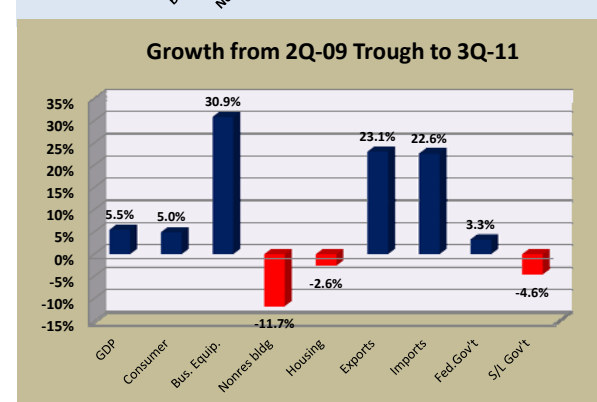
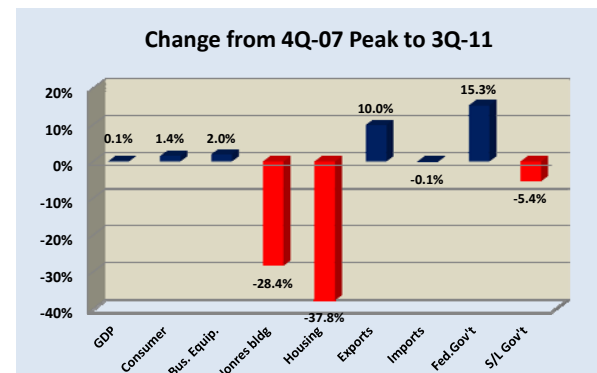
Although growth prospects improved and core inflation remained moderate, financial markets reacted adversely to the government debt issues impacting the U.S. and Euro-zone. Significant market volatility contributed to uncertainty regarding future economic conditions, eroded the confidence of U.S. consumers and businesses, and aggravated the downward slide in stock prices in August and September.

Despite historically low readings in consumer confidence, third quarter data reflected renewed consumer buying, especially for autos and other durable goods. Surveys revealed low levels of business sentiment, but those readings did not prevent businesses from stepping up their spending on equipment and software in the third quarter. Uncertainty over economic conditions was apparent in the reluctance by businesses to add significantly to payrolls and inventories.

The housing industry typically takes the lead in recoveries, as cyclically low interest rates and increased job creation fostered a pickup in home sales. For the current cycle, interest rates plummeted to historic lows. Missing in the recovery equation for homebuilding were the lack of job creation and the post-war high in the volume of foreclosed homes or homes in the process of foreclosure. Unprecedented and persistent declines in home prices prevented a sustained rebound in home buying, thus keeping the inventory of unsold homes at high levels. New home construction, as measured by the current pace of housing starts, was 40% below its 52-year average rate and less than one-quarter the record rate for starts. Prospects for homebuilding in the year ahead suggested continuing weakness, in part as sluggish growth in jobs will constrain household incomes and as mortgage credit conditions are likely to remain tight and impacted by the limited secondary market for mortgages.



Consumer, business & federal government spending and the trade sector propelled the recovery. Construction & state/local government spending were cyclical laggards.



Funding at all levels of government constricted public sector hiring and spending. Declining government payrolls and cuts in spending programs caused the public sector to be a damper on third quarter GDP growth. The protracted debate over the debt ceiling and the inability to agree upon a strategy to reduce the federal budget deficit contributed to the unprecedented reduction by S&P on its rating of U.S. treasury debt.

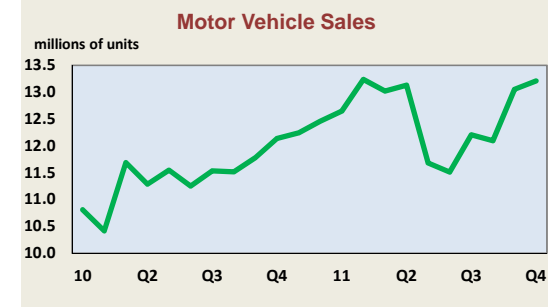
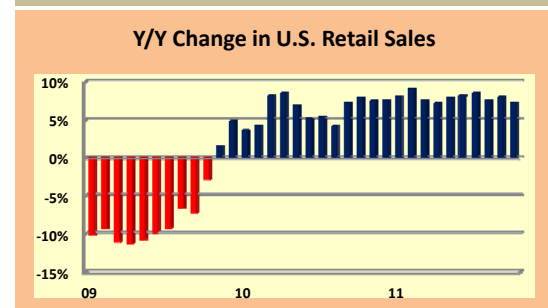
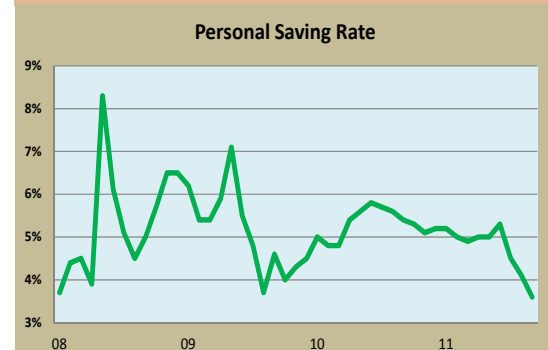
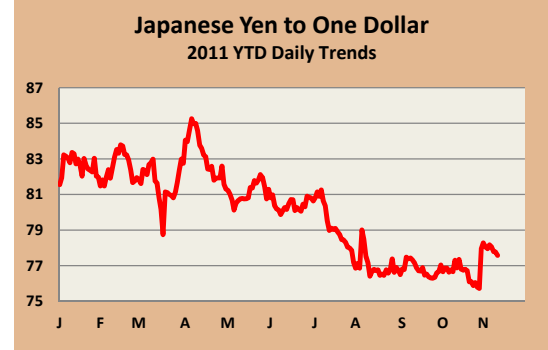
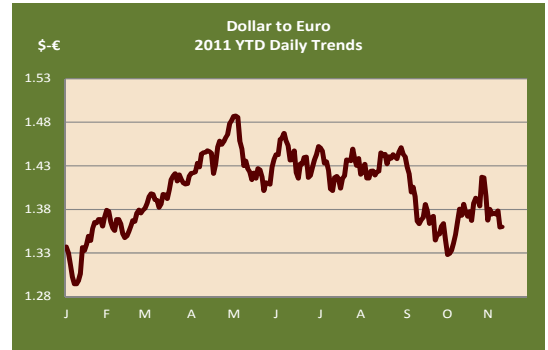
Since the middle of 2009, the national economy benefitted greatly from a pickup in export shipments. U.S. exports responded to favorable foreign exchange movements, wherein the dollar generally declined against the currencies of its major trading partners, thus making U.S. products more affordable in many markets worldwide. A cloud over the outlook for U.S. trade was the persistent financial crisis in Europe and the observation that even without an escalation in the Euro-zone debt crisis, prospects increasingly pointed toward Europe entering into a recession. Such a recession would have adverse consequences for global growth and the demand for goods exported from the United States.

Concern over the Euro-zone debt crisis contributed to the decline in the Euro relative to the dollar during the third quarter. Investors worldwide sought alternative investments to provide principal preservation and thus pushed up the Japanese yen. The dollar declined to a record low versus the yen in October 2011, before intervention by the Japanese central bank stanchied the yen's appreciation.

## Consumer Spending

Typically, the U.S. consumer was a robust engine for an economic recovery. Consumer spending in the current business cycle grew 2.2% compared with gains ranging between 4% and 6% during the previous recoveries. Recently, consumer buying was held down by weak gains in income, notably in real disposable personal income (DPI). During the third quarter, real DPI declined 1.7% and remained even with the fourth quarter 2010 level. Despite the income decline, retail sales in the third quarter climbed at an annualized rate of 7.5%, up from the 1.4% annualized growth in the second quarter. Consumers apparently dipped into savings to support spending in the third quarter. The personal saving rate declined to 3.6% in September, the lowest rate since early 2008 and a significant decline from the May 2009 high of 7.1%.

A rebound in motor vehicle sales propelled the brisk upturn in retail sales during September. Total retail sales climbed 1.1% over August and were up 7.9% YoY. Higher prices contributed to the 19% YoY rise in gasoline sales in September. Advance reports indicated that retail sales continued to expand in October, rising 0.5% over September and 7.2% YoY.



Sales of motor vehicles averaged an annual rate of 13.1 million units in September and October, up from the low for the year of 11.5 million units in June. Prior to the Japanese earthquake and the ensuing supply disruptions, sales of motor vehicles were on an improving trend in the U.S., as indicated by the chart on the preceding page. Supply disruptions caused sales to decline 13% from February's high to the low in June. The September-October readings finally brought sales back to the early 2011 levels.

## Business Sector

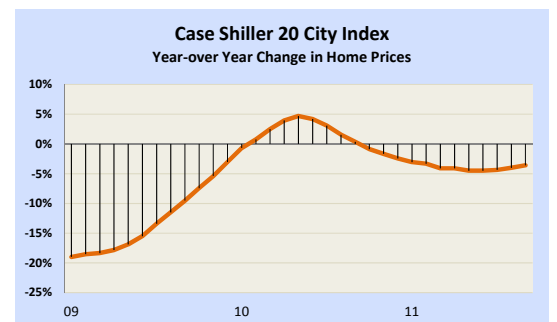
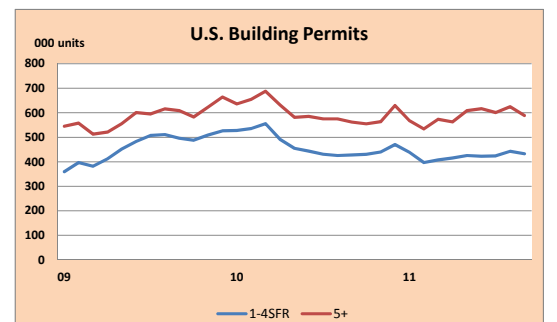
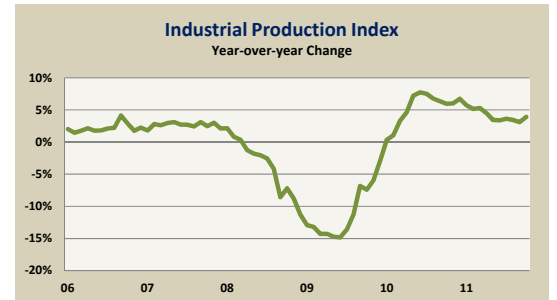
Business investment spending on equipment and software provided significant support to the economic recovery. Despite this growth, it was not until the third quarter of 2011 that such spending exceeded its previous peak. Business equipment spending grew 16% in the third quarter, a robustness that belied the surveys indicating that manufacturing was slowing. The Institute of Supply Management (ISM) survey of manufacturing activity declined sharply in August and through October remained barely above 50, the demarcation between rising and declining activity. Corporate earnings, however, rebounded sharply, up 134% from year-end 2008 through the third quarter.

Industrial production slowed, with the average YoY increases in the third quarter equaling 3.3%, down from the 6.9% YoY gain during the third quarter of 2010. Part of the slowdown in industrial production was attributable to the reduced pace of inventory accumulation. Based upon monthly data on manufacturing and trade inventories, business inventories in the three months ending September 2011 advanced at an annualized rate of 3.3% compared with the 9.2% growth in the June quarter. Inventories declined on a monthly basis in September and the YoY change in inventories equaled 9.0%, which was the lowest YoY reading since December 2010.

## Construction

Both commercial and residential construction remained sluggish in the third quarter of 2011. The volume of investment in commercial and residential structures continued well below the pre-recession peak in spending. Commercial construction typically is a lagging economic indicator, whereas homebuilding typically leads the economy out of recession.

Residential building permits reached an annualized rate of 589,000 units in September, a level that was up 15% from the March 2009 low in permits, yet down 14% from the near-term high in permits as of March 2010. New building activity remained within a narrow band throughout the past three years, held down by persistent declines in home prices and high inventories of distressed properties. From the beginning of 2009 through September 2011, residential building permits averaged 591,000 units, which essentially matched the September reading.



## Unemployment and Other Indicators

Through October 2011 the rate of unemployment remained at or above 9.0% for 28 out of the past 30 months. Nonfarm payrolls grew 1.2% during the past year compared with annual growth rates of 2% to 5% for the previous recessions. As of October, nonfarm payrolls were still 4.7% below the pre-recession peak in jobs. At the YTD pace of job creation, the economy would finally generate sufficient jobs to surpass the prior peak by early 2015, more than six years from the start of the recession. The average duration of unemployment climbed to 39 weeks in October, while many discouraged job seekers exited the labor force, thus pulling the labor force participation rate down to its lowest level since 1983.

The rate of inflation, as measured by the consumer price index, rose 3.9% YoY in September before easing to a 3.6% YoY advance in October. Higher prices for energy and food contributed significantly to the step-up in prices. During 2010 the consumer price index rose 1.6%. The October 2011 reading showed a 3.0% increase over the year-end 2010 index. Consumer prices, less food and fuel, rose by 2.1% YoY in October 2011, essentially in line with the Federal Reserve's tolerated rate for core inflation.

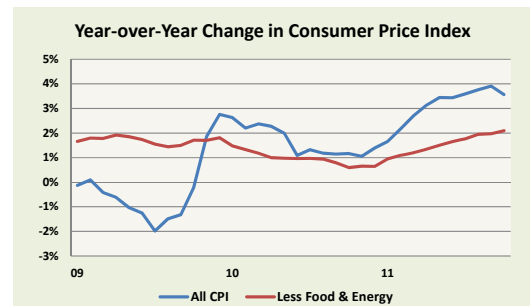
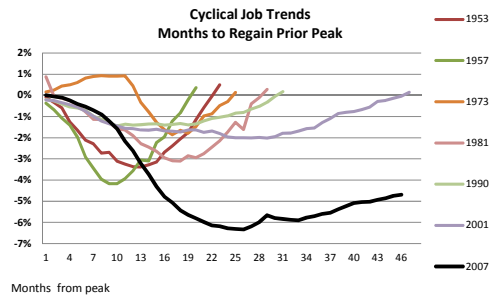
Inflation on the wholesale level mirrored the trends in consumer prices. The producers price index for all finished goods climbed 7.0% YoY in September before easing to a 6.1% YoY advance in October. The producers price index, excluding food and fuel, was up 2.5% YoY in September and 2.8% in October. Recent slowing in the pace of global economic activity will likely place downward pressures on producers prices.

## Policy Responses

Recent economy activity and generally contained rates of inflation prompted monetary and fiscal policies to focus on stimulating the economy and job creation. Fiscal policy faced conflicting challenges of bringing down persistently high rates of unemployment and trimming large budget deficits. The budget super-committee failed to reach any agreement on ways to trim a minimum of \$1.2 trillion in the longer-term federal budget deficit. Hence, automatic cuts in spending programs were legislated to be initiated beginning in fiscal 2013. In addition to the cuts imposed under the sequestration trigger of the September 2011 Budget Control Act the bill imposed \$900 billion in ten-year spending cuts, which will begin in fiscal 2012. Still unresolved at this time was the fate of extended unemployment benefits and Social Security payroll tax reductions, which were scheduled to expire at year-end 2011. Given the current stalemate in Washington and the rancor during an election year, the reining in of federal spending and the prospect potential increases in payroll taxes will cut into economic growth in the upcoming year and potentially contribute to a slowdown in consumer spending.

Slow growth and stubbornly high rates of unemployment prompted the Federal Open Market Committee (FOMC) to assert that economic conditions were likely to mandate exceptionally low rates of interest through the middle of 2013. The FOMC will continue to assess the economic outlook in light of incoming information and is prepared to employ its tools to promote a stronger economic recovery in the context of price stability. The FOMC announced its intention to reinvest principal repayments of its mortgage-backed securities (MBS) portfolio back into MBS and to lengthen the maturity of its treasury reinvestments from three years to seven-plus years.

In light of recent economic conditions, the Federal Reserve Governors and Reserve Bank Presidents lowered their expectations regarding growth through 2013 compared with their June forecast and raised their forecasts for the rate of unemployment through 2013. The November forecasts showed a higher expected rate of inflation in 2011, while keeping the forecast for inflation unchanged for 2012 and 2013.



## Economic Projections Federal Reserve Governors and Reserve Bank Presidents November 2011

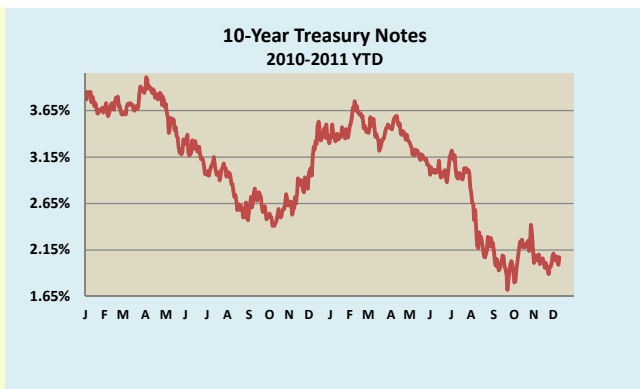
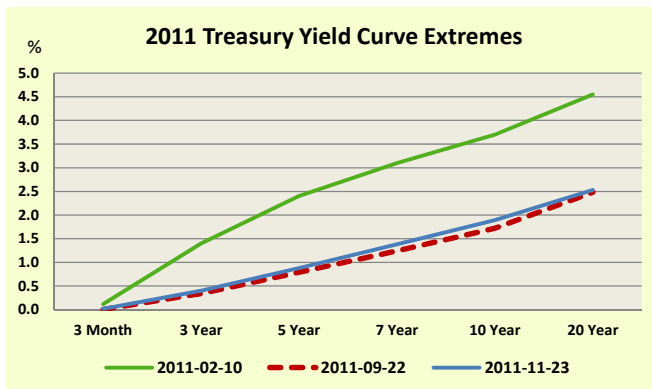
Variable	CENTRAL TENDENCY				
	2011	2012	2013	2014	Longer run
Change in real GDP	1.6-1.7%	2.5-2.9%	3.0-3.5%	3.0-3.9%	2.4-2.7%
June projection	2.7-2.9%	3.3-3.7%	3.5-4.2%		2.5-2.8%
Unemployment rate	9.0-9.1%	8.5-8.7%	7.8-8.2%	6.8-7.7%	5.2-6.0%
June projection	8.6-8.9%	7.8-8.2%	7.0-7.5%		5.2-5.6%
PCE Inflation	2.7-2.9%	1.4-2.0%	1.5-2.0%	1.5-2.0%	1.7-2.0%
June projection	2.3-2.5%	1.5-2.0%	1.5-2.0%		1.7-2.0%
Core PCE inflation	1.8-1.9%	1.5-2.0%	1.4-1.9%	1.5-2.0%	
June projection	1.5-1.8%	1.4-2.0%	1.4-2.0%		

**NOTE:** Projections of the change in real gross domestic product (GDP) and in inflation are from the fourth quarter of the previous year to the fourth quarter of the year indicated. PCE inflation and core PCE inflation are the percentage rates of change in, respectively, the price index for personal consumption expenditures (PCE) and the price index for PCE excluding food and energy. Projections for the unemployment rate are for the average civilian unemployment rate in the fourth quarter of the year indicated. Longer-run projections represent each participant's assessment of the rate to which each variable would be expected to converge under appropriate monetary policy and in the absence of further shocks to the economy. The June projections were made in conjunction with the meeting of the FOMC on June 21-22, 2011.

### Interest Rates

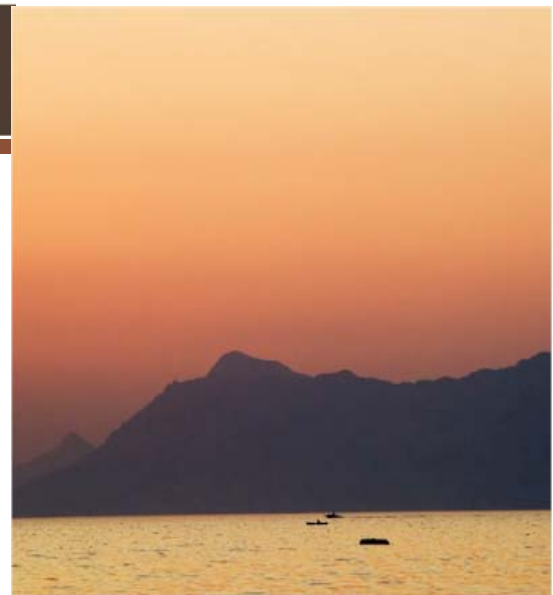
Slack economic growth, moderate core inflation and accommodative monetary policy contributed to a reduction in interest rates in the third quarter. The treasury yield curve, a measure of rates with maturities between three months and twenty years, flattened to a low for the year on September 22<sup>nd</sup> and remained near that slope in late November. The rate on ten-year treasuries increased 70 basis points from its record low in late September before trending lower by approximately 40 basis points in early November.

With equity market prices in the third quarter generally lower in volatile trading and with the turmoil surrounding the European debt crisis, investors apparently preferred safety and capital preservation over return, thus bidding up prices on treasury securities. Risk spreads on corporate bonds widened in the second half of 2011. The spread between the rates on AAA and BAA corporate bonds expanded from 75 basis points in early June to 130 basis points at the end of November. Due to the weak housing market, rates on 30-year conventional mortgages fell to a record low in early October and ended November under 4.0%.



## Update: California Economy: Third Quarter 2011

Over the past decade, California GDP slipped in ranking relative to other economies worldwide. The state continued to struggle with high rates of unemployment and a significant fiscal budgetary challenges.



### Relative Rankings

In 2000, California ranked fifth worldwide based upon gross domestic product. Only the U.S., Japan, Germany and the United Kingdom reported higher GDP than the state. In the subsequent decade, California's worldwide ranking fell to ninth position. The state's ten-year growth rate of 40% was the second lowest among the major global economies. Only Japan with its ten-year growth of 18% experienced slower growth than California. The four countries that exceeded California's GDP in 2000 remained ahead of the state in 2010. China, France, Brazil and Italy climbed over California to push the state to ninth place.

Relative Rankings of GDP

Country	GDP (\$ MLN)		Rank		GDP Chg 2000-10
	2000	2010	2000	2010	
United States	9,883	14,582	1	1	48%
China	1,080	5,879	7	2	444%
Japan	4,677	5,498	2	3	18%
Germany	1,870	3,310	3	4	77%
France	1,286	2,560	6	5	99%
United Kingdom	1,413	2,246	4	6	59%
Brazil	588	2,088	10	7	255%
Italy	1,069	2,051	8	8	92%
<b>CALIFORNIA</b>	<b>1,358</b>	<b>1,901</b>	<b>5</b>	<b>9</b>	<b>40%</b>
India	479	1,729	13	10	261%
Canada	690	1,574	9	11	128%
Russia	251	1,480	18	12	490%
Spain	555	1,407	12	13	154%
Mexico	575	1,040	11	14	81%
Korea	457	1,014	14	15	122%

Since 2007, the California economy underperformed the national economy based upon annual growth in inflation-adjusted GDP. Going into the recession, economic growth in 2007 was slower in California than the 1.9% growth nationwide. The declines in output during 2008 and 2009

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 State's GDP slipped to 9<sup>th</sup> place worldwide compared to its 5<sup>th</sup> place ranking in 2000  
 State's per capita income declined sharply in recent years, more than the national trends

Commercial Real Estate ..... Page 8  
 Improvements in commercial real estate were regionalized and based on selected industries  
 Silicon Valley and San Francisco properties were faring well

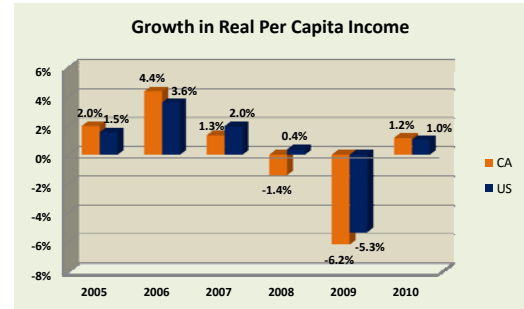
Housing..... Page 8  
 Housing yet to recover, due to high volumes of bank owned properties  
 Housing affordability greatly improved

Employment ..... Page 9  
 State jobless remained well above the national average

State Budget ..... Page 10  
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 Revenues in FY 2012 were running below projections

were generally comparable on average for both the state and the nation. During the recovery year of 2010, the state's growth of 1.8% significantly lagged the 3.0% growth rate for the U.S.

A major reason for the disparity in growth rates between the state and nation was evidenced in the trends for real per capita income. Californians suffered a downturn in income that was more severe than for the U.S. California real per capita income peaked in 2007 and through 2010 fell 6.4%. U.S. real per capita income peaked in 2008 and declined 4.4% through 2010. In 2010, California per capita income grew slightly faster than the 1.0% gain for the U.S.

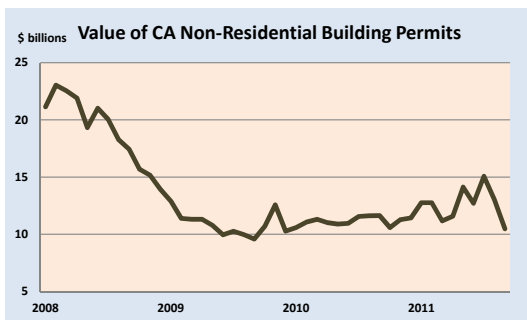


## Commercial Real Estate

Fundamentals were beginning to improve for commercial real estate in the major metropolitan markets of California, based upon studies by commercial brokerage firms, CBRE and Grubb-Ellis. The market for industrial space in Greater Los Angeles stabilized following the decline during the recession. Third quarter vacancy rates for Los Angeles industrial properties were unchanged from the prior quarter, while lease rates rose last quarter. Increased trade flows through the area's ports boosted demand for warehouse space. The market for industrial properties in the Silicon Valley gained momentum in the second and third quarters of 2011. Vacancy rates for Silicon Valley industrial space declined in the third quarter, and lease rates and net absorption rose.

Demand exceeded supply within the San Francisco office market, while the office market in Los Angeles gradually transitioned toward recovery. Office vacancy rates declined in the third quarter in both of these cities. The strength of demand in San Francisco was reflected in the 12.5% vacancy rate in the third quarter, which was down from 16.5% in the first quarter of 2010. Office tenant demand was fueled by the technology sector. Many tech companies pursued the strategy of attracting and retaining a young, well-educated workforce by establishing operations in San Francisco. The office vacancy rate in Los Angeles equaled 17.9% in the third quarter, down only slightly from the 18.0% rate in the second quarter. Los Angeles office lease rates were unchanged last quarter.

In San Francisco, the market for retail space continued to improve, as the area's growth in technology jobs fueled consumer spending. With San Francisco's jobless rate 340 basis points below the California average, sale gains, especially for grocery, fitness and discount apparel retailers, prompted heightened demand for leased space. Conversely, the momentum of the Los Angeles retail market slowed markedly following the robust second half of 2010. The L.A. jobless rate remained elevated, equaling 12.2% in September and averaging 420 basis points higher than the rate of San Francisco. High levels of unemployment in Los Angeles placed a significant damper on retail sales and on retailers' demand for additional space.



Prior to September, valuations of non-residential construction showed progressively higher YoY growth. In September, valuations fell to their lowest level since September 2009. Prior to September, the YTD average valuations were up 16% relative to 2010. The inclusion of September's data brought the YTD comparison down to 13%. Nonetheless, 2011 seemed to be on track to record the second consecutive annual rise in non-residential permit valuations.

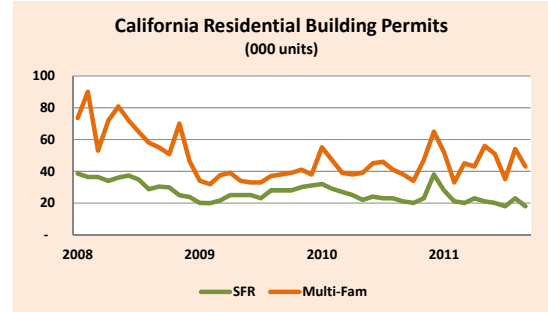
## Housing

The California residential market reflected the national trends. The state's housing market remained anemic. For the first nine months of 2011, California building permits for single-family homes were lower on a YoY comparison and for eight of these nine months single-family permits declined on a monthly basis. In contrast, permits for multi-family residential units showed YoY gains in seven of the first nine months of 2011. So far this year, multi-family

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permits accounted for more than 52% of total residential permits in contrast to 2006 when multi-family permits represented less than 35% of total permits.

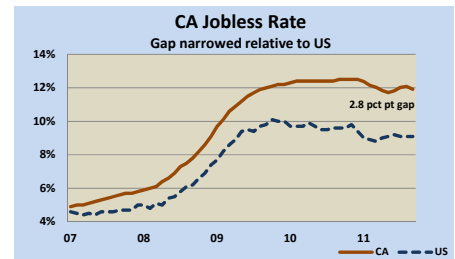
California home sales declined in September 2011, off 2.1% over the month yet up 4.1% over the year. The median price of a home sold in September fell 3.2% from August and 8.3% over the year. The inventory of unsold existing family homes equaled 5.1 months, little changed from August and down from the 5.9 month supply in September 2010. Pending home sales declined 5.2% in September, yet were up 8.4% compared with the year-earlier level. The share of distressed property sales increased to 44.4% of total sales, up from 43.7% in August. Sales of bank-owned properties represented 54% of the distressed sales in September, with short sales accounting for the remaining share. San Benito and Solano counties led the state with the highest percentage of distressed home sales. In those counties, distressed sales accounted for 73% of total sales.



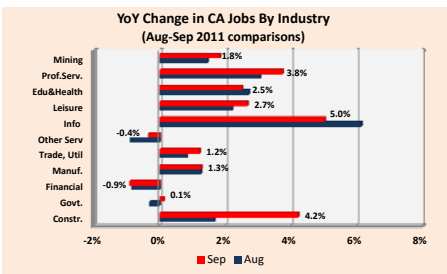
In the third quarter of 2011, the California rate of home affordability rose to 52% from 51% in the second quarter and 46% a year earlier. Housing affordability improved throughout the state with the notable exception of Los Angeles County. The least affordable regions were in the San Francisco Bay area, notably Marin County with its 25% rate of home affordability. The most affordable areas were in the Central Valley and San Bernardino County. According to the survey by the California Association of Realtors, the county with the highest median home price was Marin at \$786,320, while the lowest median priced county was Tulare at \$120,170.

## Employment

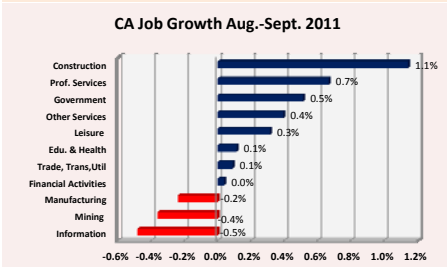
The jobless rate in California equaled 11.9% in September, down from 12.1% in the previous month, yet up from 11.8% at the end of the second quarter. Total payroll employment grew by 11,800 jobs in September and was up 28,300 over June. The household survey showed that employment increased 0.2% YoY, while the number of unemployed declined 4.9% YoY.



In September, the gap between California and U.S. jobless rates narrowed to 2.8 percentage points, down from the record gap of 3.4 percentage points this past January. Of the 2.15 million unemployed Californians, more than 33% of them had been unemployed for more than a year, up from the 30% share a year earlier.

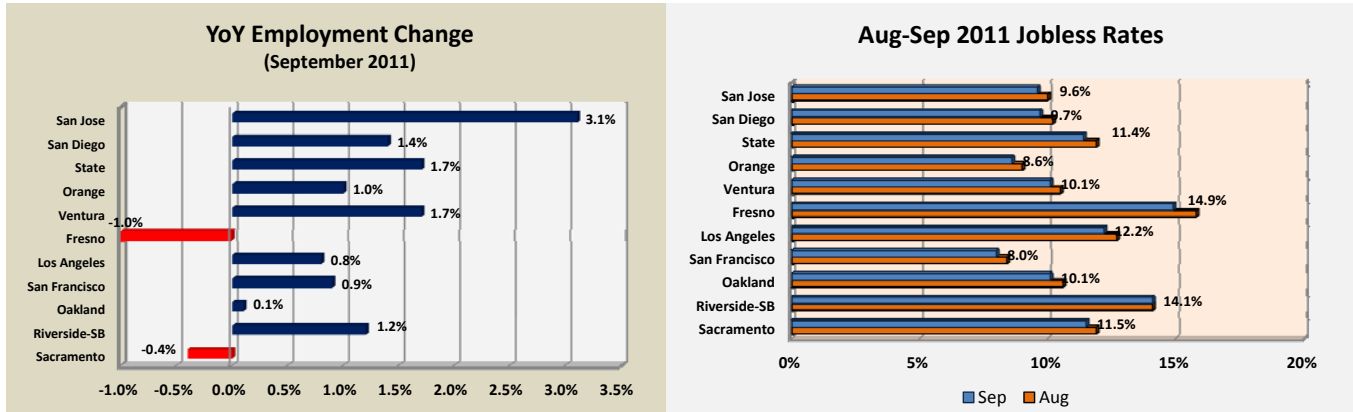


Total payrolls increased 1.8% on a YoY basis, with the information sector reporting the steepest YoY gain at 5.0% followed by construction at 4.2%. In September only financial and other services reported job declines on a YoY basis. On a month-over-month basis, eight of the 11 major industrial sectors reported gains in September. Construction experienced the steepest monthly growth. Three industries shed jobs on a monthly basis, with the information industry reporting the sharpest decline.



Monthly employment data for the major regions of California are available on a non-seasonally adjusted basis. In September, the statewide seasonally unadjusted rate of unemployment equaled 11.4%. For the ten major metropolitan areas of the state, the lowest jobless rate was in the San Francisco MSA at 8.0%, while the highest rate was 14.9% in Fresno County. In addition to San Francisco, the counties of Orange, Santa Clara and San Diego reported jobless rates under 10.0%. In addition to Fresno, Sacramento, Los Angeles and the Inland Empire had jobless rates above the

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statewide average. For the 58 counties within the state, the lowest rate of unemployment was 7.4% for Marin County. The highest jobless rate was in Imperial County at 29.6%. These two counties have consistently held first and last place rankings based upon their jobless rates.

In September, eight of the ten major metropolitan areas reported YoY gains in non-farm payrolls. Only Fresno and Sacramento counties reported decreases. The sharpest YoY job growth was the 3.1% advance in Santa Clara County, in large measure due to the robust expansion in technology. Employment data were reported for 49 counties and MSAs within the state. More than half of these entities reported YoY declines in payroll employment during September, while only 15 of the 49 areas experienced job declines compared with the previous month.

## State Budget

The state ended its 2010-11 fiscal year with nearly \$1.8 billion more in receipts than in expenditures. Total revenues in FY 2011 equaled \$95.5 billion, up 7.8% from the previous fiscal year. Personal income tax receipts accounted for 53% of total revenues, showing a 12.9% gain over the year. Sales and use tax receipts represented 28% of last year's revenues and grew 1.9% during the year. Corporate tax receipts provided 10% of last year's state revenues, expanding 3.8% over the level in the prior fiscal year.

Total expenditures in FY 2011 equaled \$93.8 billion, an 8.2% rise over the year. Local assistance payments accounted for 70% of the FY 2011 total expenditures, up 8.0% over the year. Expenses associated with state operations accounted for 29% of total outlays and grew 14.3% relative to the previous fiscal year.

Based upon data for the first four months of FY 2012, state revenue collections fell \$1.5 billion or 6.2% behind projections. For the first four months of the fiscal year, the largest gap between projected and actual revenues was in other revenues, an outcome that occurred due to the recent expiration of the higher user taxes and fees that were enacted to close previous funding gaps.

Total outlays for the first four months of FY2012 were \$1.7 billion ahead of budget with the over-spending concentrated in the category of local assistance payments. State operation expenses were below budget. The FY2012 budget called for \$86 billion in total spending, which was a reduction of 8.3% from the expenditures in FY2011. The FY2012 budget process required spending cuts to be activated if revenues fall below certain levels. If the revenue shortfall was \$1 billion, the first tier of cuts would trim budgets for the University of California and California State University systems, would increase community college fees and would cut in-home services for the elderly and disabled. A second round of cuts would reduce the school year and eliminate other subsidiaries. The revenue estimates had been predicated on the assumption that the state's economic recovery would be more robust than had materialized and that the greater economic activity would boost revenues significantly.

## Update: United States Banking: Third Quarter 2011

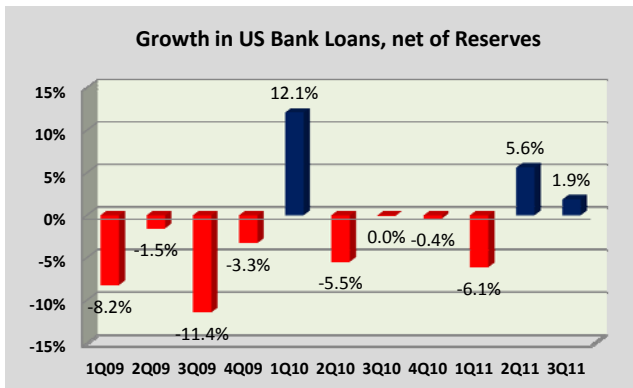
*Loan growth slowed in the third quarter, while improving asset quality contributed to the best earnings performance since early 2007. Capital ratios remained high. The number of banking failures and problem banks declined in the third quarter.*



### Balance Sheet Trends

Total assets of U.S. commercial banks grew at a 6.3% annualized rate in the third quarter, off slightly from 6.9% in the second quarter. Total assets grew to a record \$12.6 trillion. Continuing the pattern that was in place since the beginning of 2011, loans grew more slowly than the growth in total assets. The growth in net loans was a sluggish 1.9% and an easing from the 5.9% growth in the second quarter. Deposits advanced at a 10% rate last quarter. Thus, the loan-to-deposit ratio fell to 70.5% in the third quarter, down from 71.9% in the second quarter and from the recent high of 82.0% in the first quarter of 2009.

Net loans at commercial banks rose \$30 billion in the third quarter. Increased commercial & industrial (C&I) loans and farm loans offset declines in real estate and consumer lending to generate the recent expansion in loans. Within the subsets of real estate loans only the residential categories of apartment and single-family real estate loans were higher on a quarterly basis. All of the major categories of real estate lending, even single-family mortgages, reported reductions YoY. In contrast to real estate lending, C&I loans were up 10% over the past year.

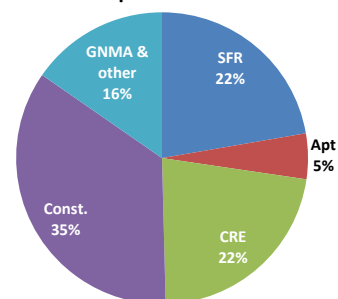


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Banks continued to eliminate their holdings of other real estate owned (OREO) properties during the third quarter. OREO declined to \$45 billion, off \$0.7 billion from the prior quarter and \$2.3 billion below the level in the third quarter of 2010. Declines in OREO on a quarterly and YoY basis were reported for 1-4 family homes, multi-family and construction & development properties. Commercial OREO increased on quarterly and YoY comparisons, while properties foreclosed from GNMA loans were lower on a quarterly basis and up sharply YoY. Construction properties accounted for the largest share of OREO at 35%. The aggregate share of single-family homes and foreclosed GNMA properties equaled 38% of outstanding OREO.

**US OREO by Property Type**  
September 2011



The majority of the \$193 billion increase in total assets was concentrated in the \$70 billion expansion in investment securities and the \$58 billion advance in federal funds sold. The sum of cash, securities and federal funds sold expanded 12% on a YoY basis. This category of bank assets increased to 33% of total assets, up from the 31% share a year earlier. The growth in investment and cash securities was attributable to the slow growth in loans and not from a preference for low-yielding securities.

Growth in domestic bank deposits was brisk over the past year. The YoY growth in deposits held in domestic offices of commercial banks increased 11.9% compared with the third quarter of 2010. Buoying up deposits was the 38% YoY growth in transaction accounts. Unlimited FDIC insurance coverage through 2012 for non-interest bearing deposits contributed to the 31% YoY growth in such deposits. With loan-to-deposit ratios declining, commercial banks allowed time deposits to continue to run down. Time deposits were 12% lower than the year-earlier balances. Core deposits climbed 12.5% YoY. As liquidity in the banking system grew, banks reduced their reliance on borrowed funds and subordinated debt during the third quarter; such borrowing was down 24% YoY. Total equity capital grew at an annualized rate of 6% in the third quarter.

## Earnings

Profits at U.S. commercial banks climbed to \$32.7 billion in the third quarter, the industry's best result since the second quarter of 2007 and an increase of \$6.2 billion over the second quarter results. As was the case for most of the past two years, reductions in loan loss provision expense contributed to the increase in quarterly earnings. The \$0.4 billion reduction in quarterly provision expense, however, was the smallest step-down since the downward trend in provision expense began in the first quarter of 2010.

Since the first quarter of 2010, net interest income declined steadily. From the first quarter of 2010 through the most recent quarter, net interest income declined \$4.5 billion. Over this seven quarter period, interest income declined \$11.5 billion and interest expense was down \$7.0 billion. In the third quarter, interest income fell \$2.6 billion, while the decline in interest expense equaled \$1.9 billion, thus producing a \$0.7 billion quarterly drop in net interest income.

**Quarterly Earnings of US Commercial Banks**  
(\$ millions)

	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11
Total interest income	124,239	121,211	119,657	118,140	115,986	115,393	112,755
Total interest expense	24,285	22,925	21,581	21,372	19,509	19,148	17,253
Net interest income	99,954	98,286	98,075	96,769	96,476	96,246	95,502
Provision for loan losses	48,347	37,745	32,432	29,776	18,900	17,339	16,904
Total non-interest income	56,031	54,723	51,506	54,389	53,846	54,402	55,175
Fiduciary activities	6,075	6,347	6,372	6,701	6,621	6,942	6,996
Service charges on deposits	9,411	9,646	8,634	8,045	7,766	8,149	8,442
Trading account gains	8,297	6,700	4,126	3,472	7,180	7,601	13,132
Additional non-interest income	32,249	32,031	32,375	36,171	32,280	31,711	26,605
Total non-interest expense	87,189	89,030	88,322	94,826	92,166	95,232	91,836
Salaries & employee benefits	38,358	39,738	38,856	39,996	41,822	41,016	40,937
Premises & equipment	10,099	9,883	10,017	10,593	10,315	10,046	10,163
Additional expense	38,732	39,408	39,449	44,237	40,029	44,170	40,736
Pre-tax net operating income	20,450	26,235	28,828	26,556	39,257	38,077	41,937
Securities gains (losses)	1,361	2,072	2,780	2,108	(332)	710	2,909
Incomes taxes	6,238	8,875	9,485	8,931	11,742	12,275	12,464
Extraordinary gains/other	(200)	(409)	(461)	(125)	(143)	(48)	313
Net income	15,373	19,022	21,662	19,608	27,039	26,463	32,695

Non-interest income rose slightly in the third quarter. At \$55.2 billion, non-interest income reached its highest level since the first quarter of 2010. Trading account gains and fees were sharply higher last quarter and more than offset the decline in additional non-interest income. On a YoY comparison, reduced additional non-interest income was more than offset by the steep upturn in trading account gains.

Non-interest expense declined \$3.4 billion in the third quarter, with salary expense marginally lower. The decline in additional non-interest expense nearly reversed the marked step-up in such expenses in the second quarter. Compared with the third quarter of 2010, non-interest expense was up \$3.5 billion, largely due to higher salary expenses.

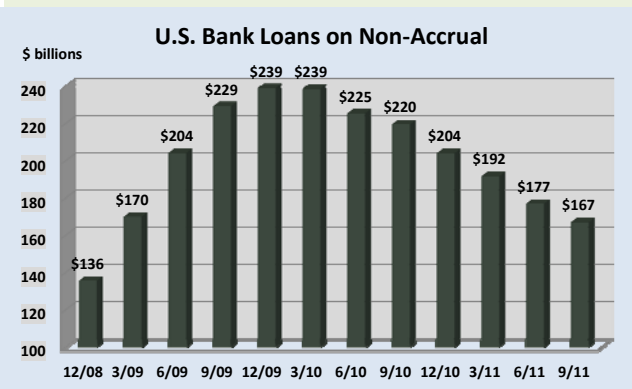
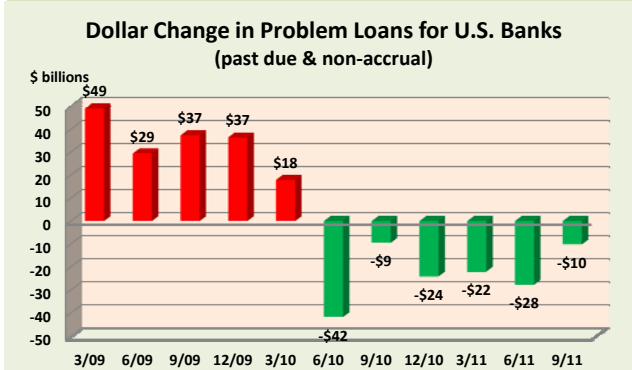
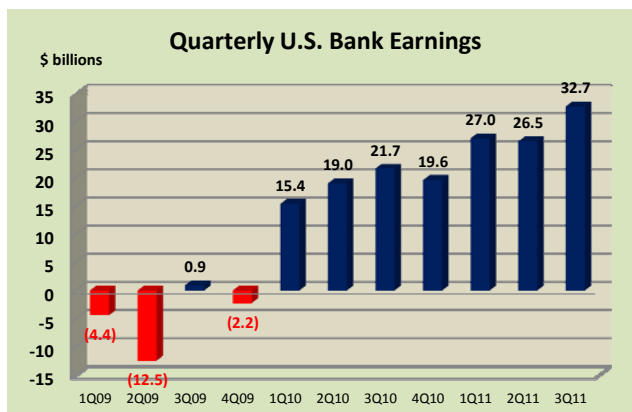
Provision expense was \$0.4 billion below the second quarter and was \$15.5 billion lower than the year-earlier provision. The recent quarter's \$16.9 billion in provision expense contrasted with the record \$64.4 billion taken in the first quarter of 2009. Net earnings in the third quarter 2011 benefitted from the \$2.2 billion in additional gains from securities holdings. Securities gains equaled \$2.9 billion in the third quarter, up from \$0.7 billion in the second quarter.

## Asset Quality

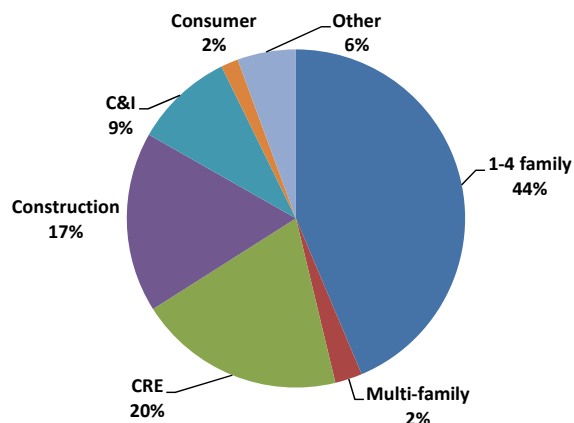
The slow but continuing economic recovery contributed to improvement in the quality of banking assets. Improvement was apparent in the various ratios of asset quality. The volume of problem assets, defined as loans 30 plus days delinquent and on non-accrual, declined in the third quarter. Net loan charge-offs were steadily lower. Due to the improved asset quality, commercial banks continued to reduce provision expense.

Non-accrual loans declined nearly \$10 billion in the third quarter to \$167 billion. Non-accrual loans were down 30% from the first quarter 2010 peak and fell to the lowest level since the fourth quarter of 2008. Non-accrual construction loans declined 52% from its peak. Non-accrual C&I loans were off 59% from their peak. Loans that were 30-89 days delinquent declined in the third quarter, while loans 90 plus days delinquent increased slightly. Total loans 30 plus days delinquent and on non-accrual declined for the sixth consecutive quarter.

Non-current loans represented 4.3% of total U.S. bank loans in the third quarter, compared with 5.2% one year earlier. On a quarterly comparison, this ratio declined 15



## Share of U.S. Non-accrual Loans—3Q2011



basis points. Home equity loans were the only major loan category registering an increased non-current ratio relative to the second quarter. On a YoY basis, all major loan types reported reduced non-current ratios. Although non-current construction loans represented 14.6% of all construction loans in the third quarter, this rate was down from 16.8% a year earlier. Non-current loans plus OREO declined to 2.6% of total assets, compared with 2.8% in the second quarter and 3.3% a year earlier.

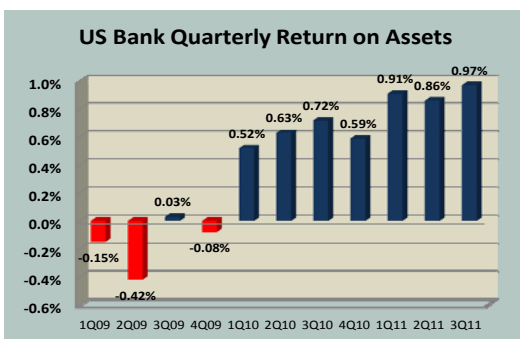
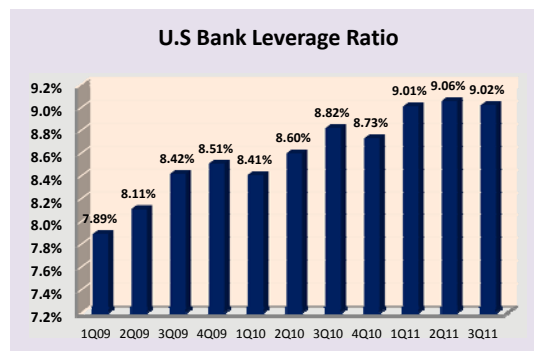
Net charge-offs declined to 1.7% of loans in the third quarter, down from 1.8% in the second quarter and 2.8% a year earlier. Charge-off rates were lower across all major categories of lending both on a quarterly and YoY basis. The highest rate of net charge-offs was in credit cards at 6.0% of such loans, down from 11.3% a year earlier. Commercial banks reported net charge-offs of \$25 billion in the most recent quarter, down from \$26.7 billion in the previous quarter and \$41 billion a year earlier.

## Ratio Trends

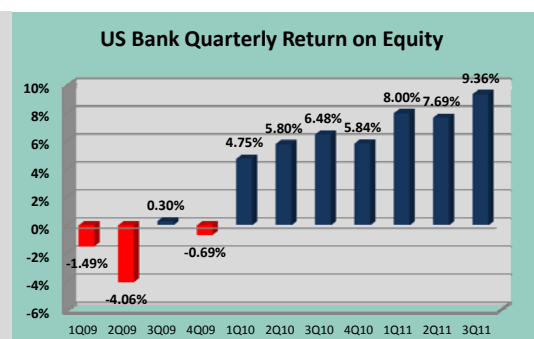
The core capital (leverage) ratio edged slightly lower in the third quarter to 9.02% from 9.06% in the previous quarter, yet was up compared with the 8.82% rate a year earlier. Total risk-based capital ratio slid to 15.22% in the most recent quarter down from 15.25% in the second quarter. A year earlier, the total risk-based capital ratio equaled 14.99%.

The step-up in earnings pushed the quarterly return on assets to 1.05% in the third quarter compared with 0.86% in the second quarter and 0.72% a year earlier. The recent quarter's ROA was the highest rate since the second quarter of 2007.

The quarterly return on equity climbed to 9.36% in the third quarter, up from 7.69% in the second quarter and 6.48% in the year-earlier quarter. This result was the highest ROE since September 2007. The percent of unprofitable institutions equaled 13.7% of all banks, down from 14.8% in the second quarter and 19.2% a year earlier. The share of unprofitable banks was the lowest since March 2008.



Return ratios climbed to their highest levels since the second quarter of 2007.



Banks reported improved efficiency ratios in the third quarter relative to the second quarter. Nonetheless, the year-earlier efficiency ratio was superior to the most recent period. In the third quarter of 2010, commercial banks reported on margin higher net interest income and lower operating expense than in the most recent quarter.

## Banking Population

At the end of the third quarter, there were 6,352 commercial banks, a decline of 61 banks over the quarter and a reduction of 198 banks since the beginning of the year. Through November, the number of banks was reduced by an additional 36 banks to 6,316. YTD through November, there were 90 failures of financial institutions, including 85 commercial banks. Georgia topped the list with the most failures YTD at 23, nearly double the 12 failures for second

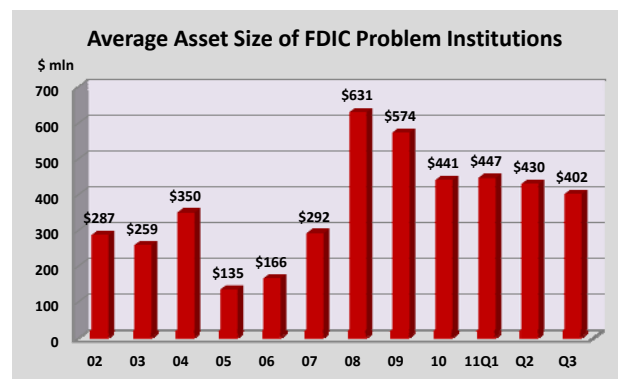
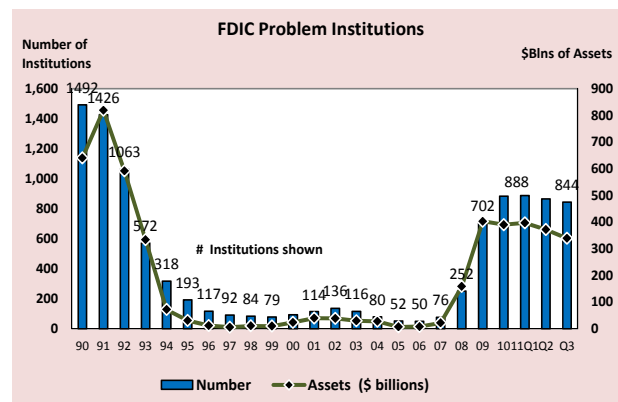
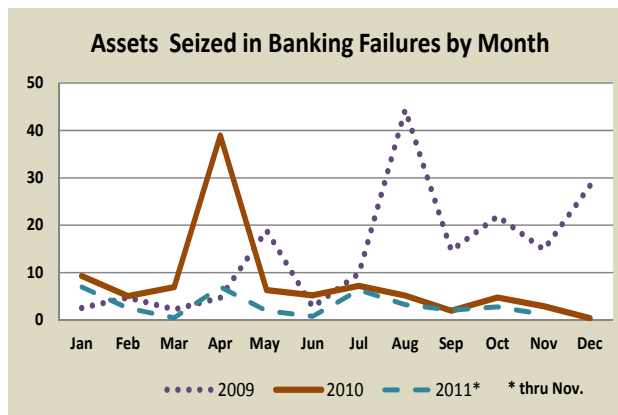
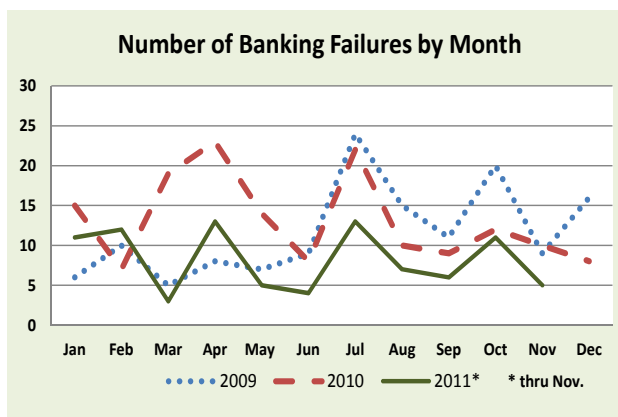
place Florida. The 90 failures involved \$35.1 billion in assets or an average failure size of \$390 million. This average size contrasted with average-sized failures of \$1.2 billion in 2009 and \$600 million in 2010. More than 41% of the 90 banking failures in 2011 involved institutions formed in 2000 or later in contrast to the 29% failure share since 2008 for these newer banks.

If the recent pace of failures continued through year-end, there will be fewer than 95 failures this year, compared with 157 in 2010. According to the recently released FDIC budget for 2012, the agency projected fewer failures in 2012, citing: *"It appears that the peak of the recent banking failures may have passed, and the FDIC is now positioned to begin reducing budget and staffing levels, while continuing to fulfill our mission and maintain readiness to handle remaining bank failures and supervisory challenges."*

The FDIC reported a third-quarter decline in the number of institutions on its problem list. There were 844 institutions classified as problems, down from 865 in the second quarter and 888 in the first quarter. Total assets of the problem institutions equaled \$339 billion, down from \$372 billion in the second quarter and \$397 billion in the first quarter. In addition to the reduction in the number of problem banks, those institutions on the problem list represented a slightly lower percentage of the total number of depository institutions. This share peaked in the first quarter of 2011 at 11.7% and declined to 11.4% in the third quarter. The average asset size of problem institutions narrowed to \$402 million from the recent high of \$631 million in 2008.

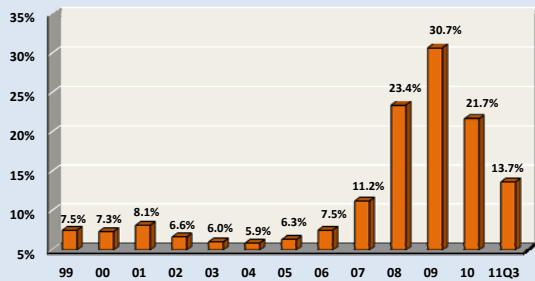
YTD through December 5 2011, there were 143 announced bank mergers of financial institutions. Additionally, there were ten announced mergers that were subsequently terminated. In 2010, there were 215 announced mergers, comprised of 37 mergers that were terminated, 170 mergers that were completed and 8 mergers that were still in process.

The 2011 merger history involved \$193 billion in total assets, compared with \$159 billion for all of 2010. Capital One's acquisition of ING Bank, FSB accounted for nearly 48% of the assets under merger agreements. For mergers with reported deal ratios, the average price to tangible book value (P/TBV) ratio equaled 108.3x in 2011 compared with the 2010 ratio of 119.7x. The highest P/TBV in 2011 was 229x paid by Comerica for Sterling Bancshares. In 2010, the highest P/TBV was 365x.

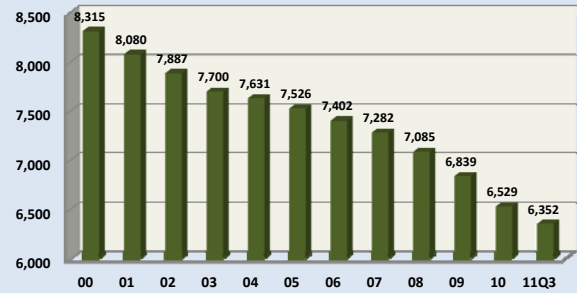


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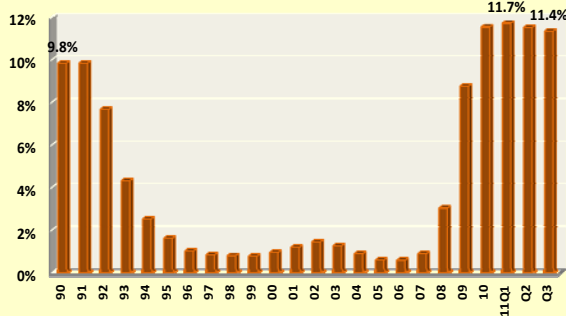
Unprofitable Banks to Total US Banks



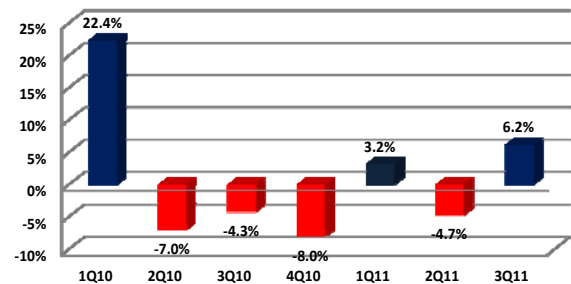
Number of US Banks



Problem Institutions to Total Institutions



Quarterly Change in Net Operating Revenues  
U.S. Banks



## 2009-11 U.S. Bank Performance - By Quarter

(Dollars in Millions % are Averages)

	03/31/09	06/30/09	09/30/09	12/31/09	03/31/10	06/30/10	09/30/10	12/31/10	03/31/11	06/30/11	9/30/2011
Number of institutions	7,039	6,996	6,912	6,840	6,773	6,677	6,623	6,530	6,453	6,413	6,352
Total assets	11,992,091	11,873,290	11,845,195	11,822,923	12,065,683	11,948,391	12,120,116	12,065,933	12,157,610	12,366,570	12,559,925
Net loans & leases	6,544,429	6,519,281	6,333,029	6,281,336	6,471,392	6,382,880	6,382,523	6,376,874	6,279,382	6,367,505	6,397,046
Loan loss allowance	176,061	195,179	204,228	213,836	248,249	237,264	228,196	217,934	205,453	195,221	185,040
Loan loss allowance (%)	2.62%	2.91%	3.12%	3.29%	3.69%	3.58%	3.45%	3.30%	3.17%	2.97%	2.81%
Total deposits	7,982,848	8,077,803	8,178,250	8,333,220	8,294,125	8,242,708	8,373,015	8,514,347	8,675,266	8,855,119	9,077,040
Total equity capital	1,224,832	1,254,312	1,294,022	1,308,380	1,317,957	1,343,530	1,368,495	1,364,523	1,382,994	1,409,122	1,430,205
Net Income (Quarterly)	(4,405)	(12,465)	946	(2,228)	15,373	19,022	21,663	19,608	27,039	26,463	32,695
ROA (Quarterly)	-0.15%	-0.42%	0.03%	-0.08%	0.52%	0.63%	0.72%	0.59%	0.91%	0.86%	0.97%
ROE (Quarterly)	-1.49%	-4.06%	0.30%	-0.69%	4.75%	5.80%	6.48%	5.84%	8.00%	7.69%	9.36%
NPAs/Assets	2.33%	2.73%	3.06%	3.40%	3.49%	3.35%	3.26%	3.11%	2.96%	2.75%	2.62%
NPAs	279,416	324,141	362,463	401,979	421,092	400,271	395,116	375,251	359,865	340,081	329,070
Core capital (leverage) ratio	7.89%	8.11%	8.42%	8.51%	8.41%	8.60%	8.82%	8.73%	9.01%	9.06%	9.02%
Total risk-based capital ratio	13.24%	13.55%	13.92%	14.09%	14.46%	14.82%	14.99%	15.00%	15.28%	15.25%	15.22%
% of unprofitable banks	21.84%	28.90%	26.95%	35.57%	18.96%	20.61%	19.15%	27.34%	15.02%	14.80%	13.66%
# of unprofitable banks	1,537	2,022	1,863	2,433	1,284	1,376	1,268	1,785	969	949	868
% of profitable banks	78.16%	71.10%	73.05%	64.43%	81.04%	79.39%	80.85%	72.66%	84.98%	85.20%	86.34%
# of profitable banks	5,502	4,974	5,049	4,407	5,489	5,301	5,355	4,745	5,484	5,464	5,484

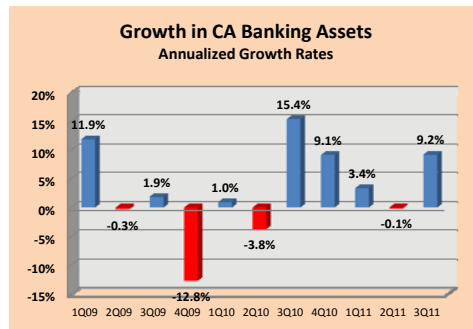
## Update: California Banking: Third Quarter 2011



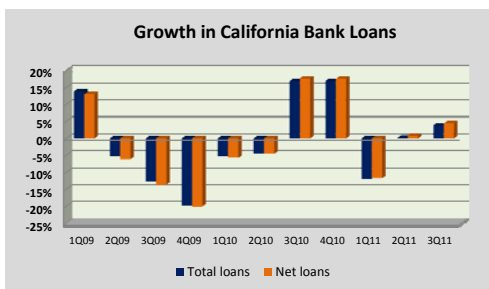
Asset growth rebounded in the third quarter. Loan growth exceeded the national rate, but was still sluggish. Earnings continued to expand. The improvement in asset quality was sustained. The number of banks continued lower, fueled by the pick-up in merger activity.

### Balance Sheet

Total assets of California commercial banks increased \$10 billion in the third quarter to a level of \$444.1 billion. That rise represented an annualized growth of 9.2%, and more than offset the small decline in assets in the second quarter. The annualized third quarter growth in loans equaled 4.3% or more double the growth rate for U.S. loans.



Like the U.S., the growth in California bank deposits greatly exceeded the growth in California loans. The loan-to-deposit ratio for the California banking industry declined to 88.3% in the third quarter from the recent high of 108.7% in the first quarter of 2010.



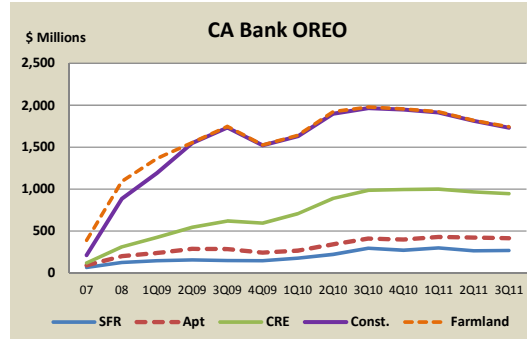
The third quarter rise in net loans was concentrated in C&I and farm loans. Consumer and real estate loans declined. Within the categories of real estate lending, only multi-family loans expanded. Loans were 1% lower on a YoY basis. C&I and farm loans were higher over the year, as was single-family mortgages and apartment loans.

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California banks continued to report a run-off in OREO. Third-quarter increases in 1-4 family residential and farmland OREO were more than offset by reductions in multi-family, commercial and construction and development properties. OREO was down 12% from the peak in such holdings that occurred in the third quarter of 2010.

California bank holdings of cash, due from, securities and federal funds sold increased at a quarterly rate of 6.3% and a YoY rate of 17.4%. The share of such assets to total California bank assets increased from 25.0% in the third quarter of 2010 to 27.8% in the most recent quarter.



California bank deposits increased \$8.5 billion in the third quarter, with significant increases reported in demand deposit and money market account balances. Bank capital grew at an quarterly rate of 2.4% in the third quarter and was up 7.0% compared with year-earlier levels. Unlike the slight reductions in the national capital ratios, California banks reported third-quarter increases. The core leverage capital rate climbed 7 basis points to 10.70%, while the rise in the total risk-based capital ratio equaled 17 basis points to produce a record high of 16.34%.

## Earnings

Earnings of California banks expanded \$8.8 million in the third quarter to a quarterly result of \$1.11 billion, the best quarterly earnings since the fourth quarter of 2009. Unlike the national trend, California banks reported that net interest income rose in the third quarter. Like the nation, the reduction in loss provision contributed greatly to the step-up in California bank earnings. Both non-interest income and non-interest expense declined in the third quarter.

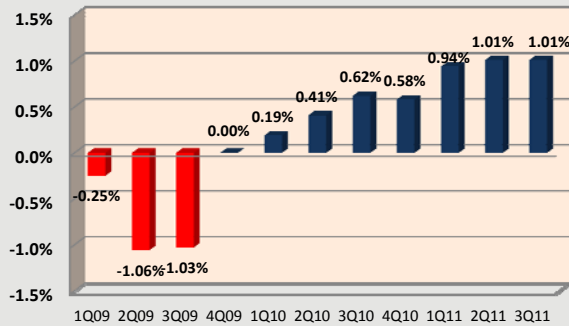
### Quarterly Earnings of CA Commercial Banks

(\$ millions)

	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11
Total interest income	4,351	4,277	4,432	4,476	4,430	4,415	4,401
Total interest expense	842	773	711	649	602	584	559
Net interest income	3,509	3,504	3,721	3,827	3,828	3,831	3,842
Provision for loan losses	1,518	1,054	990	878	398	306	293
Total non-interest income	757	900	822	970	996	894	855
Fiduciary activities	119	120	120	123	125	117	117
Service charges on deposits	243	237	213	215	205	213	211
Trading account gains	37	37	46	58	51	41	53
Additional non-interest income	358	506	444	574	616	522	473
Total non-interest expense	2,493	2,671	2,583	3,017	2,847	2,825	2,807
Salaries & employee benefits	1,278	1,286	1,321	1,478	1,478	1,470	1,483
Premises & equipment	307	310	331	335	328	333	336
Additional expense	908	1,076	931	1,204	1,042	1,022	988
Pre-tax net operating income	255	678	970	902	1,580	1,594	1,596
Securities gains (losses)	93	25	78	61	39	105	44
Incomes taxes	166	291	390	354	600	602	535
Extraordinary gains/other	9	1	1	6	1	1	1
Net income	192	414	659	614	1,020	1,097	1,106

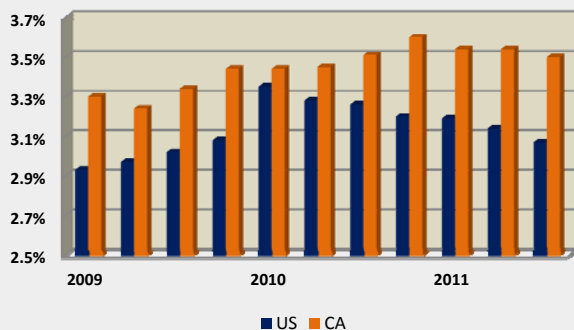
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CA Bank Quarterly Return on Assets



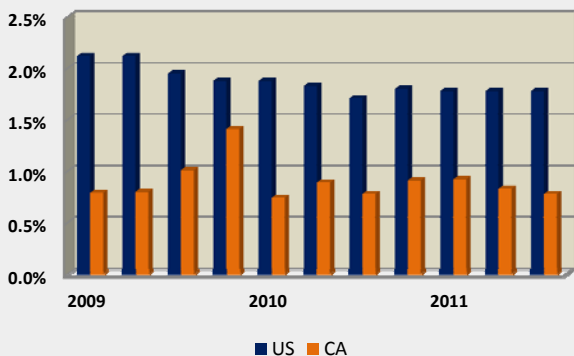
The quarterly return on assets of California banks held steady in the third quarter at 1.01%, while California banks reported a dip in their average return on equity to a rate of 7.74% from 7.87% in the second quarter.

Net Interest Income to Average Assets



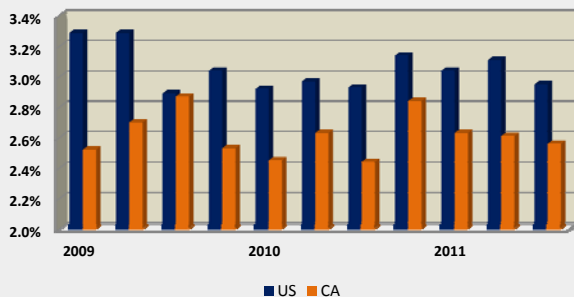
The California banking industry represented 3.5% of the nation's total banking assets. This ratio stood in stark contrast to the state's share of GDP at 13.0% of U.S. GDP.

Non-Interest Income to Average Assets



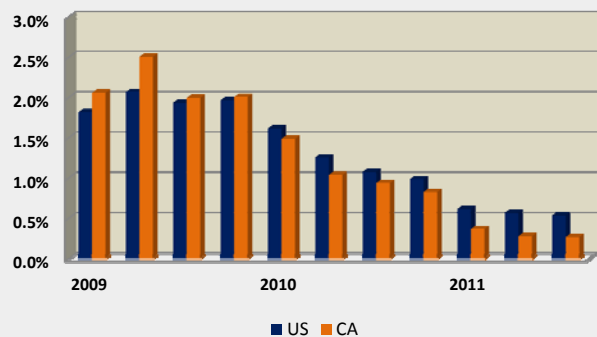
An appropriate method to assess how the state's banking industry performed relative to the nation is predicated upon a review of the earnings statement as a percent of average assets. California banks reported that net interest income as a percent of average assets was significantly higher than the national trend. Since the beginning of 2009, California banks reported that net interest income to average assets averaged 31 basis points higher than the nation. In the third quarter that differential equaled 43 basis points. In contrast, California bank non-interest income as a percent of average assets averaged 98 basis points below the nation over the past 11 quarters. In the third quarter the U.S. differential in non-interest income widened to 100 basis points.

Non-Interest Expense to Average Assets



The California bank ratio of non-interest expense to average assets was consistently lower than the national ratio. Since 2009, California bank expense ratio averaged 44 basis points below the nation. In the third quarter, the non-interest expense ratio differential narrowed to 39 basis points. In terms of provision expense as a percent of average assets, the nation-state comparison showed generally little variance, with the 11-quarter differential averaging only 6 basis points in favor of California. California banks reported higher provision expense ratios than the nation in 2009 and reversed that trend during the last seven quarters. In the third quarter of this year, California provision expense was 27 basis points lower than the national ratio.

Provision Expense to Average Assets



Relative earnings data yielded mixed results, with California banks exhibiting more favorable trends than the nation for net interest income, non-interest expense and provision expense. The state had inferior ratios for non-interest income. On balance, the edge for net income as a percent of average assets went to the U.S. banking industry, with net income to assets averaging 21 basis points higher than the state over the past 11 quarters. During the last three quarters, California banks narrowed the nation's edge, outperforming the national results in the first two quarters of 2011 and lagging only 4 basis points behind the nation in the third quarter.

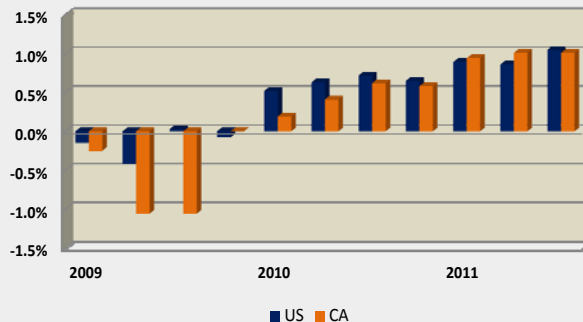
## Asset Quality

Asset quality continued to improve for California banks. California problem assets, as defined as loans 30 plus days delinquent and in non-accrual status, declined in the third quarter, with such assets nearly \$900 million lower than in the second quarter. Loans 30-89 days delinquent increased slightly last quarter, while the volume of loans 90 plus days delinquent and on non-accrual fell sharply. Problem loans declined for seven of the past eight quarters, and non-accrual bank loans dropped to their lowest level since the fourth quarter of 2008. Total non-current assets plus OREO declined to 2.37% of total assets in the third quarter, down from 2.66% in the second quarter and 3.24% a year earlier.

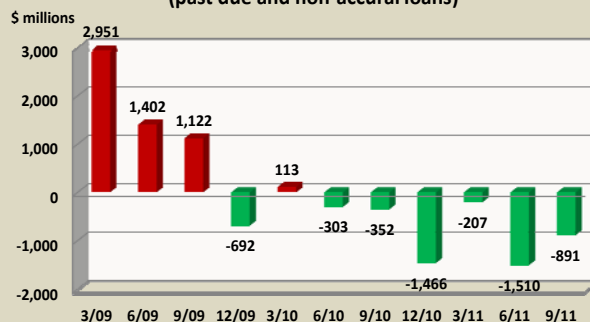
Non-current loans as a percent of total California loans declined 35 basis points in the third quarter to a rate of 3.05%, down from 4.13% a year earlier. Non-current construction and development loans declined 259 basis points to a still lofty 16.84% ratio. Of the major categories of real estate lending, the smallest decline in non-current ratios occurred for single-family mortgages, which dropped to 2.47% from 2.53%. Non-current consumer loans to total consumer loans declined to 1.16% from 1.52% in the second quarter. The California ratio of non-current loans was 124 basis points lower than the national ratio. In early 2007, the state's ratio of non-current loans exceeded the nation. Since 2009, non-current ratios showed significantly greater improvement for California than for the nation.

Net charge-offs fell to 0.71% of California loans from 0.89% in the second quarter. Charge-offs increased as a percent of total construction and development loans and credit card loans. The charge-off rate held steady for apartment loans, while all other lending categories reported reduced rates of charge-offs.

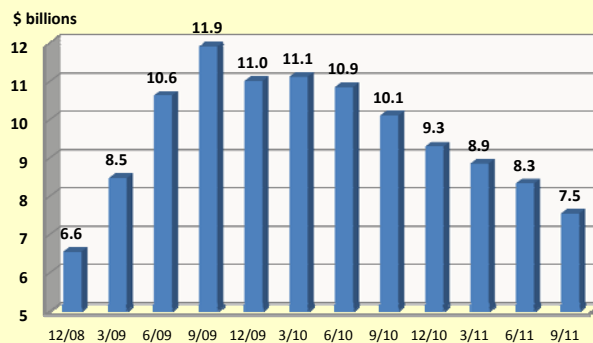
Net Income to Average Assets



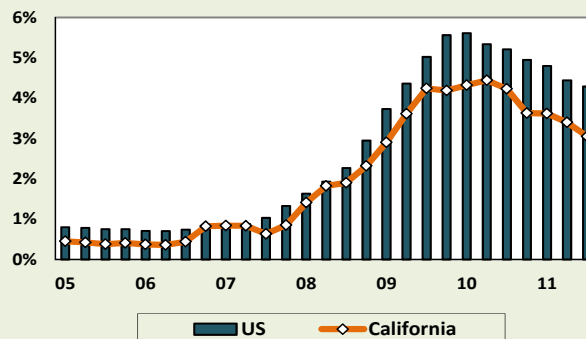
Change in CA Bank Problem Assets (past due and non-accrual loans)



California Bank Non-accrual Loans



Non-Current Loans to Total Loans



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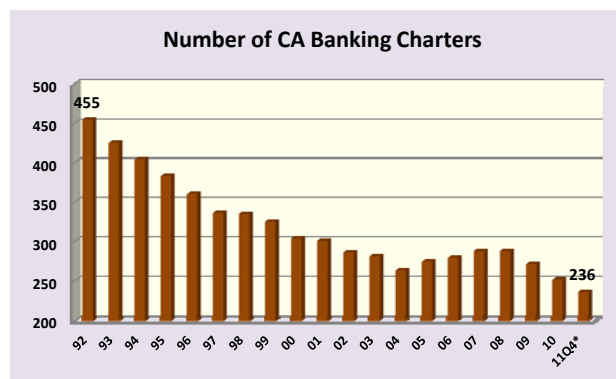
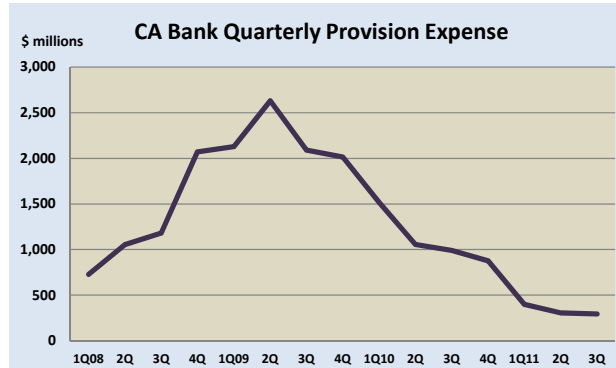
The steady improvement in asset quality allowed California banks to reduce quarterly provision expense. The third quarter's provision of \$293 million was lowest since the third quarter of 2007 and was down by 89% from the record expense of \$2.6 billion taken in the second quarter of 2009. The ratio of loss allowance as a percent of total loans slipped to 1.99%. In the second quarter of this year, the loan loss allowance equaled 2.11% of total loans. This ratio reached a recent high of 2.59% in the second quarter of 2010.

## Population

The number of California commercial banks declined by five in the third quarter to a total of 240. In the fourth quarter through November, four additional California banks were acquired to bring the state's banking population to 236.

Seventeen California banks were acquisition targets in 2011, up from nine mergers announced in 2010. Ten of the 17 mergers announced in 2011 were completed by early December.

YTD through early December a total of four California financial institutions failed, accounting for less than \$1 billion in total banking assets. In 2010, 12 California institutions failed involving \$9.3 billion in assets.



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## 2009-11 California Bank Performance - By Quarter

(Dollars in Millions, % are Averages)

	03/31/09	06/30/09	09/30/09	12/31/09	03/31/10	06/30/10	09/30/10	12/31/10	03/31/11	06/30/11	9/30/2011
Number of institutions	287	284	278	271	266	260	257	251	247	245	240
Total assets	420,138	419,800	421,787	408,312	409,291	405,405	420,977	430,593	434,214	434,075	444,092
Net loans & leases	298,994	294,394	284,355	270,084	266,184	263,122	274,752	286,783	278,334	278,850	281,885
Loan loss allowance	5,849	6,481	7,063	6,824	7,085	7,007	6,766	6,658	6,410	6,007	5,725
Loan loss allowance (%)	1.92%	2.15%	2.42%	2.46%	2.59%	2.59%	2.40%	2.27%	2.25%	2.11%	1.99%
Total deposits	275,114	286,383	291,201	287,545	285,997	282,323	298,905	299,326	309,433	311,865	319,081
Total equity capital	47,580	47,290	48,134	48,214	50,648	51,372	54,473	54,591	55,604	56,933	58,292
Net Income (Quarterly)	(263)	(1,114)	(1,076)	1,246	192	414	659	614	1,020	1,097	1,106
ROA (Quarterly)	-0.25%	-1.06%	-1.03%	0.00%	0.19%	0.41%	0.62%	0.58%	0.94%	1.01%	1.01%
ROE (Quarterly)	-2.24%	-9.41%	-9.03%	0.01%	1.56%	3.28%	4.93%	4.55%	7.46%	7.87%	7.74%
NPAs/Assets	2.40%	3.00%	3.37%	3.22%	3.30%	3.44%	3.24%	2.94%	2.82%	2.66%	2.37%
NPAs	10,083	12,594	14,214	13,148	13,507	13,946	13,640	12,659	12,245	11,546	10,525
Core capital (leverage) ratio	9.08%	8.64%	8.92%	9.51%	9.67%	9.77%	10.08%	10.16%	10.32%	10.63%	10.70%
Total risk-based capital ratio	12.69%	12.54%	13.21%	14.42%	15.08%	15.32%	15.74%	15.48%	16.07%	16.20%	16.34%
% of unprofitable banks	50.52%	57.04%	51.80%	59.04%	38.35%	36.54%	28.79%	34.66%	22.27%	22.04%	22.50%
# of unprofitable banks	145	162	144	160	102	95	74	87	55	54	54
% of profitable banks	49.48%	42.96%	48.20%	40.96%	63.16%	63.46%	71.21%	65.34%	77.73%	77.96%	77.50%
# of profitable banks	142	122	134	111	168	165	183	164	192	191	186

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