EAST WEST BANCORP INC
Form 10-K
March 01, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Mark One

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____ to ____.

Commission file number 000-24939

EAST WEST BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**95-4703316**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
135 North Los Robles Ave., 7th Floor, Pasadena, California	**91101**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code:

(626) 768-6000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.001 Par Value	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:

NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 or Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filed, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filed x Accelerated filer o Non-accelerated filer o

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

The aggregate market value of the registrant s common stock held by non-affiliates is approximately $2,265,914,061 (based on the June 30, 2006 closing price of Common Stock of $37.91 per share).

As of January 31, 2007, 61,511,243 shares of East West Bancorp, Inc. Common Stock were outstanding.

DOCUMENT INCORPORATED BY REFERENCE

Definitive Proxy Statement for the Annual Meeting of Stockholders - Part III

EAST WEST BANCORP, INC.
2006 ANNUAL REPORT ON FORM 10-K
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PART I

Certain matters discussed in this Annual Report may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the 1933 Act) and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act) and as such, may involve risks and uncertainties. These forward-looking statements relate to, among other things, expectations of the environment in which the Company operates and projections of future performance including future earnings and financial condition. The Company s actual results, performance, or achievements may differ significantly from the results, performance, or achievements expected or implied in such forward-looking statements. For a discussion of some of the factors that might cause such differences, see Item 1A. RISK FACTORS. The Company does not undertake, and specifically disclaims any obligation to update any forward looking statements to reflect the occurrence of events or circumstances after the date of such statements except as required by law.

ITEM 1. BUSINESS

Organization

East West Bancorp, Inc. East West Bancorp, Inc. (referred to herein on an unconsolidated basis as East West and on a consolidated basis as the Company or we) is a bank holding company incorporated in Delaware on August 26, 1998 and registered under the Bank Holding Company Act of 1956, as amended. The Company commenced business on December 30, 1998 when, pursuant to a reorganization, it acquired all of the voting stock of East West Bank, or the Bank . The Bank is the Company s principal asset. In addition to the Bank, the Company has eight other subsidiaries, namely East West Insurance Services, Inc., East West Capital Trust I, East West Capital Trust II, East West Capital Statutory Trust III, East West Capital Trust IV, East West Capital Trust V, East West Capital Trust VI, and East West Capital Trust VII.

East West Insurance Services, Inc. On August 22, 2000, East West completed the acquisition of East West Insurance Services, Inc. or, the Agency , in a stock exchange transaction. The Agency provides business and consumer insurance services to the Southern California market. The Agency runs its operations autonomously from the operations of the Company.

Other Subsidiaries of East West Bancorp, Inc. The Company has established seven other subsidiaries as statutory business trusts, East West Capital Trust I and East West Capital Trust II in 2000, East West Capital Statutory Trust III in 2003, East West Capital Trust IV and East West Capital Trust V in 2004, East West Capital Trust VI in 2005, and East West Capital Trust VII in 2006, collectively referred to as the Trusts . In seven separate private placement transactions, the Trusts have issued either fixed or variable rate capital securities representing undivided preferred beneficial interests in the assets of the Trusts. East West is the owner of all the beneficial interests represented by the common securities of the Trusts. The purpose of issuing the capital securities was to provide the Company with a cost-effective means of obtaining Tier I capital for regulatory purposes. In accordance with Financial Accounting Standards Interpretation No. 46R, *Consolidation of Variable Interest Entities* (FIN No. 46R), the Trusts are not consolidated into the accounts of the Company.

East West s principal business is to serve as a holding company for the Bank and other banking or banking-related subsidiaries which East West may establish or acquire. East West has not engaged in any other activities to date. As a legal entity separate and distinct from its subsidiaries, East West s principal source of funds is, and will continue to be, dividends that may be paid by its subsidiaries. East West s other sources of funds include proceeds from the issuance of its common stock in connection with stock option

and warrant exercises and employee stock purchase plans. At December 31, 2006, the Company had $10.82 billion in total consolidated assets, $8.18 billion in net consolidated loans, and $7.24 billion in total consolidated deposits.

The principal office of the Company is located at 135 N. Los Robles Ave., 7th Floor, Pasadena, California 91101, and the telephone number is (626) 768-6000.

East West Bank. East West Bank was chartered by the Federal Home Loan Bank Board in June 1972, as the first federally chartered savings institution focused primarily on the Chinese-American community, and opened for business at its first office in the Chinatown district of Los Angeles in January 1973. From 1973 until the early 1990 s, the Bank conducted a traditional savings and loan business by making predominantly long-term, single family residential and commercial and multifamily real estate loans. These loans were made principally within the ethnic Chinese market in Southern California and were funded primarily with retail savings deposits and advances from the Federal Home Loan Bank of San Francisco. The Bank has emphasized commercial lending since its conversion to a state-chartered commercial bank on July 31, 1995. The Bank now also provides loans for commercial, construction, and residential real estate projects and for the financing of international trade for companies in California.

Acquisitions of existing banks have contributed to the Bank s growth. On May 28, 1999, the Bank completed its acquisition of First Central Bank, N.A. for an aggregate cash price of $13.5 million. First Central Bank had three branches in Southern California one branch located in the Chinatown sector of Los Angeles, one branch in Monterey Park and one branch in Cerritos. The Bank acquired approximately $55.0 million in loans and assumed approximately $92.6 million in deposits.

On January 18, 2000, the Bank completed its acquisition of American International Bank for an aggregate cash price of $33.1 million. American International Bank had eight branches in Southern California. The Bank acquired approximately $107.9 million in loans and assumed approximately $170.8 million in deposits.

On January 16, 2001, the Bank completed the acquisition of Prime Bank for a combination of shares and cash valued at $16.6 million. Prime Bank was a one-branch commercial bank located in the Century City area of Los Angeles. The Bank acquired approximately $45.0 million in loans and assumed approximately $98.1 million in deposits.

On March 14, 2003, the Bank completed its acquisition of Pacific Business Bank for an aggregate cash price of $25.0 million. Pacific Business Bank operated four branches in Southern California located in Santa Fe Springs, Carson, El Monte, and South El Monte. The Bank acquired approximately $110.1 million in loans and $134.9 million in deposits.

On August 6, 2004, the Bank completed its acquisition of Trust Bancorp, parent company of Trust Bank, in an all-stock transaction valued at $32.9 million. Trust Bank operated four branches in Southern California, located in Monterey Park, Rowland Heights, West Covina and Arcadia. The Bank acquired approximately $164.0 million in loans and assumed $193.4 million in deposits through this acquisition.

On September 6, 2005, the Bank completed its acquisition of United National Bank (UNB), a commercial bank headquartered in San Marino, California. The purchase price was $177.9 million with sixty percent paid in stock and the remainder in cash. UNB provided community banking services through eleven branches, with eight located in Southern California, two in Northern California and one in Houston, Texas. The Bank acquired approximately $665.0 million in net loans receivable and assumed $865.1 million in deposits through this acquisition.

On March 17, 2006, the Bank completed its acquisition of Standard Bank, a federal savings bank headquartered in Monterey Park, California. The purchase price was $200.3 million with sixty-seven percent paid in stock and the remainder in cash. Standard Bank provided banking services to the community through six branches in the Los Angeles metropolitan area. The Bank acquired approximately $490.0 million in net loans receivable and assumed $728.5 million in deposits through this acquisition.

The Bank has also grown through strategic partnerships and additional branch locations. On August 30, 2001, the Bank entered into an exclusive ten-year agreement with 99 Ranch Market to provide retail banking services in their stores throughout California. 99 Ranch Market is the largest Asian-focused chain of supermarkets on the West Coast, with twenty-two full service stores in California, two in Washington, and affiliated licensee stores in Arizona, Georgia, Hawaii, Nevada, and Indonesia. Tawa Supermarket Companies or Tawa is the parent company of 99 Ranch Market. Tawa s property development division owns and operates many of the shopping centers where 99 Ranch Market stores are located. We are currently providing in-store banking services to eight 99 Ranch Market locations in Southern California and one in Northern California.

The Bank continues to expand its market presence in the international arena. On January 20, 2003, the Bank opened its first overseas office in Beijing, China. The Beijing representative office serves to further develop the Bank s existing international banking capabilities. In addition to facilitating traditional letters of credit and trade finance business, the Beijing office allows the Bank to assist existing clients, as well as develop new business relationships. Through this office, the Bank is focused on growing its export-import lending volume by aiding domestic exporters in identifying and developing new sales opportunities to China-based customers as well as capturing additional letters of credit business generated from China-based exports through broader correspondent banking relationships with a variety of Chinese financial institutions.

On August 1, 2006, we received approval from the Hong Kong Monetary Authority (HKMA) to open a branch in Hong Kong. This branch is the Bank s first full-service branch office offering a variety of deposit, loan, and international banking products. The Hong Kong branch commenced business operations during the first quarter of 2007. On December 31, 2006, we also received regulatory approval to open a representative office in Shanghai, China. Similar to the Beijing representative office, the Shanghai office is anticipated to augment the Bank s international banking capabilities in the greater China region relative to its existing client base as well as new business relationships.

Banking Services

The Bank was the second largest independent commercial bank headquartered in Southern California as of December 31, 2006, and one of the largest banks in the United States that focuses on the Chinese-American community. Through its network of 60 banking locations, the Bank provides a wide range of personal and commercial banking services to small and medium-sized businesses, business executives, professionals, and other individuals. The Bank offers multilingual services to its customers in English, Cantonese, Mandarin, Vietnamese, and Spanish. The Bank also offers a variety of deposit products which includes the traditional range of personal and business checking and savings accounts, time deposits and individual retirement accounts, travelers checks, safe deposit boxes, and MasterCard and Visa merchant deposit services.

The Bank s lending activities include residential and commercial real estate, construction, commercial, trade finance, accounts receivable, small business administration, or the SBA , inventory and working capital loans. It provides commercial loans to small and medium-sized businesses with annual revenues that generally range from several million to $200 million. In addition, the Bank provides

short-term trade finance facilities for terms of less than one year primarily to U.S. importers and manufacturers doing business in the Asia Pacific region. The Bank s commercial borrowers are engaged in a wide variety of manufacturing, wholesale trade, and service businesses.

Market Area and Competition

The Bank concentrates on marketing its services in the Los Angeles metropolitan area, Orange County, the San Francisco Bay area, San Mateo County, the Silicon Valley area in Santa Clara County and Alameda County, with a particular focus on regions with a high concentration of ethnic Chinese. The ethnic Chinese markets within the Bank s primary market area have experienced rapid growth in recent years. According to information provided by the California State Department of Finance, there were an estimated 4.7 million Asians and Pacific Islanders residing in California, or 13.2% of the total population, as of March 2004. As California continues to gain momentum as the hub of the Pacific Rim, the Bank provides important competitive advantages to its customers participating in the Asia Pacific marketplace. We believe that our customers benefit from our understanding of Asian markets and cultures, our corporate and organizational ties throughout Asia, as well as our international banking products and services. We believe that this approach, combined with the extensive ties of our management and Board of Directors to the growing Asian and ethnic Chinese communities, provides us with an advantage in competing for customers in our market area.

The banking and financial services industry in California generally, and in our market areas specifically, is highly competitive. The increasingly competitive environment is a result primarily of changes in laws and regulation, changes in technology and product delivery systems, and the accelerating pace of consolidation among financial services providers.

The Bank competes for loans, deposits, and customers with other commercial banks, savings and loan associations, savings banks, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions, and other nonbank financial service providers. Some of these competitors are larger in total assets and capitalization, have greater access to capital markets, including foreign-ownership, and offer a broader range of financial services than the Bank. The Bank has 59 branches in California located in the following counties: Los Angeles, Orange, San Bernardino, San Francisco, San Mateo, Santa Clara and Alameda. Neither the deposits nor loans of the offices of the Bank exceed 1% of the deposits or loans of all financial services companies located in the counties in which it operates.

Additionally, the Bank has one branch in Houston, Texas as a result of the UNB acquisition in September 2005.

Recently Issued Accounting Standards

In December 2003, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants (AICPA) issued Statement of Position No. 03-3 (SOP 03-3), *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*. SOP 03-3 addresses the accounting for differences between contractual cash flows and the cash flows expected to be collected from purchased loans or debt securities if those differences are attributable, in part, to credit quality. SOP 03-3 requires purchased loans and debt securities to be recorded initially at fair value based on the present value of the cash flows expected to be collected with no carryover of any valuation allowance previously recognized by the seller. Interest income should be recognized based on the effective yield from the cash flows expected to be collected. To the extent that the purchased loans or debt securities experience subsequent deterioration in credit quality, a valuation allowance would be established for any additional cash flows

that are not expected to be received. However, if more cash flows subsequently are expected to be received than originally estimated, the effective yield would be adjusted on a prospective basis. SOP 03-3 is effective for loans and debt securities acquired by the Company after December 15, 2004. The adoption of this Statement on January 1, 2005 did not have a material impact on the Company s financial position, results of operations, or cash flows.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, which addresses accounting for changes in accounting principle, changes in accounting estimates, changes required by an accounting pronouncement in the instance that the pronouncement does not include specific transition provisions and error correction. SFAS No. 154 requires retrospective application to prior periods financial statements of changes in accounting principle and error correction unless impracticable to do so. SFAS No. 154 states an exception to retrospective application when a change in accounting principle, or the method of applying it, may be inseparable from the effect of a change in accounting estimate. When a change in principle is inseparable from a change in estimate, such as depreciation, amortization or depletion, the change to the financial statements is to be presented in a prospective manner. SFAS No. 154 and the required disclosures are effective for accounting changes and error corrections in fiscal years beginning after December 15, 2005.

In November 2005, the FASB issued Staff Position (FSP) Nos. FAS 115-1 and 124-1 to address the determination as to when an investment is considered impaired, whether that impairment is other than temporary and the measurement of an impairment loss. This FSP nullified certain requirements of Emerging Issues Task Force 03-1 *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (EITF 03-1), and references existing other than temporary guidance. Furthermore, this FSP creates a three step process in determining when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. The FSP is effective for reporting periods beginning after December 15, 2005. The adoption of this FSP did not have a material impact on the Company s financial condition or results of operations.

During December 2005, the FASB issued FSP Statement of Position (SOP) 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk*, which addresses the circumstances under which the terms of loan products give rise to such risk and the disclosures or other accounting considerations that apply for entities that originate, hold, guarantee, service, or invest in loan products with terms that may give rise to a concentration of credit risk. The guidance under this FSP is effective for interim and annual periods ending after December 19, 2005 and for loan products that are determined to represent a concentration of credit risk, disclosure requirements of SFAS No. 107, *Disclosures about Fair Value of Financial Instruments*, should be provided for all periods presented. The adoption of this FSP did not have a significant impact on the Company s consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets*, which provides the following: 1) revised guidance on when a servicing asset and servicing liability should be recognized; 2) requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable; 3) permits an entity to elect to measure servicing assets and servicing liabilities at fair value each reporting date and report changes in fair value in earnings in the period in which the changes occur; 4) upon initial adoption, permits a onetime reclassification of available-for-sale securities to trading securities for securities which are identified as offsetting the entity s exposure to changes in the fair value of servicing assets or liabilities that a servicer elects to subsequently measure at fair value; and 5) requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional footnote disclosures. SFAS No. 156 is effective as of the beginning of an entity s first fiscal year that begins after September 15, 2006 with the effects of initial adoption being reported as a cumulative-effect adjustment to retained earnings. It

is not anticipated that adoption will have a material impact on the Company s consolidated financial statements.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48) which supplements SFAS No. 109, *Accounting for Income Taxes*, by defining the confidence level that a tax position must meet in order to be recognized in the financial statements. The Interpretation requires that the tax effects of a position be recognized only if it is more-likely-than-not to be sustained based solely on its technical merits as of the reporting date. The more-likely-than-not threshold represents a positive assertion by management that a company is entitled to economic benefits of a tax position. If a tax position is not considered more-likely-than-not to be sustained based solely on its technical merits, no benefits of the position are to be recognized. Moreover, the more-likely-than-not threshold must continue to be met in each reporting period to support continued recognition of a benefit. At adoption, companies must adjust their financial statements to reflect only those tax positions that are more-likely-than-not to be sustained as of the adoption date. Any necessary adjustment would be recorded directly to retained earnings in the period of adoption and reported as a change in accounting principle. FIN 48 is effective for fiscal years beginning after December 15, 2006. Management has evaluated the Company s uncertain tax positions in accordance with the provisions of FIN 48. During the first quarter of 2007, the adoption of this standard is expected to result in a reduction of retained earnings by approximately $6.5 million to $7.5 million. This adjustment will be recorded on a net of tax basis.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 108, *Quantifying Financial Misstatements*, which expresses the Staff s views regarding the process of quantifying financial statement misstatements. Registrants are required to quantify the impact of correcting all misstatements, including both the carryover and reversing effects of prior year misstatements, on the current year financial statements. The techniques most commonly used in practice to accumulate and quantify misstatements are generally referred to as the rollover (current year income statement perspective) and iron curtain (year-end balance perspective) approaches. The financial statements would require adjustment when either approach results in quantifying a misstatement that is material, after considering all relevant quantitative and qualitative factors. Management does not expect this guidance to have a material effect on the Company s financial condition and results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which provides a single definition of fair value, establishes a framework for measuring fair value in generally accepted accounting principles, expands required disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 12, 2007, and interim periods within those years. The provisions of SFAS No. 157 should be applied on a prospective basis. Management is assessing the potential impact of this guidance on the Company s financial condition and results of operations.

In September 2006, the FASB issued SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*, which requires employers to fully recognize obligations associated with single-employer defined benefit pension, retiree healthcare and other postretirement plans in their financial statements. The provisions of SFAS No, 158 require employers to (a) recognize in its statement of financial position an asset for a plan s overfunded status or a liability for a plan s underfunded status; (b) measure a plan s assets and its obligations that determine its funded status as of the end of the employer s fiscal year (with limited exceptions); and (c) recognize changes in the funded status of a defined benefit postretirement plan in the year in which the changes occur. These changes will be reported in comprehensive income in the statement of changes in stockholders equity. Statement No. 158 applies to plan sponsors that are public and private companies and nongovernmental not-for-profit organizations. The requirement to recognize the funded status of a benefit plan and the disclosure requirements are

effective as of the end of the fiscal year ending after December 15, 2006, for entities with publicly traded equity securities, and at the end of the fiscal year ending after June 15, 2007, for all other entities. The requirement to measure plan assets and benefit obligations as of the date of the employer s fiscal year-end statement of financial position is effective for fiscal years ending after December 15, 2008. It is not anticipated that adoption will have a material impact on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, which establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. This standard requires companies to provide additional information that will help investors and other users of financial statements to more easily understand the effect of the company s choice to use fair value on its earnings. It also requires entities to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. This new guidance does not eliminate disclosure requirements included in other accounting standards, including fair value measurement disclosures required by SFAS No. 157 and SFAS No. 107, *Disclosures about Fair Value of Financial Instruments*. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity makes that choice in the first 120 days of that fiscal year and also elects to apply the provisions of SFAS N0. 157. Management does not expect this guidance to have a material effect on the Company s financial condition and results of operations.

Economic Conditions, Government Policies, Legislation, and Regulation

The Company s profitability, like most financial institutions, is primarily dependent on interest rate differentials. In general, the difference between the interest rates paid by the Bank on interest-bearing liabilities, such as deposits and other borrowings, and the interest rates received by the Bank on our interest-earning assets, such as loans extended to customers and securities held in our investment portfolio, will comprise the major portion of the Company s earnings. These rates are highly sensitive to many factors that are beyond the control of the Company and the Bank, such as inflation, recession and unemployment, and the impact which future changes in domestic and foreign economic conditions might have on the Company and the Bank cannot be predicted.

The Company s business is also influenced by the monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Board of Governors of the Federal Reserve System (the FRB). The FRB implements national monetary policies (with objectives such as curbing inflation and combating recession) through its open-market operations in U.S. Government securities by adjusting the required level of reserves for depository institutions subject to its reserve requirements, and by varying the target federal funds and discount rates applicable to borrowings by depository institutions. The actions of the FRB in these areas influence the growth of bank loans, investments, and deposits and also affect interest earned on interest-earning assets and paid on interest-bearing liabilities. The nature and impact of any future changes in monetary and fiscal policies on the Company cannot be predicted.

From time to time, federal and state legislation is enacted which may have the effect of materially increasing the cost of doing business, limiting or expanding permissible activities, or affecting the competitive balance between banks and other financial services providers. The Company cannot predict whether or when potential legislation will be enacted, and if enacted, the effect that it, or any implementing regulations, would have on our financial condition or results of operations. In addition, the outcome of any investigations initiated by state or federal authorities or litigation may result in necessary changes in our operations, additional regulation and increased compliance costs.

Supervision and Regulation

General. The Company and the Bank are extensively regulated under both federal and state laws. Regulation and supervision by the federal and state banking agencies is intended primarily for the protection of depositors and the Deposit Insurance Fund (DIF) administered by the Federal Deposit Insurance Corporation (FDIC) and not for the benefit of stockholders. Set forth below is a summary description of key laws and regulations which relate to our operations. These descriptions are qualified in their entirety by reference to the applicable laws and regulations.

The Company. As a bank and financial holding company, the Company is subject to regulation and examination by the FRB under the Bank Holding Company Act of 1956, as amended (or BHCA). The Company is required to file with the FRB periodic reports and such additional information as the FRB may require.

The FRB may require us to terminate an activity or terminate control of or liquidate or divest certain subsidiaries, affiliates or investments if the FRB believes the activity or the control of the subsidiary or affiliate constitutes a significant risk to the financial safety, soundness or stability of any bank subsidiary. The FRB also has the authority to regulate provisions of certain bank holding company debt, including the authority to impose interest ceilings and reserve requirements on such debt. Under certain circumstances, we must file written notice and obtain FRB approval prior to purchasing or redeeming our equity securities. Further, we are required by the FRB to maintain certain levels of capital. See Capital Standards.

The Company is required to obtain prior FRB approval for the acquisition of more than 5% of the outstanding shares of any class of voting securities or substantially all of the assets of any bank or bank holding company. Prior FRB approval is also required for the merger or consolidation of a bank holding company with another bank holding company. Similar state banking agency approvals may also be required. Certain competitive, management, financial and other factors are considered by the bank regulatory agencies in granting these approvals.

With certain exceptions, the Company is prohibited from acquiring direct or indirect ownership or control of more than 5% of the outstanding voting shares of any company that is not a bank or bank holding company and from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or furnishing services to subsidiaries. However, subject to prior notice or FRB approval, bank holding companies may engage in any, or acquire shares of companies engaged in, those nonbanking activities determined by the FRB deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. The Company may also engage in these nonbanking and certain other activities without prior FRB approval pursuant to our election as a financial holding company.

FRB regulations require that bank holding companies serve as a source of financial and managerial strength to subsidiary banks and commit resources as necessary to support each subsidiary bank. A bank holding company s failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice or a violation of FRB regulations or both. The FRB s bank holding company rating system also emphasizes risk management and evaluation of the potential impact of nondepository entities on safety and soundness.

The Company is also a bank holding company within the meaning of the California Financial Code. As such, the Company and its subsidiaries are subject to examination by, and may be required to file reports with, the California Department of Financial Institutions (DFI).

Financial Holding Company Status

In order to elect or retain financial holding company status, all depository institution subsidiaries of a bank holding company must be well capitalized, well managed, and, except in limited circumstances, be in satisfactory compliance with the Community Reinvestment Act (or CRA). Failure to sustain compliance with these requirements or correct any non-compliance within a fixed time period could lead to divestiture of subsidiary banks or require all activities to conform to those permissible for a bank holding company. The Company elected to become a financial holding company on July 17, 2000 and is currently in compliance with the financial holding company election requirements.

As a financial holding company, we may affiliate with securities firms and insurance companies and engage in other activities without prior FRB notice or approval that are determined to be financial in nature or are incidental or complementary to activities that are financial in nature. Financial in nature activities include:

- lending, exchanging, transferring, investing for others, or safeguarding financial assets other than money or securities;
- providing any device or other instrumentality for transferring money or other financial assets;
- arranging, effecting or facilitating financial transactions for the account of third parties;
- securities underwriting;
- dealing and market making;
- sponsoring mutual funds and investment companies;
- insurance underwriting and agency sales;
- merchant banking investments; and
- activities that the FRB, in consultation with the Secretary of the Treasury, determines from time to time to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

The Bank. As a California chartered bank, the Bank is subject to primary supervision, periodic examination, and regulation by the DFI. In September 2004, the Bank became a member bank of the Federal Reserve System and the FRB replaced the FDIC as the Bank s primary federal regulator. If, as a result of an examination, the DFI or the FRB should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank s operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, various remedies are available to the DFI and the FRB. These remedies include the power to require affirmative action to correct any conditions resulting from any violation or practice; enter into informal nonpublic or formal public memoranda of understanding or written agreements with the Bank to take corrective action; issue an administrative cease and desist order that can be judicially enforced; direct an increase in capital; enjoin unsafe and unsound practices; restrict the Bank s growth; assess civil monetary penalties; and remove officers and directors. Ultimately, the DFI could take possession and close and liquidate the Bank.

Changes such as the following in federal or state banking laws or the regulations, policies or guidance of the federal or state banking agencies could have an adverse cost or competitive impact on the Company, the Bank and our operations:

(i) In December 2006, the federal banking agencies issued final guidance to reinforce sound risk management practices for bank holding companies and banks in commercial real estate (CRE) loans which establishes CRE concentration thresholds as criteria for examiners to identify CRE concentration that may warrant further analysis. The implementation of these guidelines could

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result in increased reserves and capital costs for banks with CRE concentration. Management believes that the Bank s CRE portfolio as of December 31, 2006 does not have the risks associated with high CRE concentration due to mitigating factors, including low loan-to-value ratios, adequate debt coverage ratios and a wide variety of property types.

(ii) In September 2006, the federal banking agencies issued final guidance on alternative residential mortgage products that allow borrowers to defer repayment of principal and sometimes interest, including interest-only mortgage loans, and payment option adjustable rate mortgages where a borrower has flexible payment options, including payments that have the potential for negative amortization. While acknowledging that innovations in mortgage lending can benefit some consumers, the final guidance states that management should (1) assess a borrower s ability to repay the loan, including any principal balances added through negative amortization, at the fully indexed rate that would apply after the introductory period; (2) recognize that certain nontraditional mortgages are untested in a stressed environment and warrant strong risk management standards as well as appropriate capital and loan loss reserves; and (3) ensure that borrowers have sufficient information to clearly understand loan terms and associated risks prior to making a product or payment choice. The Bank believes its products and disclosures are in conformance with the requirements of the guidance.

(iii) Pursuant to the Financial Services Regulatory Relief Act of 2006, the SEC and the FRB have released, as Regulation R, joint proposed rules expected to be finalized by midyear to implement exceptions provided for in the Gramm-Leach-Bliley Act (GLBA) for bank securities activities which banks may conduct without registering with the SEC as securities brokers or moving such activities to a broker-dealer affiliate. The proposed Regulation R push out rules exceptions would allow a bank, subject to certain conditions, to continue to conduct securities transactions for customers as part of the Bank s trust and fiduciary, custodial and deposit sweep functions, and to refer customers to a securities broker-dealer pursuant to a networking arrangement with the broker-dealer. The proposed rules, if adopted, are not expected to have a material effect on the current securities activities which the Bank now conducts for customers.

Because California permits commercial banks chartered by the state to engage in any activity permissible for national banks, the Bank may form subsidiaries to engage in the many so-called closely related to banking or nonbanking activities commonly conducted by national banks in operating subsidiaries, and may conduct certain financial activities in a subsidiary to the same extent as may a national bank. However, in order to form a financial subsidiary, the Bank must be well-capitalized, well-managed and in satisfactory compliance with the CRA. Further, the Bank must exclude from its assets and equity all equity investments, including retained earnings, in a financial subsidiary. The assets of the subsidiary may not be consolidated with the Bank s assets. The Bank must also have policies and procedures to assess financial subsidiary risk and protect the Bank from such risks and potential liabilities and would be subject to the same capital deduction, risk management and affiliate transaction rules as are applicable to national banks. Generally, a financial subsidiary is permitted to engage in activities that are financial in nature or incidental thereto, even though they are not permissible for the national bank to conduct directly within the bank. The definition of financial in nature includes, among other items, underwriting, dealing in or making a market in securities, including, for example, distributing shares of mutual funds. The subsidiary may not, however, under present law, engage as principal in underwriting insurance (other than credit life insurance), issue annuities or engage in real estate brokerage or development or in merchant banking activities. Presently, none of the Bank s subsidiaries are financial subsidiaries.

Federal Home Loan Bank System

The Bank is a member of the Federal Home Loan Bank of San Francisco (the FHLB). Among other benefits, each FHLB serves as a reserve or central bank for its members within its assigned region. Each FHLB is financed primarily from the sale of consolidated obligations of the FHLB system. Each FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the Board of Directors of the individual FHLB. As an FHLB member, the Bank is required to own a certain amount of capital stock in the FHLB. At December 31, 2006, the Bank was in compliance with the FHLB s stock ownership requirement and our investment in FHLB capital stock totaled $77.5 million.

Federal Reserve System

FRBThe Federal Reserve Board requires all depository institutions to maintain non-interest bearing reserves at specified levels against their transaction accounts (primarily checking and non-personal time deposits). At December 31, 2006, the Bank was in compliance with these requirements. As a member bank, the Bank is also required to own capital stock in the Federal Reserve Bank of San Francisco (the Reserve Bank). At December 31, 2006, the Bank held an investment of $17.8 million in Reserve Bank capital stock.

Interstate Banking and Branching

Subject to certain size limitations under the Riegle-Neal Interstate Banking Act, bank holding companies and banks have the ability to acquire or merge with banks in other states; and, subject to certain state restrictions, banks may also acquire or establish new branches outside their home states. Interstate branches are subject to certain laws of the states in which they are located. The Bank presently has one interstate branch in Houston, Texas.

Securities Registration

The Company s securities are registered with the SEC under the Exchange Act of 1934, as amended. As such, the Company is subject to the information, proxy solicitation, insider trading, corporate governance, and other requirements and restrictions of the Exchange Act.

Foreign Operations

The Bank has a branch in Hong Kong and a representative office in Beijing, China, and has received approval to open another representative office in Shanghai, China.

The Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002 addresses accounting oversight and corporate governance matters and, among other things:

- required executive certification of financial presentations;
- increased requirements for board audit committees and their members;
- enhanced disclosure of controls and procedures and internal control over financial reporting;
- enhanced controls on, and reporting of, insider trading; and
- increased penalties for financial crimes and forfeiture of executive bonuses in certain circumstances.

This legislation and its implementing regulations resulted in increased costs of compliance, including certain outside professional costs. To date, these costs have not had a material impact on our operations.

Dividends and Other Transfers of Funds

Dividends from the Bank constitute the principal source of income to the Company. An FRB policy statement provides that a bank holding company should pay cash dividends only to the extent that the holding company s net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the holding company s capital needs, asset quality and overall financial condition. The policy statement also provides that it would be inappropriate for a company experiencing serious financial problems to borrow funds to pay dividends. Furthermore, under the federal prompt corrective action regulations, the FRB may prohibit a bank holding company from paying any dividends if the holding company s bank subsidiary is classified as undercapitalized. See Capital Standards .

The Bank is subject to various statutory and regulatory restrictions on its ability to pay dividends. Under such restrictions, the amount available for payment of dividends to the Company by the Bank totaled $315.6 million at December 31, 2006. In addition, the banking agencies have the authority to prohibit the Bank from paying dividends, depending upon the Bank s financial condition, if such payment is deemed to constitute an unsafe or unsound practice.

Capital Standards

The federal banking agencies have adopted risk-based minimum capital guidelines for bank holding companies and banks which are intended to provide a measure of capital that reflects the degree of risk associated with a banking organization s operations for both transactions reported on the balance sheet as assets and transactions which are recorded as off-balance sheet items.

The risk-based capital ratio is determined by classifying assets and certain off-balance sheet financial instruments into weighted categories, with higher levels of capital being required for those categories perceived as representing greater risk. Under the capital guidelines, a banking organization s total capital is divided into tiers. Tier I capital consists of (1) common equity, (2) qualifying noncumulative perpetual preferred stock, (3) a limited amount of qualifying cumulative perpetual preferred stock and (4) minority interests in the equity accounts of consolidated subsidiaries (including trust-preferred securities), less goodwill and certain other intangible assets. Qualifying Tier I capital may consist of trust-preferred securities, subject to certain criteria and quantitative limits for inclusion of restricted core capital elements in Tier I capital. Tier II capital consists of hybrid capital instruments, perpetual debt, mandatory convertible debt securities, a limited amount of subordinated debt, preferred stock and trust-preferred securities that do not qualify as Tier I capital, a limited amount of the allowance for loan and lease losses and a limited amount of unrealized holding gains on equity securities. Tier III capital consists of qualifying unsecured subordinated debt. The sum of Tier II and Tier III capital may not exceed the amount of Tier I capital.

The risk-based capital guidelines require a minimum ratio of qualifying total capital to risk-adjusted assets of 8% and a minimum ratio of Tier I capital to risk-adjusted assets of 4%. In addition to the risk-based guidelines, the federal bank regulatory agencies require banking organizations to maintain a minimum amount of Tier I capital to total assets, referred to as the leverage ratio. For a banking organization rated well-capitalized, the minimum leverage ratio of Tier I capital to total assets must be 3%.

An institution s risk-based capital, leverage capital and tangible capital ratios together determine the institution s capital classification. An institution is treated as well capitalized if its total capital to risk-weighted assets ratio is 10.00% or more; its core capital to risk-weighted assets ratio is 6.00% or more; and its core capital to adjusted total assets ratio is 5.00% or more. At December 31, 2006, the Company s and the Bank s capital ratios exceed these minimum percentage requirements for well capitalized institutions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Capital for further information regarding the regulatory capital guidelines as well as the Company s and the Bank s actual capitalization as of December 31, 2006.

The current risk-based capital guidelines are based upon the 1988 capital accord of the International Basel Committee on Banking Supervision. A new international accord, referred to as Basel II, which emphasizes internal assessment of credit, market and operational risk; supervisory assessment and market discipline in determining minimum capital requirements, currently becomes mandatory for large international banks outside the U.S. in 2008. In October 2006, the U.S. federal banking agencies issued a notice of proposed rulemaking for comment to implement Basel II for U.S. banks with certain differences from the international Basel II framework and which would not be fully in effect for U.S. banks until 2012. Further, the U.S. banking agencies propose to retain the minimum leverage requirement and prompt corrective action regulatory standards. In December 2006, the federal banking agencies issued another notice of proposed rulemaking for comment, referred to as Basel IA, that proposed alternative capital requirements for smaller U.S. banks which may be negatively impacted competitively by certain provisions of Basel II. Additional guidance on Basel II issued in February 2007 stated the agencies expectation that to determine the extent to which banks should hold capital in excess of regulatory minimum levels, examiners would look at the combined implications of a bank s compliance with qualification requirements for regulatory risk-based capital standards, the quality and results of the bank s internal capital adequacy assessment process, and the examiners assessment of the bank s risk profile and capital position. At this time the impact that proposed changes in capital requirements may have on the cost and availability of different types of credit and the potential compliance cost to us of implementing Basel II or Basel IA, as applicable, are uncertain.

The federal banking agencies possess broad powers under the Federal Deposit Insurance Act (FDI Act) to take prompt corrective action to resolve the problems of insured depository institutions that fall within any undercapitalized category. In addition, the federal banking agencies have adopted non-capital safety and soundness standards to assist examiners in identifying and addressing potential safety and soundness concerns before capital becomes impaired. The guidelines set forth operational and managerial standards relating to: (i) internal controls, information systems and internal audit systems, (ii) loan documentation, (iii) credit underwriting, (iv) asset quality and growth, (v) earnings, (vi) risk management, and (vii) compensation and benefits.

Premiums for Deposit Insurance

Through the DIF, the FDIC insures our customer deposits up to prescribed limits for each depositor. The amount of FDIC assessments paid by each DIF member institution is based on its relative risk of default as measured by regulatory capital ratios and other supervisory factors. The assessment rate currently ranges from zero to 27 cents per $100 of domestic deposits. The FDIC may increase or decrease the assessment rate schedule on a semi-annual basis. The Federal Deposit Insurance Reform Act of 2006, or FDIRA, provides, among other things, for changes in the formula and factors to be considered by the FDIC in calculating the FDIC reserve ratio, assessments and dividends, and a one-time aggregate assessment credit for depository institutions in existence on December 31, 1996 (or their successors) which paid assessments to recapitalize the insurance funds after the banking crises of the late 1980s and early 1990s. The FDIC issued final regulations, effective January 1, 2007, implementing the provisions of FDIRA, and in February 2007 issued for comment guidelines, including business line concentrations and

risk of failure and severity of loss in the event of failure, to be used by the FDIC for possibly raising premiums by up to 0.50 basis points for large banks with $10 billion or more in assets. The Bank expects to receive a one-time assessment credit that is expected to exceed any increase in assessments by the FDIC in 2007.

All FDIC-insured depository institutions must also pay an annual assessment to provide funds for the payment of interest on bonds issued by the Financing Corporation, a federal corporation chartered under the authority of the Federal Housing Finance Board. The bonds, commonly referred to as FICO bonds, were issued to capitalize the Federal Savings and Loan Insurance Corporation. The FICO assessment rate for the fourth quarter of fiscal 2006 was 1.24 basis points for each $100 of assessable deposits. The FICO assessments are adjusted quarterly to reflect changes in the assessment bases of the FDIC s insurance funds and do not vary depending on a depository institution s capitalization or supervisory evaluations.

The FDIC may terminate a depository institution s deposit insurance upon a finding that the institution s financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices that pose a risk to the DIF or that may prejudice the interest of the bank s depositors. The termination of deposit insurance for the Bank would also result in the revocation of the Bank s charter by the DFI.

Loans-to-One Borrower Limitations

With certain limited exceptions, the maximum amount of obligations, secured or unsecured, that any borrower (including certain related entities) may owe to a California state bank at any one time may not exceed 25% of the sum of the shareholders equity, allowance for loan losses, capital notes and debentures of the bank. Unsecured obligations may not exceed 15% of the sum of the shareholders equity, allowance for loan losses, capital notes and debentures of the bank. The Bank has established internal loan limits which are lower than the legal lending limits for a California bank.

Extensions of Credit to Insiders and Transactions with Affiliates

The Federal Reserve Act and FRB Regulation O place limitations and conditions on loans or extensions of credit to:

- a bank s or bank holding company s executive officers, directors and principal shareholders (i.e., in most cases, those persons who own, control or have power to vote more than 10% of any class of voting securities);
- any company controlled by any such executive officer, director or shareholder; or
- any political or campaign committee controlled by such executive officer, director or principal shareholder.

Loans and leases extended to any of the above persons must comply with loan-to-one-borrower limits, require prior full board approval when aggregate extensions of credit to the person exceed specified amounts, must be made on substantially the same terms (including interest rates and collateral) as, and follow credit-underwriting procedures that are not less stringent than those prevailing at the time for comparable transactions with non-insiders, and must not involve more than the normal risk of repayment or present other unfavorable features. In addition, Regulation O provides that the aggregate limit on extensions of credit to all insiders of a bank as a group cannot exceed the bank s unimpaired capital and unimpaired surplus. Regulation O also prohibits a bank from paying an overdraft on an account of an executive officer or director, except pursuant to a written pre-authorized interest-bearing extension of credit plan that specifies a method of repayment or a written pre-authorized transfer of funds from another account of the officer or director at the Bank. California has laws and the DFI has regulations which adopt and also apply Regulation O to the Bank.

The Bank also is subject to certain restrictions imposed by Federal Reserve Act Sections 23A and 23B and FRB Regulation W on any extensions of credit to, or the issuance of a guarantee or letter of credit on behalf of, any affiliates, the purchase of, or investments in, stock or other securities thereof, the taking of such securities as collateral for loans, and the purchase of assets of any affiliates. Such restrictions prevent any affiliates from borrowing from the Bank unless the loans are secured by marketable obligations of designated amounts. Further, such secured loans and investments to or in any affiliate are limited, individually, to 10.0% of the Bank s capital and surplus (as defined by federal regulations), and such secured loans and investments are limited, in the aggregate, to 20.0% of the Bank s capital and surplus. Some of the entities included in the definition of an affiliate are parent companies, sister banks, sponsored and advised companies, investment companies whereby the Bank s affiliate serves as investment advisor, and financial subsidiaries. Additional restrictions on transactions with affiliates may be imposed on the Bank under the FDI Act prompt corrective action provisions and the supervisory authority of the federal and state banking agencies.

USA PATRIOT Act

The USA PATRIOT Act of 2001 and its implementing regulations significantly expanded the anti-money laundering and financial transparency laws. Under the USA PATRIOT Act, financial institutions are required to establish and maintain anti-money laundering programs which include:

- the establishment of a customer identification program;
- the development of internal policies, procedures, and controls;
- the designation of a compliance officer;
- an ongoing employee training program; and
- an independent audit function to test the programs.

The Bank has adopted comprehensive policies and procedures to address the requirements of the USA PATRIOT Act. Material deficiencies in anti-money laundering compliance can result in public enforcement actions by the banking agencies, including the imposition of civil money penalties and supervisory restrictions on growth and expansion. Such enforcement actions could also have serious reputation consequences for the Company and the Bank.

Consumer Laws

Examination and enforcement by the state and federal banking agencies for non-compliance with consumer protection laws and their implementing regulations have become more intense. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below. The Bank and the Company are also subject to federal and state laws prohibiting unfair or fraudulent business practices, untrue or misleading advertising and unfair competition.

The Home Ownership and Equity Protection Act of 1994, or HOEPA, requires extra disclosures and consumer protections to borrowers for certain lending practices. The term predatory lending, much like the terms safety and soundness and unfair and deceptive practices, is far-reaching and covers a potentially broad range of behavior. As such, it does not lend itself to a concise or a comprehensive definition. Typically, however, predatory lending involves at least one, and perhaps all three, of the following elements:

- making unaffordable loans based on the assets of the borrower rather than on the borrower s ability to repay an obligation (asset-based lending);

- inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced (loan flipping); and/or

- engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

Regulations and banking agency guidelines aimed at curbing predatory lending significantly widen the pool of high-cost home-secured loans covered by HOEPA. In addition, the regulations bar certain refinances within a year with another loan subject to HOEPA by the same lender or loan servicer. Lenders also will be presumed to have violated the law which says loans should not be made to people unable to repay them unless they document that the borrower has the ability to repay. Lenders that violate the rules face cancellation of loans and penalties equal to the finance charges paid. The Bank does not expect these rules and potential state action in this area to have a material impact on our financial condition or results of operations.

Privacy policies are required by federal banking regulations which limit the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. Pursuant to those rules, financial institutions must provide:

- initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates;

- annual notices of their privacy policies to current customers; and

- a reasonable method for customers to opt out of disclosures to nonaffiliated third parties.

These privacy protections affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. In addition, state laws may impose more restrictive limitations on the ability of financial institutions to disclose such information. California has adopted such a privacy law that, among other things, generally provides that customers must opt in before information may be disclosed to certain nonaffiliated third parties.

The Fair Credit Reporting Act, as amended by the Fair and Accurate Credit Transactions Act, or the FACT Act, requires financial firms to help deter identity theft, including developing appropriate fraud response programs, and gives consumers more control of their credit data. It also reauthorizes a federal ban on state laws that interfere with corporate credit granting and marketing practices. In connection with FACT Act, the federal financial institution regulatory agencies proposed rules that would prohibit an institution from using certain information about a consumer it received from an affiliate to make a solicitation to the consumer, unless the consumer has been notified and given a chance to opt out of such solicitations. A consumer s election to opt out would be applicable for at least five years. The agencies have also proposed guidelines required by the FACT Act for financial institutions and creditors which require financial institutions to identify patterns, practices and specific forms of activity, known as Red Flags, that indicate the possible existence of identity theft and require financial institutions to establish reasonable policies and procedures for implementing these guidelines.

The Check Clearing for the 21st Century Act, or Check 21, facilitates check truncation and electronic check exchange by authorizing a new negotiable instrument called a substitute check, which is the legal equivalent of an original check. Check 21 does not require banks to create substitute checks or accept checks electronically; however, it does require banks to accept a legally equivalent substitute check in place of an original. In addition to its issuance of regulations governing substitute checks, the Federal Reserve has issued final rules governing the treatment of remotely created checks (sometimes referred to as demand drafts) and electronic check conversion transactions (involving checks that are converted to electronic transactions by merchants and other payees).

The Equal Credit Opportunity Act, or ECOA, generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act, or TILA, is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act, or FH Act, regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Community Reinvestment Act, or CRA, is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank s record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution s record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of outstanding to a low of substantial noncompliance. In its last examination for CRA compliance, as of May 15, 2006, the Bank was rated satisfactory.

The Home Mortgage Disclosure Act, or HMDA, grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a fair lending aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes. The Federal Reserve Board amended regulations issued under HMDA to require the reporting of certain pricing data with respect to higher priced mortgage loans for review by the federal banking agencies from a fair lending perspective. We do not expect the HMDA data reported by the Bank to raise material issues regarding its compliance with the fair lending laws.

The Real Estate Settlement Procedures Act, or RESPA, requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties.

The National Flood Insurance Act, or NFIA, requires homes in flood-prone areas with mortgages from a federally regulated lender to have flood insurance. Hurricane Katrina focused awareness on this requirement. Lenders are required to provide notice to borrowers of special flood hazard areas and require such coverage before making, increasing, extending or renewing such loans. Financial institutions which demonstrate a pattern and practice of lax compliance are subject to the issuance of cease and desist

orders and the imposition of per loan civil money penalties, up to a maximum fine which currently is $125,000. Fine payments are remitted to the Federal Emergency Management Agency for deposit into the National Flood Mitigation Fund.

Due to heightened regulatory concern related to compliance with HOEPA, privacy laws and regulations, FACT, Check 21, ECOA, TILA, FH Act, CRA, HMDA, RESPA, and NFIA generally, the Bank may incur additional compliance costs or be required to expend additional funds for CRA investments.

Regulation of Nonbank Subsidiaries

Nonbank subsidiaries are subject to additional or separate regulation and supervision by other state, federal and self-regulatory bodies. East West Insurance Services, Inc. is subject to the licensing and supervisory authority of the California Commissioner of Insurance.

Employees

East West does not have any employees other than officers who are also officers of the Bank. Such employees are not separately compensated for their employment with the Company. As of December 31, 2006, the Bank had a total of 1,243 full-time employees and 55 part-time employees and the Agency had a total of 14 full-time employees. None of the employees are represented by a union or collective bargaining group. The managements of the Bank and Agency believe that their employee relations are satisfactory.

Available Information

The Company also maintains an internet website at *www.eastwestbank.com*. The Company makes its website content available for information purposes only. It should not be relied upon for investment purposes.

We make available free of charge through our website our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and proxy statements for its annual shareholder meetings, as well as any amendments to those reports, as soon as reasonably practicable after the Company files such reports with the Securities and Exchange Commission. The Company s SEC reports can be accessed through the investor information page of its website. None of the information contained in or hyperlinked from our website is incorporated into this Form 10-K. The SEC also maintains a website at *www.sec.gov* that contains reports, proxy statements and other information regarding SEC registrants, including the Company.

Executive Officers of the Registrant

The following table sets forth the executive officers of the Company, their positions, and their ages. Each officer is appointed by the Board of Directors of the Company or the Bank and serves at their pleasure.

Name	Age (1)	Position with Company or Bank
Dominic Ng	48	Chairman of the Board, President, and Chief Executive Officer of the Company and the Bank
Wellington Chen	47	Executive Vice President and Director of Corporate Banking Division of the Bank

K.Y. Cheng	54	Executive Vice President and Director of International Trade Banking
Donald S. Chow	56	Executive Vice President and Director of Commercial Lending of the Bank
Robert L. Dingle, Jr.	55	Executive Vice President and Chief Information Officer of the Bank
Richard Ercole	64	Executive Vice President and Director of Treasury Management Services of the Bank
William H. Fong	59	Executive Vice President and Head of Northern California Commercial Lending of the Bank
Agatha Fung	47	Executive Vice President and Head of International Banking of the Bank
Julia S. Gouw	47	Executive Vice President and Chief Financial Officer of the Company and the Bank
Douglas P. Krause	50	Executive Vice President, General Counsel, and Secretary of the Company and the Bank
Michael W. Lai	56	Executive Vice President and Director of Retail Operations of the Bank
Kelvin Lee	50	Managing Director, Community Banking Division, of the Bank
William J. Lewis	63	Executive Vice President and Chief Credit Officer of the Bank
Steven D. Munter	50	Executive Vice President and Director of Commercial Banking of the Bank
David L. Spigner	46	Executive Vice President and Chief Strategic Officer of the Bank
Andy Yen	49	Executive Vice President and Director of Business Banking of the Bank

(1) As of February 28, 2007

Dominic Ng serves as Chairman, President and Chief Executive Officer of East West Bancorp, Inc. and East West Bank. Prior to taking the helm of East West in 1992, Mr. Ng was President and Chief Executive Officer of Seyen Investment, Inc. and before that spent over a decade as a CPA with Deloitte & Touche LLP. Mr. Ng serves on the Boards of Directors of the Federal Reserve Bank of San Francisco, Los Angeles Branch and Mattel, Inc.

Wellington Chen serves as Executive Vice President and Director of Corporate Banking Division. Prior to joining East West in 2003, Mr. Chen was Senior Executive Vice President of Far East National Bank (Far East), heading up their Commercial Banking and Consumer Banking groups. He also served on

the Board of Directors of Far East. Mr. Chen s career with Far East started in 1986 and included a variety of branch and credit management positions. Prior to that, Mr. Chen spent three years with Security Pacific National Bank where he began his banking career as an asset-based lending auditor. Mr. Chen serves on the Board of Directors of the Pasadena Tournament of Roses Foundation.

K. Y. Cheng serves as Executive Vice President and Director of International Trade Banking. Prior to joining the Bank in 1999, Mr. Cheng was the general manager of the Pacific Rim Business Division at Union Bank of California. Mr. Cheng has over 25 years of experience in banking and has focused his career on international, corporate and correspondent banking. He has also held positions at Wells Fargo Bank, First Interstate Bank and Mitsui Manufacturing Bank. He serves as Vice Chairman of the Board of the International Bankers Association of California and as Executive Director of the Los Angeles Economic Development Corporation. Mr. Cheng is also a member of the Pacific Council on International Policy and has been nominated to be the Pacific Rim Committee Chair of the Los Angeles Chamber of Commerce.

Donald S. Chow serves as Executive Vice President and Director of Commercial Lending. Mr. Chow has over 30 years of experience in commercial lending. Before joining East West in 1993, Mr. Chow was First Vice President and Senior Credit Officer for Mitsui Manufacturers Bank from 1987 to 1993, and prior to that spent over 14 years with Security Pacific National Bank where he held a number of management positions in the commercial lending area.

Robert L. Dingle, Jr. serves as Executive Vice President and Chief Information Officer. Prior to joining East West in November 2005, Mr. Dingle held CIO positions at IndyMac Bank, Resource Bancshares, First Union and Directors Mortgage. He also worked with Booz, Allen & Hamilton and Southwest Bancshares. Mr. Dingle has over 25 years of experience in the financial services industry.

Richard Ercole serves as Executive Vice President and Director of Treasury Management Services. Mr. Ercole heads the development of the Bank s cash management products and services. Prior to joining East West in April 2006, Mr. Ercole led Bank of America s Los Angeles treasury management sales team. His 30-year banking career also includes experience in product management and development with Union Bank and senior positions with Security Pacific National Bank and Huntington Bancshares.

William H. Fong serves as Executive Vice President and Head of the Bank s Northern California Commercial Lending division. Mr. Fong joined East West in April 2006 from United Commercial Bank where he was the Head of Commercial Banking. Prior to this, Mr. Fong spent 23 years with the BNP Paribas/Bank of the West group. His responsibilities as an Executive Vice President with Bank of the West included the oversight of the Pacific Rim Division s Corporate Banking department as well as the strategic planning and development of the division s branch network in Portland, California, Nevada, and representative offices in Taiwan and Shanghai. Before transferring to Bank of the West, Mr. Fong spent 20 years with BNP Paribas as Director of the Asia Desk.

Agatha Fung serves as Executive Vice President and Head of International Banking of East West Bank. In October 2005, Ms. Fung joined East West from CITIC International Financial Holdings in Hong Kong where she held positions as Head of Business Banking of CITIC Ka Wah Bank and Chief Executive Officer and Executive Director of HKCB Finance. Ms. Fung has over 20 years of banking experience and has also held senior management positions at Standard Chartered Bank and Citibank in both Hong Kong and Tokyo.

Julia S. Gouw serves as Executive Vice President and Chief Financial Officer of East West Bancorp, Inc. and East West Bank. Prior to joining East West in 1989, Ms. Gouw spent over five years as a

CPA with KPMG LLP. She was ranked among the top ten bank CFOs in the nation by *U.S. Banker* in January 2006. She serves on the Board of Visitors of the UCLA School of Medicine and is the founding chair of the Executive Advisory Board of the Iris Cantor-UCLA Women s Health Center. Ms. Gouw is also on the Board of Directors of Huntington Memorial Hospital.

Douglas P. Krause serves as Executive Vice President, General Counsel and Corporate Secretary of East West Bancorp, Inc. and East West Bank. Prior to joining East West in 1996, Mr. Krause was Corporate Senior Vice President and General Counsel of Metrobank from 1991 to 1996. Prior to that, Mr. Krause was with the law firms of Dewey Ballantine, and Jones, Day, Reavis and Pogue where he specialized in financial services. Mr. Krause also serves on the governing boards of the Port of Los Angeles and of the Alameda Corridor Transportation Authority; he is the chairman of the Audit Committees of both Commissions.

Michael W. Lai serves as Executive Vice President and Director of the Bank s Retail Operations. Mr. Lai has over 25 years of experience in banking and has held a number of senior management positions. Before joining East West in 2000, Mr. Lai managed several private investments and provided consulting services to various financial institutions related to business organization and financing issues. Prior to that, Mr. Lai served as President, Chief Executive Officer and Director of United Savings Bank from 1994 to 1996, and as Senior Vice President, Chief Credit Officer and Director from 1991 to 1994. Mr. Lai has also worked in various management capacities for financial institutions located in New York and Hong Kong.

Kelvin Lee serves as Managing Director, heading the Bank s Community Banking Division. Prior to joining East West in 2000, Mr. Lee was the Deputy Director, Global Strategic Alliance Group, of Deloitte & Touche LLP. Mr. Lee started his banking career with Sumitomo Bank of California in 1980 and later joined Sanwa Bank of California in 1986, where he established its Pacific Rim Banking unit. Mr. Lee serves on the advisory Board of the Asia Society Southern California Center and on the Board of Governors of the Little Tokyo Service Center. He was also past President of the Asian Business League of Southern California and the Asian Youth Center.

William J. Lewis serves as Executive Vice President and Chief Credit Officer. Mr. Lewis joined the Bank in 2002 with over 35 years of banking experience, during which time he has held a number of senior management positions. He was Executive Vice President and Chief Credit Officer of PriVest Bank from 1998 to 2002 and held the same positions with Eldorado Bank from 1994 to 1998. Prior to this, Mr. Lewis was with Sanwa Bank for over 12 years where he administered a 35 branch region. Before that, Mr. Lewis spent 13 years with First Interstate Bank where he held a variety of branch and credit management positions.

Steven D. Munter serves as Executive Vice President and Director of Commercial Lending. Prior to joining East West in November 2006, Mr. Munter spent over 25 years with Bank of America where he held a number of senior management positions, most recently as the Commercial Banking National Credit Products Executive for Government, Healthcare and Institutions. His long standing global career with Bank of America has also included assignments in Central and South America and, for five years in Asia, where he held senior positions with Banc America Securities, Japan.

David L. Spigner serves as Executive Vice President and Chief Strategic Officer. Prior to joining East West in April 2004, Mr. Spigner served as Managing Principal of Strategic Business Management, a management consulting practice of which the Bank was a client. His career includes eight years in management consulting, five of which he worked for Deloitte & Touche LLP. He served as President and Chief Executive Officer of Lil Tots, LLC for five years and, prior to that, spent three years as President of Seyen Trading Inc.

Andy Yen serves as Executive Vice President and Director of Business Banking Division. Mr. Yen joined the Bank in September 2005 through its merger with United National Bank. Before being promoted to President of UNB in 2001, Mr. Yen was the Executive Vice President from 1998 to 2000; and Senior Vice President from 1992 to 1997, overseeing both the operations and lending functions of UNB. Mr. Yen also served as a member of the Board of Directors of UNB from 1992 to 2005. Mr. Yen has over 20 years experience in commercial and real estate lending and also held positions at Tokai Bank of California and Trans National Bank before he joined UNB.

ITEM 1A. RISK FACTORS

Risk Factors That May Affect Future Results

In addition to the other information on the risks we face and our management of risk contained in this annual report or in our other SEC filings, the following are significant risks which may affect us. Events or circumstances arising from one or more of these risks could adversely affect our business, financial condition, operating results and prospects and the value and price of our common stock could decline. The risks identified below are not intended to be a comprehensive list of all risks we face and additional risks that we may currently view as not material may also impair our business operations and results.

Changes in economic conditions could materially hurt our business. *Our business is directly affected by changes in economic conditions, including finance, legislative and regulatory changes and changes in government monetary and fiscal policies and inflation, all of which are beyond our control. Deterioration in economic conditions could result in the following consequences:*

- problem assets and foreclosures may increase;
- demand for our products and services may decline;
- low cost or non-interest bearing deposits may decrease; and
- collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers borrowing power, and reducing the value of assets and collateral associated with our existing loans.

In view of the concentration of our operations and the collateral securing our loan portfolio in Northern and Southern California, we may be particularly susceptible to the adverse economic conditions in the state of California where our business is concentrated.

Our business is subject to interest rate risk and variations in interest rates may negatively affect our financial performance. *A substantial portion of our income is derived from the differential or spread between the interest earned on loans, investment securities and other interest-earning assets, and the interest paid on deposits, borrowings and other interest-bearing liabilities. Because of the differences in the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities, changes in interest rates do not produce equivalent changes in interest income earned on interest-earning assets and interest paid on interest-bearing liabilities. Significant fluctuations in market interest rates could*

materially and adversely affect not only our net interest spread, but also our asset quality and loan origination volume.

We are subject to extensive government regulation that could limit or restrict our activities, which, in turn, may hamper our ability to increase our assets and earnings. Our operations are subject to extensive regulation by federal, state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Because our business is highly regulated, the laws, rules, regulations and supervisory guidance and policies applicable to us are subject to regular modification and change. Perennially various laws, rules and regulations are proposed, which, if adopted, could impact our operations by making compliance much more difficult or expensive, restricting our ability to originate or sell loans or further restricting the amount of interest or other charges or fees earned on loans or other products.

Failure to manage our growth may adversely affect our performance. Our financial performance and profitability depend on our ability to manage our recent and possible future growth. Future acquisitions and our continued growth may present operating, integration and other issues that could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We face strong competition from financial services companies and other companies that offer banking services. We conduct most of our operations in California. The banking and financial services businesses in California are highly competitive and increased competition in our primary market area may adversely impact the level of our loans and deposits. Ultimately, we may not be able to compete successfully against current and future competitors. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including savings and loan associations, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. In particular, our competitors include major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous locations and mount extensive promotional and advertising campaigns. Areas of competition include interest rates for loans and deposits, efforts to obtain loan and deposit customers and a range in quality of products and services provided, including new technology-driven products and services. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits.

Our loan portfolio is predominantly secured by real estate and thus we have a higher degree of risk from a downturn in our real estate markets. A downturn in our real estate markets could hurt our business because many of our loans are secured by real estate. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other governmental statutes, regulations and policies and acts of nature, such as earthquakes and national disasters particular to California. If real estate prices decline, particularly in California, the value of real estate collateral securing our loans could be significantly reduced. Our ability to recover on defaulted loans by foreclosing and selling the real estate collateral would then be diminished and we would be more likely to suffer losses on defaulted loans. A large majority of our loans is collateralized by various types of real estate. Substantially all of our real estate collateral is located in California. If there is a significant decline in real estate values, especially in California, the collateral for our loans will provide less security.

If a significant number of borrowers, guarantors and related parties fail to perform as required by the terms of their loans, we will sustain losses. A significant source of risk arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. We have adopted underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, which we believe are

appropriate to minimize this risk by assessing the likelihood of nonperformance, tracking loan performance, and diversifying our loan portfolio. These policies and procedures, however, may not prevent unexpected losses that could have a material adverse effect on our results of operations.

If we cannot attract deposits, our growth may be inhibited. Our ability to increase our asset base depends in large part on our ability to attract additional deposits at favorable rates. We seek additional deposits by offering deposit products that are competitive with those offered by other financial institutions in our markets. We cannot assure you that these efforts will be successful.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company currently neither owns nor leases any real or personal property. The Company uses the premises, equipment, and furniture of the Bank. The Agency also currently conducts its operations in one of the administrative offices of the Bank. The Company is currently reimbursing the Bank for the Agency s use of this facility.

The Bank owns the buildings and land at 12 of its retail branch offices. Three of these retail branch locations are either attached or adjacent to offices that are being used by the Bank to house various administrative departments. All other branch and administrative locations are leased by the Bank, with lease expiration dates ranging from 2007 to 2020, exclusive of renewal options.

Due to the Bank s continuing growth and expansion, we entered into several new leases during 2006 related primarily to new branch locations, including the Hong Kong branch, as well as additional administrative locations. The Company believes that its existing facilities are adequate for its present purposes. The Company believes that, if necessary, it could secure alternative facilities on similar terms without adversely affecting its operations.

At December 31, 2006, the Bank s consolidated investment in premises and equipment, net of accumulated depreciation and amortization, totaled $43.9 million. Total occupancy expense, inclusive of rental payments and furniture and equipment expense, for the year ended December 31, 2006, was $21.4 million. Total annual rental expense (exclusive of operating charges and real property taxes) was approximately $9.2 million during 2006.

ITEM 3. LEGAL PROCEEDINGS

Neither the Company nor the Bank is involved in any material legal proceedings. The Bank, from time to time, is party to litigation which arises in the ordinary course of business, such as claims to enforce liens, claims involving the origination and servicing of loans, and other issues related to the business of the Bank. After taking into consideration information furnished by counsel to the Company and the Bank, management believes that the resolution of such issues would not have a material adverse impact on the financial position, results of operations, or liquidity of the Company or the Bank.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

There were no matters submitted to a vote of security holders during the fourth quarter of the year ended December 31, 2006.

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

East West Bancorp, Inc. commenced trading on the NASDAQ National Market on February 8, 1999 under the symbol EWBC. The following table sets forth the range of sales prices for the Company s common stock for the years ended December 31, 2006 and 2005.

	2006		**2005**	
	High	**Low**	**High**	**Low**
First quarter	$ 39.59	34.83	$ 42.29	$ 34.86
Second quarter	41.75	36.56	37.29	30.68
Third quarter	41.20	36.71	38.43	32.09
Fourth quarter	39.77	34.29	38.88	31.57

The foregoing reflects information available to the Company and does not necessarily include all trades in the Company s stock during the periods indicated. The closing price of our common stock on January 31, 2007 was $38.40 per share, as reported by the Nasdaq National Market.

Issuance of Common Stock

On March 17, 2006, we issued 3,647,440 shares of common stock at a price of $36.70 in conjunction with the acquisition of Standard Bank. The stock was issued without registration under the Securities Act pursuant to a fairness hearing conducted in compliance with Section 3(a)(10) of the Securities Act.

Holders

As of January 31, 2007, 61,511,243 shares of the Company s common stock were held by 1,739 shareholders of record.

Dividends

We declared and paid cash dividends of $0.05 per share during each of the four quarters of 2006 and 2005. On January 24, 2007, the Company s Board of Directors announced a 100% quarterly dividend increase to $0.10 per share beginning in the first quarter of 2007. Refer to Item 1. BUSINESS Supervision and Regulation Dividends and Other Transfer of Funds for information regarding dividend payment restrictions.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table provides information as of December 31, 2006 regarding equity compensation plans under which equity securities of the Company were authorized for issuance.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in Column (a) (c)
Equity compensation plans approved by security holders	2,728,171	$ 17.81	3,835,804
Equity compensation plans not approved by security holders	-	-	-
Total	2,728,171	$ 17.81	3,835,804

Stock Performance Graph

The following graph shows a comparison of stockholder return on the Company s common stock based on the market price of the common stock assuming the reinvestment of dividends, with the cumulative total returns for the companies in the SNL Western Bank Index for the 5-year period beginning on December 31, 2001 through December 31, 2006. This graph is historical only and may not be indicative of possible future performance of the common stock.

Total Return Performance

	Period Ending					
Index	**12/31/01**	**12/31/02**	**12/31/03**	**12/31/04**	**12/31/05**	**12/31/06**
East West Bancorp, Inc.	100.00	141.30	212.38	334.22	292.29	285.23
SNL Western Bank Index	100.00	109.41	148.21	168.43	175.36	197.86

Source: SNL Financial LC, Charlottesville, VA, (434) 977-1600, www.snl.com

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

On January 23, 2007, the Company s Board of Directors authorized a new stock repurchase program to buy back up to $30.0 million of the Company s common stock.

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with the Company s consolidated financial statements and the accompanying notes presented elsewhere herein.

	2006	2005	2004	2003	2002
	(In thousands, except per share data)				
Summary of Operations:					
Interest and dividend income	$ 660,050	$ 411,399	$ 252,070	$ 178,543	$ 167,288
Interest expense	292,568	131,284	52,897	35,232	48,979
Net interest income	367,482	280,115	199,173	143,311	118,309
Provision for loan losses	6,166	15,870	16,750	8,800	10,200
Net interest income after provision for loan losses	361,316	264,245	182,423	134,511	108,109
Noninterest income	34,358	29,649	30,371	31,081	23,364
Noninterest expense	161,893	123,533	91,461	75,932	62,657
Income before provision for income taxes	233,781	170,361	121,333	89,660	68,816
Provision for income taxes	90,412	61,981	43,311	30,668	20,115
Income before cumulative effect of change in accounting principle	143,369	108,380	78,022	58,992	48,701
Cumulative effect of change in accounting principle, net of tax (1)	-	-	-	-	788
Net income	$ 143,369	$ 108,380	$ 78,022	$ 58,992	$ 49,489
Basic earnings per share (2)	$ 2.40	$ 2.03	$ 1.54	$ 1.23	$ 1.05
Diluted earnings per share (2)	$ 2.35	$ 1.97	$ 1.49	$ 1.19	$ 1.00
Dividends per share (2)	$ 0.20	$ 0.20	$ 0.20	$ 0.20	$ 0.14
Average number of shares outstanding, basic (2)	59,605	53,454	50,654	48,112	47,192
Average number of shares outstanding, diluted (2)	60,909	55,034	52,297	49,486	49,260
At Year End:					
Total assets	$ 10,823,711	$ 8,278,256	$ 6,028,880	$ 4,055,433	$ 3,321,489
Loans receivable, net	8,182,172	6,724,320	5,080,454	3,234,133	2,313,199
Investment securities available-for-sale	1,647,080	869,837	534,452	445,142	531,607
Deposits	7,235,042	6,258,587	4,522,517	3,312,667	2,926,352
Federal Home Loan Bank advances	1,136,866	617,682	860,803	281,300	34,000
Stockholders equity	1,019,390	734,138	514,309	361,983	302,117
Shares outstanding (2)	61,431	56,519	52,501	48,857	47,764
Book value per share (2)	$ 16.59	$ 12.99	$ 9.80	$ 7.41	$ 6.33
Financial Ratios:					
Return on average assets	1.46 %	1.55 %	1.57 %	1.64 %	1.63 %
Return on average equity	15.78	18.27	17.86	18.12	18.29
Dividend payout ratio	8.35	9.88	12.93	16.31	12.87
Average stockholders equity to average assets	9.26	8.48	8.77	9.04	8.92
Net interest margin	3.98	4.22	4.24	4.26	4.14
Efficiency ratio (3)	37.16	36.53	35.64	38.57	39.64
Asset Quality Ratios:					
Net (recoveries) chargeoffs to average loans	(0.01)%	0.08 %	0.12 %	0.06 %	0.11 %
Nonperforming assets to year end total assets	0.18	0.36	0.10	0.16	0.37
Allowance for loan losses to year end total gross loans	0.95	1.01	0.99	1.20	1.50

(1) In 2002, this figure represents the remaining balance of negative goodwill at December 31, 2001. On January 1, 2002, the Company adopted SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 142 requires companies to cease amortizing goodwill that existed at June 30, 2001.

(2) Prior period amounts have been restated to reflect the 2 for 1 stock split on June 21, 2004.

(3) Represents noninterest expense, excluding the amortization of intangibles and investments in affordable housing partnerships, divided by the aggregate of net interest income before provision for loan losses and noninterest income.

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of East West Bancorp, Inc. and its subsidiaries. This information is intended to facilitate the understanding and assessment of significant changes and trends related to our financial condition and the results of our operations. This discussion and analysis should be read in conjunction with our consolidated financial statements and the accompanying notes presented elsewhere herein. Information related to share volume and per share amounts have been adjusted to reflect the two-for-one stock split that became effective on June 21, 2004.

Critical Accounting Policies

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and general practices within the banking industry. The financial information contained within these statements is, to a significant extent, financial information that is based on approximate measures of the financial effects of transactions and events that have already occurred. All of our significant accounting policies are described in Note 1 of our consolidated financial statements presented elsewhere herein and are essential to understanding Management s Discussion and Analysis of Financial Condition and Results of Operations. Various elements of our accounting policies, by their nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. In addition, certain accounting policies require significant judgment in applying complex accounting principles to individual transactions to determine the most appropriate treatment. We have established procedures and processes to facilitate making the judgments necessary to prepare financial statements.

The following is a summary of the more judgmental and complex accounting estimates and principles. In each area, we have identified the variables most important in the estimation process. We have used the best information available to make the estimations necessary to value the related assets and liabilities. Actual performance that differs from our estimates and future changes in the key variables could change future valuations and impact net income.

Investment Securities

The classification and accounting for investment securities are discussed in detail in Note 1 of the consolidated financial statements presented elsewhere herein. Under SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities***,** investment securities generally must be classified as held-to-maturity, available-for-sale, or trading. The appropriate classification is based partially on our ability to hold the securities to maturity and largely on management s intentions with respect to either holding or selling the securities. The classification of investment securities is significant since it directly impacts the accounting for unrealized gains and losses on securities. Unrealized gains and losses on trading securities flow directly through earnings during the periods in which they arise, whereas for available-for-sale securities, they are recorded as a separate component of stockholders equity (accumulated other comprehensive income or loss) and do not affect earnings until realized. The fair values of our investment securities are generally determined by reference to quoted market prices and reliable independent sources.

We are obligated to assess, at each reporting date, whether there is an other-than-temporary impairment to our investment securities. Such impairment must be recognized in current earnings rather than in other comprehensive income. We examine all individual securities that are in an unrealized loss position at each reporting date for other-than-temporary impairment. Specific investment level factors we

examine to assess impairment include the severity and duration of the loss, an analysis of the issuers of the securities and if there has been any cause for default on the securities and any change in the rating of the securities by the various rating agencies. Additionally, we reexamine the financial resources and overall ability the Company has and the intent management has to hold the securities until their fair values recover. Management does not believe that there are any investment securities, other than those identified in previous periods, which are deemed to be other-than-temporarily impaired as of December 31, 2006. Investment securities are discussed in more detail in Note 5 to the Company s consolidated financial statements presented elsewhere herein.

Allowance for Loan Losses

Our allowance for loan loss methodologies incorporate a variety of risk considerations, both quantitative and qualitative, in establishing an allowance for loan loss that management believes is appropriate at each reporting date. Quantitative factors include our historical loss experience, delinquency and chargeoff trends, collateral values, changes in nonperforming loans, and other factors. Quantitative factors also incorporate known information about individual loans, including borrowers sensitivity to interest rate movements and borrowers sensitivity to quantifiable external factors including commodity and finished good prices as well as acts of nature (earthquakes, floods, fires, etc.) that occur in a particular period. Qualitative factors include the general economic environment in our markets and, in particular, the state of certain industries. Size and complexity of individual credits, loan structure, extent and nature of waivers of existing loan policies and pace of portfolio growth are other qualitative factors that are considered in our methodologies.

A detailed discussion of our allowance for loan loss methodologies can be found in Management s Discussion and Analysis of Consolidated Financial Condition and Results of Operations Allowance for Loan Losses. As we add new products, increase the complexity of our loan portfolio, and expand our geographic coverage, we continue to enhance our methodologies to keep pace with the size and complexity of the loan portfolio. Changes in any of the factors cited above could have a significant impact on the loan loss calculation. We believe that our methodologies continue to be appropriate given our size and level of complexity. This discussion should also be read in conjunction with the Company s consolidated financial statements and the accompanying notes presented elsewhere herein including the section entitled Loans and Allowance for Loan Losses.

Loan Sales

We routinely sell and securitize single family and multifamily loans to secondary market investors. When mortgage loans are sold, we generally retain the right to service these loans and we may retain residual and other interests, which are considered retained interests in the sold or securitized loans. The gain on sale recorded on these loans depends, in part, on our allocation of the previous carrying amount of the loans to the retained interests. Previous carrying amounts are allocated in proportion to the relative fair values of the loans sold and the interests retained. The fair values of retained interests are estimated based upon the present value of the associated expected future cash flows taking into consideration future prepayment rates, discount rates, expected credit losses, and other factors that impact the value of the retained interests.

We may also record mortgage servicing assets, or MSA , when the benefits of servicing are expected to be more than adequate compensation to a servicer. The Company determines whether the benefits of servicing are expected to be more than adequate compensation to a servicer by discounting all of the future net cash flows associated with the contractual rights and obligations of the servicing agreement. The expected future net cash flows are discounted at a rate equal to the return that would

adequately compensate a substitute servicer for performing the servicing. In addition to the anticipated rate of loan prepayments and discount rates, other assumptions such as the cost to service the underlying loans, foreclosure costs, ancillary income and float rates are also used in determining the value of the MSAs. Mortgage servicing assets are discussed in more detail in Notes 1 and 11 to the Company s consolidated financial statements presented elsewhere herein.

Goodwill Impairment

Under SFAS No. 142, *Goodwill and Other Intangibles,* goodwill must be allocated to reporting units and tested for impairment. The Company tests goodwill for impairment at least annually or more frequently if events or circumstances, such as adverse changes in the business, indicate that there may be justification for conducting an interim test. Impairment testing is performed at the reporting-unit level (which is the same level as the Company s four major operating segments identified in Note 24 to the Company s consolidated financial statements presented elsewhere herein). The first part of the test is a comparison, at the reporting unit level, of the fair value of each reporting unit to its carrying value, including goodwill. If the fair value is less than the carrying value, then the second part of the test is needed to measure the amount of potential goodwill impairment. The implied fair value of the reporting unit goodwill is calculated and compared to the actual carrying value of goodwill recorded within the reporting unit. If the carrying value of reporting unit goodwill exceeds the implied fair value of that goodwill, then the Company would recognize an impairment loss for the amount of the difference, which would be recorded as a charge against net income. The fair values of the reporting units are determined primarily using discounted cash flow models based on each reporting unit s internal forecasts. For additional information regarding goodwill, see Note 10 to the Company s consolidated financial statements presented elsewhere herein.

Share-Based Compensation

We account for share-based awards to employees, officers, and directors in accordance with the provisions of SFAS No. 123(R), *Share-Based Payment*. Under SFAS No. 123(R), share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the employee s requisite service period. We adopted SFAS No. 123(R), as required, on January 1, 2006. Prior to 2006, we recognized stock-based compensation expense for employee share-based awards based on their intrinsic value on the date of grant pursuant to Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and followed the disclosure requirements of SFAS No. 123, *Accounting for Stock-Based Compensation*.

We adopted SFAS No. 123(R) using the modified prospective approach. Under the modified prospective approach, prior periods are not restated for comparative purposes. The valuation provisions of SFAS No. 123(R) apply to new awards and to awards that are outstanding on the effective date and subsequently modified, repurchased or cancelled. Compensation expense, net of estimated forfeitures, for awards outstanding at the effective date is recognized over the remaining service period using the compensation cost calculated for pro forma disclosures under the original SFAS No. 123.

We have granted nonqualified stock options and restricted stock. Most of our stock option and restricted stock awards include a service condition that relates only to vesting. The stock option awards generally vest in one to four years from the grant date, while the restricted stock awards generally vest in three to five years from the date of grant. Compensation expense is amortized on a straight-line basis over the requisite service period for the entire award, which is generally the maximum vesting period of the award.

We use an option-pricing model to determine the grant-date fair value of our stock options which is affected by assumptions regarding a number of complex and subjective variables. These methods used to determine these variables are generally similar to the methods used prior to 2006 for the purposes of our pro forma disclosures under SFAS No. 123. We make assumptions regarding expected term, expected volatility, expected dividend yield, and risk-free interest rate in determining the fair value of our stock options. The expected term represents the weighted-average period that stock options are expected to remain outstanding. The expected term assumption is estimated based on the stock options vesting terms and remaining contractual life and employees historical exercise behavior. The expected volatility is based on the historical volatility of our common stock over a period of time equal to the expected term of the stock options. The dividend yield assumption is based on the Company s current dividend payout rate on its common stock. For the risk-free interest rate assumption is based upon the U.S. Treasury yield curve in effect at the time of grant appropriate for the term of the employee stock options.

For restricted share awards, the grant-date fair value is measured at the fair value of the Company s common stock as if the restricted share was vested and issued on the date of grant.

As share-based compensation expense under SFAS No. 123(R) is based on awards ultimately expected to vest, it is reduced for estimated forfeitures. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Share-based compensation is discussed in more detail in Notes 1 and 19 to the Company s consolidated financial statements presented elsewhere herein.

Overview

During 2006, we achieved another year of record financial performance attaining our tenth consecutive year of record earnings. Our 19% increase in diluted earnings per share for 2006 represents one of the highest earnings per share growth rates among our peer banks. These consistently solid financial results have been achieved over various economic, interest rate and real estate cycles. We also ended the year on a very positive note with fourth quarter 2006 earnings amounting to $39.1 million, representing a 27% increase over the corresponding quarter in the previous year. We are highly encouraged by the results of the fourth quarter and plan to build on this momentum in 2007.

One of the highlights of 2006 was the successful completion of another large acquisition. Standard Bank was headquartered in Monterey Park, California and provided community banking services through six branches in the Los Angeles metropolitan area which are prime locations in the Bank s niche market. As of the transaction closing date of March 17, 2006, Standard Bank had total assets of $897.7 million, net loans of $490.0 million, and total deposits of $728.5 million. The acquisition resulted in total goodwill of $100.9 million and core deposit premium of $8.6 million. All of Standard Bank s systems have been successfully integrated into our infrastructure. This strategic acquisition has enhanced the Bank s already strong franchise in the ethnic Chinese-American retail and commercial markets.

During 2006, we also made noteworthy strides in expanding our market presence in the greater China region. We received approval from the Hong Kong Monetary Authority (HKMA) on August 1, 2006 to open a full service branch in Hong Kong. This branch commenced operations during the first quarter of 2007, offering a variety of deposit, loan and international banking products. Additionally, we recently received regulatory approval to open a representative office in Shanghai, China. Similar to our existing representative office in Beijing, the Shanghai office will broaden our international banking capabilities and extend our penetration into the robust greater China market. We anticipate the Shanghai office to open sometime in the second quarter of 2007.

Net income totaled $143.4 million during 2006, a 32% increase from the $108.4 million earned during 2005. As previously mentioned, diluted earnings per share for the full year increased 19% to $2.35 from $1.97 in 2005. Our return on average assets in 2006 was 1.46%, compared to 1.55% in 2005 and return on average equity was15.78 % in 2006, compared to 18.27% in 2005. Management expects net income per diluted common share for 2007 to be 6% to 7% higher than in 2006 based on a projected annual loan growth of 12% to 16% and annual deposit growth of 8% to 10%. Our earnings projection for 2007 also assumes a stable interest rate environment and a strategy to securitize loans on a consistent basis to improve liquidity and to reduce overall credit risk.

Net interest income increased 31% to $367.5 million during 2006, compared with $280.1 million during 2005. The substantial increase in net interest income is predominantly due to the growth in loans and investment securities compounded by steady increases in interest rates by the Federal Reserve during 2006. These factors were partially offset by increases in both the volume and rates paid for time deposits and money market accounts, as well as growth in the volume of all types of borrowings and higher rates paid on FHLB advances. Our net interest margin decreased 24 basis points to 3.98% during 2006, compared to 4.22% during 2005. The continuing competitiveness in loan and deposit pricing as well as the flat to inverted yield curve throughout 2006 adversely impacted our net interest margin during 2006. Assuming a stable interest rate environment during 2007, we anticipate the net interest margin for 2007 to be in the range of 3.85% and 4.00%.

Noninterest income increased 16% to $34.4 million during 2006 from $29.6 million in the prior year, primarily due to higher branch-related fees as well as higher mortgage servicing fees resulting from increased loan securitization activity during 2006. These factors were partially offset by lower net gains on sales of investment securities available-for-sale and lower income from secondary market activities.

As a result of our continued expansion during 2006, total noninterest expense increased 31% to $161.9 million in 2006, compared with $123.5 million in 2005. This increase is primarily driven by a 32% increase in compensation and employee benefits, a 42% increase in occupancy and equipment expenses, and a 29% increase in other operating expenses. The increases in compensation, occupancy, and other operating expenses can be attributed to the acquisitions of United National Bank during the third quarter of 2005 and Standard Bank in the first quarter of 2006. Occupancy expenses also increased due to the recent relocation and expansion of our corporate offices and other operating expenses increased due to higher professional fees and advertising expenses. Despite the sizable increase in overall expenses, our efficiency ratio, which represents noninterest expense (excluding the amortization of intangibles and investments in affordable housing partnerships) divided by the aggregate of net interest income before provision for loan losses and noninterest income, increased only marginally to 37.16% during 2006, compared to 36.53% during 2005. We believe this to be a reflection of our ability to efficiently and effectively utilize our resources and operating platform to support our continuing growth. Due to the continuing growth of the Bank, we anticipate noninterest expenses for 2007 to increase by approximately 12% to 15%, and our efficiency ratio for the full year of 2007 to be in the 38% to 40% range.

Total consolidated assets at December 31, 2006 increased 31% to $10.82 billion, compared with $8.28 billion at December 31, 2005. A 22% growth in gross loans and an 89% growth in investment securities were the primary drivers of this increase. Excluding the impact of the Standard Bank acquisition and residential loan securitizations, organic loan growth was 26%, or $1.76 billion, during 2006. We attribute overall loan growth to the continued expansion of relationships throughout California, the addition of seasoned and skilled banking professionals, and increased loan origination volume from our branch network. We estimate loan growth in 2007 to be 12% to 16%, reflecting the core rate of growth in the Bank s lending markets, the addition of new client relationships, and the utilization of additional lending programs and products.

Total average assets increased 40% to $9.81 billion in 2006, compared to $7.00 billion in 2005, due primarily to the growth in average loans and investment securities. Total average loans grew 33% to $7.83 billion during 2006, with all major loan sectors experienced double-digit growth during 2006. Total average investment securities increased 83% to $1.24 billion during 2006 primarily due to $788.0 million in residential loan securitizations during the year. Total average deposits rose 31% during 2006 to $6.78 billion, compared to $5.18 billion in 2005. We experienced gains in all deposit categories during 2006, with the most significant contributions coming from time and money market deposits.

Total nonperforming assets were $19.9 million, or 0.18% of total assets at December 31, 2006, compared with $30.1 million, or 0.36% of total assets, at December 31, 2005. The allowance for loan losses totaled $78.2 million at December 31, 2006, representing 0.95% of outstanding total loans. We continue to experience historically low levels and little or no loss in almost every segment of our loan portfolio. During 2006, net loan recoveries totaled $484 thousand, representing 0.01% of average loans during 2006. This compares with $4.7 million in net loan chargeoffs, or 0.08% of average loans, during 2005. We anticipate our overall asset quality to remain sound throughout 2007. We estimate the ratio of the allowance for loan losses to total loans to range from 0.95% to 1.00% for 2007, reflecting our continued strategy of loan securitizations combined with credit quality remaining at high levels.

We continue to be well-capitalized under all regulatory guidelines with a Tier I risk-based capital ratio of 9.56%, a total risk-based capital ratio of 11.23%, and a Tier I leverage ratio of 8.28% at December 31, 2006. During 2006, we raised $30.9 million in additional regulatory capital through the issuance of trust preferred securities in a trust preferred offering. Trust preferred securities currently qualify as Tier I capital for regulatory purposes. The net proceeds from the trust preferred offering were used to partially fund the acquisition of Standard Bank and also to support the continued growth of the Bank.

In recognition of the Bank s consistent and solid financial performance, the Board of Directors authorized a 100% increase in the quarterly cash dividends paid to shareholders. Commencing with the first quarter of 2007, cash dividends will increase to $0.10 per share, compared with the $0.05 per share paid in previous quarters. Additionally, the Board has also authorized a new stock repurchase program to buy back up to $30.0 million of the Company s common stock. This dividend increase, along with the new stock repurchase program, reflect not only our commitment to return capital to our shareholders, but also our continued confidence about the future of the Company.

Results of Operations

Net income for 2006 totaled $143.4 million, compared with $108.4 million for 2005 and $78.0 million for 2004, representing an increase of 32% for 2006 and 39% for 2005. On a per diluted share basis, net income was $2.35, $1.97 and $1.49 for 2006, 2005 and 2004, respectively. The increases in net earnings during both 2006 and 2005 are primarily attributable to higher net interest income, partially offset by higher operating expenses and higher provision for income taxes.

Our return on average total assets declined to 1.46% in 2006, compared to 1.55% in 2005 and 1.57% in 2004. The decrease in our return on average total assets during 2006, relative to 2005 and 2004, is due to the Company s significant growth both organically and through the recent acquisitions of Standard Bank in March 2006 and United National Bank in September 2005.

Our return on average stockholders equity also decreased to 15.78% in 2006, compared with 18.27% in 2005 and 17.86% in 2004. The decrease in the return on average stockholders equity during 2006, compared to 2005, resulted from the issuance of additional shares of Company common stock in connection with the acquisition of Standard Bank.

Table 1: *Components of Net Income*

	Year Ended December 31, 2006 (In millions)	2005	2004
Net interest income	$ 367.5	$ 280.1	$ 199.2
Provision for loan losses	(6.2)	(15.9)	(16.8)
Noninterest income	34.4	29.7	30.4
Noninterest expense	(161.9)	(123.5)	(91.5)
Provision for income taxes	(90.4)	(62.0)	(43.3)
Net income	$ 143.4	$ 108.4	$ 78.0
Return on average total assets	1.46 %	1.55 %	1.57 %
Return on average stockholders equity	15.78 %	18.27 %	17.86 %

Net Interest Income

Our primary source of revenue is net interest income, which is the difference between interest earned on loans, investment securities and other earning assets less the interest expense on deposits, borrowings and other interest-bearing liabilities. Net interest income in 2006 totaled $367.5 million, a 31% increase over net interest income of $280.1 million in 2005.

Total interest and dividend income during 2006 increased 60% to $660.1 million compared with $411.4 million during 2005. This increase is attributable primarily to a 39% growth in average earning assets, predominantly loans and investment securities. Average loans increased 33% to $7.83 billion in 2006, from $5.89 billion in 2005 while average investment securities grew 83% to $1.24 billion during 2006, compared to $673.9 million during 2005. Increased yields on all categories of earning assets also contributed to the increase in interest and dividend income, but to a lesser degree.

Total interest expense during 2006 increased 123% to $292.6 million compared with $131.3 million a year ago. The increase in interest expense during 2006 can be attributed to both the significant growth in average interest-bearing liabilities, predominantly time deposits, money market accounts, and repurchase agreements, as well as higher rates paid on all categories of interest-bearing liabilities, reflecting the current interest rate environment and sustained pricing competition in the deposit market.

Net interest margin, defined as net interest income divided by average earning assets, decreased 24 basis points to 3.98% during 2006, from 4.22% during 2005. The overall yield on earning assets increased 95 basis points to 7.14% in 2006, from 6.19% in 2005, due to several consecutive Federal Reserve interest rate increases during 2006.

Our funding cost on interest-bearing liabilities increased by 133 basis points to 3.88% during 2006, compared to 2.55% for 2005. The combined impact of the current interest rate environment and continued competition in the deposit market were the primary drivers of our increased cost of funds during 2006. To help fund our substantial loan growth during 2006, we increased our reliance on time deposits, other borrowings and long-term debt, further contributing to the overall increase in our cost of funds for the year.

We also continue to rely on noninterest-bearing demand deposits as a funding source, with average noninterest-bearing demand deposits increasing 8% to $1.25 billion during 2006, compared to $1.16 billion in 2005. Our overall cost of funds, which takes into account our portfolio of noninterest-bearing demand deposits, increased 125 basis points to 3.33% during 2006, compared to 2.08% for the previous year.

Comparing 2005 to 2004, our net interest margin remained relatively stable, decreasing 2 basis points to 4.22% in 2005, compared to 4.24% in 2004. In 2005, our overall yield on earning assets increased 83 basis points to 6.19%, from 5.36% in 2004, due to several consecutive Federal Reserve interest rate increases during 2005. Similarly, our funding cost on interest-bearing liabilities increased 105 basis points to 2.55% during 2005, compared to 1.50% during 2004, reflecting the increasing interest rate environment at the time as well as heightened competition in the deposit market. Our overall cost of funds, taking into consideration our portfolio of noninterest-bearing demand deposits, increased 90 basis points to 2.08% during 2005, from 1.18% during 2004.

The following table presents the net interest spread, net interest margin, average balances, interest income and expense, and the average yields and rates by asset and liability component for the years ended December 31, 2006, 2005 and 2004:

Table 2: Summary of Selected Financial Data

	Year Ended December 31, 2006			**2005**			**2004**		
	Average Balance	**Interest**	**Average Yield Rate**	**Average Balance**	**Interest**	**Average Yield Rate**	**Average Balance**	**Interest**	**Average Yield Rate**
	(Dollars in thousands)								
ASSETS									
Interest-earning assets:									
Short-term investments	$ 10,531	$ 443	4.21 %	$ 8,554	$ 275	3.21 %	$ 54,739	$ 639	1.17 %
Securities purchased under resale agreements	94,795	7,076	7.46 %	15,961	1,118	7.00 %	-	-	-
Investment securities available-for-sale (1)(2)(3)	1,235,633	60,607	4.90 %	673,930	25,912				