HomeStreet, Inc.
Form 10-K
March 15, 2013

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, 2012

OR

¨ 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: 001-35424

HOMESTREET, INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Washington<br>(State or other jurisdiction of incorporation or organization) | 91-0186600<br>(I.R.S. Employer Identification Number) |

601 Union Street, Ste. 2000
Seattle, WA 98101
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (206) 623-3050

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

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, no par value | NASDAQ Stock Market LLC |

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 ¨ No x

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 ¨ 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 ¨

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

| | | | |
|---|---|---|---|
| Large accelerated filer | ¨ | Accelerated filer | ¨ |
| Non-accelerated filer | x (Do not check if a smaller reporting company) | Smaller reporting company | ¨ |

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

As of June 30, 2012, the last day of the registrant’s most recently completed second fiscal quarter, the aggregate market value of common stock held by non-affiliates was approximately $198.9 million, based on a closing price of $15.99, after giving effect to the 2 for 1 stock split which took place on November 5, 2012. Shares of common stock held by each executive officer and director and by each person known to the Company who beneficially owns more than 5% of the outstanding common stock have been excluded in that such persons may under certain circumstances be deemed to be affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes.

The number of outstanding shares of the registrant’s common stock as of February 28, 2013 was 14,384,453.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information that will be contained in the definitive proxy statement for the registrant's annual meeting to be held in 2013 is incorporated by reference into Part III of this Form 10-K.

Table of Contents



Unless we state otherwise or the content otherwise requires, references in this Form 10-K to “HomeStreet,” “we,” “our,” “us” or the “Company” refer collectively to HomeStreet, Inc., a Washington corporation, HomeStreet Bank (“Bank”), HomeStreet Capital Corporation (“HomeStreet Capital”) and other direct and indirect subsidiaries of HomeStreet, Inc.

Table of Contents

PART 1

FORWARD-LOOKING STATEMENTS

This Form 10-K and the documents incorporated by reference contain, in addition to historical information, “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). These statements relate to our future plans, objectives, expectations, intentions and financial performance, and assumptions that underlie these statements. All statements other than statements of historical fact are “forward-looking statements” for the purposes of these provisions. When used in this Form 10-K, terms such as “anticipates,” “believes,” “continue,” “could,” “estimates,” “expects,” “intends,” “may,” “plans,” “potential,” “predicts,” “should,” or “will” or the negative of those other comparable terms are intended to identify such forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause industry trends or actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these statements. Our actual results may differ significantly from the results discussed in such forward-looking statements.

Unless required by law, we do not intend to update any of the forward-looking statements after the date of this Form 10-K to conform these statements to actual results or changes in our expectations. Readers are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this Form 10-K.

Except as otherwise noted, references to “we,” “our,” “us” or “the Company” refer to HomeStreet, Inc. and its subsidiaries that are consolidated for financial reporting purposes.

ITEM 1 BUSINESS

General

We are a 91-year-old diversified financial services company headquartered in Seattle, Washington, serving consumers and businesses primarily in the Pacific Northwest and Hawaii. The Company is principally engaged in real estate lending, including mortgage banking activities, and retail and commercial banking operations. Our primary subsidiaries are HomeStreet Bank (the "Bank") and HomeStreet Capital Corporation. HomeStreet Bank is a Washington state-chartered savings bank that provides residential and commercial loans, deposit products and services, non-deposit investment products, and cash management services. HomeStreet Bank's primary loan products include single family residential mortgages, loans secured by commercial real estate, loans for residential and commercial real estate construction, and commercial business loans. HomeStreet Capital Corporation, a Washington corporation, originates, sells and services multifamily mortgage loans under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS®) (DUS® is a registered trademark of Fannie Mae.) in conjunction with HomeStreet Bank. Doing business as HomeStreet Insurance, we provide insurance products and services for consumers and businesses. We additionally offer single family home loans through our partial ownership in an affiliated business arrangement known as Windermere Mortgage Services Series LLC (“WMS LLC”). At December 31, 2012, we had total assets of $2.63 billion.

We currently have a network of 22 bank branches in the Puget Sound region of Washington State, Portland, Oregon, Southwest Washington, and Hawaii, as well as 24 stand-alone lending centers located in these same areas and additionally in Aberdeen and Spokane, Washington, the Eugene and Salem regions of Oregon, and in the Boise and northern regions of Idaho. WMS LLC provides point-of-sale loan origination services at approximately 40

Windermere Real Estate offices in Washington and Oregon.

We operate four primary business segments: Community Banking, Single Family Mortgage Lending, Income Property Lending and Residential Construction Lending. For a discussion of operating results of each of these lines of business, see "Business Segments" within Management's Discussion and Analysis of this Form 10-K.

Community Banking. We provide a diversified set of financial products and services to our consumer and business customers, including deposit products, investment products, insurance products, cash management services, consumer and business loans and Small Business Administration loans.

Single Family Mortgage Lending. We originate and sell residential mortgage loans into the secondary market both directly and through our affiliated business arrangement with WMS LLC. This business line also originates and services loans for our portfolio on a selective basis including home equity loans. We originate mortgages using secondary market standards and the majority are sold to or securitized by Fannie Mae, Freddie Mac or Ginnie Mae, while we retain the right to service these loans. In addition, the Company originates Federal Housing Administration ("FHA")-insured and Department of Veterans' Affairs ("VA")-guaranteed mortgage loans that are used to back Ginnie Mae-guaranteed securities. A small percentage of loans are brokered or sold on a servicing-released basis to correspondent lenders.

Income Property Lending. We originate commercial real estate loans, including multifamily lending through our Fannie Mae DUS business. These loans are sold to or securitized by Fannie Mae and we generally continue to service those loans after the sale. We also originate commercial construction loans, bridge loans and permanent loans for our own portfolio and for sale to other investors such as insurance companies.

Residential Construction Lending. We originate residential construction loans for our own portfolio, focusing on loans to developers for single family home construction that are short duration in nature. Generally, we do not make loans secured by or for the purchase of raw land.

Initial Public Offering

On February 15, 2012, we completed our initial public offering of 8,723,632 shares of common stock for an initial offering price of $11.00 per share (after giving effect to the 2-for-1 forward stock split effective March 6, 2012 and the 2-for-1 forward stock split effective November 5, 2012). The net increase in HomeStreet's capital was $86.4 million, which included net cash proceeds of $87.7 million received in 2012, less $1.4 million of issuance costs paid in 2011. The Company contributed $55.0 million to the Bank on February 24, 2012 and an additional $10.0 million on April 26, 2012, leaving approximately $22.7 million of net proceeds at the Company to be used for general corporate purposes. Shares of our common stock are traded on the NASDAQ Global Select Market under the symbol “HMST.”

Recent Developments

On March 12, 2013, the Company received notification from the Federal Reserve Bank permitting the Company to pay all past deferred interest due on its outstanding debt securities (Trust Preferred Securities, or "TruPS") and the interest payment due on March 15, 2013, for a total of $13.5 million. The Company intends to replenish its liquidity through payment of dividends from the Bank for which the Bank has made regulatory application and sought regulatory non-objection. No assurances can be given that such non-objection has or will be obtained from the relevant regulators.

The March 15, 2013 payment of the deferred and current interest lifts the restrictions under the terms of the TruPS indentures that prohibited the Company from making cash dividends or distributions to shareholders if the TruPS interest is not paid current. However, the Company remains under a cease and desist order which restricts the Company from making cash dividends or distributions without regulatory consent.

Regulatory Update

On March 26, 2012, the Federal Deposit Insurance Corporation (“FDIC”) and the Washington State Department of Financial Institutions (“WDFI”) terminated the cease and desist order for the Bank (“Bank Order”), dated May 8, 2009 and the Bank Order was replaced with a memorandum of understanding ("MOU"). On December 27, 2012, the Bank was notified by the FDIC and the WDFI that the Bank had taken appropriate corrective actions to address the MOU and consequently the Bank's MOU was terminated effective December 27, 2012. The Bank is no longer considered a “troubled institution” and is now considered “well-capitalized” within the meaning of the FDIC’s prompt corrective action rules. The Company remains under a cease and desist order (the “Company Order”) supervised by the Federal Reserve Bank.

The termination of the Bank Order provided several benefits, including a reduction in our FDIC assessment and examination fees; resumption of portfolio lending for certain lending products; the ability to open or re-locate retail deposit branches; access to federal funds lines from correspondent banks; the re-opening of certain correspondent lending channels that had previously been restricted; and the ability to increase the amount of trading partner relationships used for hedging purposes. Additionally, as a result of the termination of the Bank Order and the related impact on certain rating agency metrics, the Bank now fully complies with the seller servicer requirements of government-sponsored entities such as Fannie Mae and Freddie Mac.

In recognition of the significant improvement in the Bank's financial condition, results of operations and risk profile, on July 10, 2012 the Federal Reserve Bank granted full access to all Federal Reserve Bank lending and depository services.

Changes in Management

On July 26, 2012, the Company announced the appointment of Cory D. Stewart as the Company's Executive Vice President and Chief Accounting Officer, which became effective in the third quarter of 2012, upon receipt of the necessary regulatory approvals.

On July 26, 2012, the Company also announced the appointment of Darrell van Amen as the Company's Executive Vice President and Chief Investment Officer, which became effective in the third quarter of 2012, upon receipt of the necessary regulatory approvals.

On October 15, 2012, in connection with Mr. Stewart and Mr. van Amen assuming their respective positions with the Company, Mark K. Mason relinquished his role as acting Chief Financial Officer and Principal Accounting Officer of the Company. Mr. Mason continues to serve as the Company's Vice Chairman, President and Chief Executive Officer.

Business Strategy

During 2012, we recapitalized the Company through our initial public offering. In addition, our performance over the course of 2012 was characterized by strong mortgage banking results and significant improvement in asset quality. We now believe we have sufficient capital to be a source of strength to the Bank, provide for payment of our obligations under our outstanding TruPS, and pursue our business strategy.

We are pursuing the following strategies in our business segments:

Community Banking. Our Community Banking strategy involves the development of an integrated consumer and business financial services delivery platform. We seek to meet the financial needs of our consumer and business customers by providing targeted banking products and services, investment advice and products, and insurance products through our bank branches and through dedicated investment advisors, insurance agents and business banking officers. We currently plan to expand our bank branch network primarily focusing on high-growth areas of Puget Sound. We also intend to grow our core deposits by increasing business deposits from new cash management and business lending customers.

Single Family Mortgage Lending. We have leveraged our reputation for high quality service and reliable loan closing to increase our single family mortgage market share significantly over the last three years. In early 2012, we took advantage of an opportunity to add experienced loan originators and accelerated our plans to expand our single family mortgage origination business by hiring approximately 170 mortgage personnel formerly associated with MetLife Home Loans. HomeStreet continued recruiting throughout 2012, ultimately hiring 389 mortgage lending and support personnel, an increase of 146%. HomeStreet added 15 lending offices, including expansion into Idaho. The addition of these employees contributed to the significant increase in our single family mortgage loan origination volume during 2012. We intend to continue to focus on conventional conforming and government insured or guaranteed single family mortgage origination. We also expect to use portfolio lending to complement secondary market lending, particularly for well-qualified borrowers with loan sizes greater than the conventional conforming limits.

Income Property Lending. We currently plan to grow our commercial real estate business, with a focus on our multifamily lending mortgage origination business, particularly through our Fannie Mae DUS origination and servicing relationships. We plan to expand beyond our current markets by adding loan origination personnel and by forming strategic alliances with multifamily property service providers inside and outside our existing lending areas. We expect to continue to benefit from being one of only 25 companies nationally that is an approved Fannie Mae DUS seller and servicer. In addition, we have historically supported our DUS program by providing short-term bridge loans to experienced borrowers who purchase apartment buildings for renovation, which we then seek to replace with permanent financing through the Fannie Mae DUS program upon completion of the renovations. We also originate commercial construction real estate loans, bridge loans and permanent loans for our portfolio, primarily on office, retail, industrial and multifamily property types located within the Company's geographic footprint. We also may place loans with capital market sources, such as life insurance companies.

Residential Construction Lending. We have resumed originating residential construction loans under enhanced underwriting standards with a significantly reduced portfolio concentration and a focus on home construction loans as opposed to land development projects or raw land.

Market and Competition

The financial services industry is highly competitive. We compete with banks, savings and loan associations, credit unions, mortgage banking companies, insurance companies, finance companies, and investment and mutual fund companies. In particular, we compete with several financial institutions with greater resources, including the capacity to make larger loans, fund extensive advertising and offer a broader array of products and services. The number of competitors for middle-market business customers has, however, decreased in recent years due to bank failures and consolidations. In recent years national banks have focused on larger customers to achieve economies of scale in lending and depository relationships and have also consolidated business banking operations and support and reduced service levels in the Pacific Northwest. We have taken advantage of the failures and takeovers of certain of our competitors by recruiting well-qualified employees and attracting new customers who seek long-term stability, local decision-making, quality services, products and expertise. We believe there is a significant opportunity for a well-capitalized, community-focused bank that emphasizes responsive and personalized service to provide a full range of financial services to small- and middle-market commercial and consumer customers in those markets where we do business.

In addition, we believe we are well positioned to take advantage of changes in the single family mortgage origination and servicing industry that have helped to reduce the number of competitors. The mortgage industry is compliance-intensive and requires significant expertise and internal control systems to ensure mortgage loan origination and servicing providers meet all origination, processing, underwriting, servicing and disclosure requirements. These requirements are causing some competitors to exit the industry. New entrants must make significant investments in experienced personnel and specialized systems to manage the compliance process. These investments represent a significant barrier to entry. In addition, lending in conventional and government guaranteed or insured mortgage products, including FHA and VA loans, requires significantly higher capitalization than had previously been required for mortgage brokers and non-bank mortgage companies.

Our single family mortgage origination and servicing business is highly dependent upon compliance with underwriting and servicing guidelines of Fannie Mae, Freddie Mac, FHA, VA and Ginnie Mae as well as a myriad of federal and state consumer compliance regulations. Our demonstrated expertise in these activities, together with our significant volume of lending in low- and moderate-income areas and direct community investment, contribute to our uninterrupted record of “Outstanding” Community Reinvestment Act (“CRA”) ratings since 1986. We believe our ability to maintain our historically strong compliance culture represents a significant competitive advantage.

We currently intend to expand our commercial real estate mortgage lending business by targeting strong apartment markets and experienced borrowers. We expect to continue to benefit from being one of only 25 companies nationally that is approved Fannie Mae DUS sellers and servicers. The Fannie Mae DUS program became a key multifamily funding source nationally during the turmoil in the financial services industry and the resulting loss of other financing sources. During 2012, an increasing number of banks began competing for multifamily permanent loans for their portfolios. We expect to continue to be in a strong competitive position versus other banks due to our ability to offer both portfolio and Fannie Mae DUS products, depending on the needs of the customer.

Employees

As of December 31, 2012 the Company employed approximately 1,099 full-time equivalent employees compared to 613 full-time equivalents at December 31, 2011.

Where You Can Obtain Additional Information

We file annual, quarterly, current and other reports with the Securities and Exchange Commission (the "SEC"). We make available free of charge on or through our website http://www.homestreet.com all of these reports (and all amendments thereto), as soon as reasonably practicable after we file these materials with the SEC. You may review a copy of these reports, including exhibits and schedules filed therewith, and obtain copies of such materials at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website (http://www.sec.gov) that contains reports, proxy and information statements and other information regarding registrants, such as HomeStreet, Inc., that file electronically with the SEC.

Table of Contents

REGULATION AND SUPERVISION

The following is a brief description of certain laws and regulations that are applicable to us. The description of these laws and regulations, as well as descriptions of laws and regulations contained elsewhere in this annual report on Form 10-K, does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.

The bank regulatory framework to which we are subject is intended primarily for the protection of bank depositors and the Deposit Insurance Fund and not for the protection of shareholders or other security holders.

General

The Company is a savings and loan holding company and is regulated by the Board of Governors at the Federal Reserve System (the "Federal Reserve"), and the Washington State Department of Financial Institutions, Division of Banks (the "WDFI"). The Company is required to register and file reports with, and otherwise comply with, the rules and regulations of the Federal Reserve and the WDFI.

The Office of Thrift Supervision, or the OTS, previously was the Company's primary federal regulator. Under the Dodd-Frank Act, the OTS was dissolved on July 21, 2011 and its authority to supervise and regulate the Company and its non-bank subsidiaries was transferred to the Federal Reserve. References to the Federal Reserve in this document should be read to include the OTS prior to the date of the transfer with respect to those functions transferred to the Federal Reserve.

The Bank is a Washington state-chartered savings bank. The Bank is subject to regulation, examination and supervision by the WDFI and the FDIC.

As a result of the recent financial crisis, regulation of the financial services industry has been undergoing major changes. Among these is the Dodd-Frank Act, which makes significant modifications to and expansions of the rulemaking, supervisory and enforcement authority of the federal banking regulators. Some of the changes were effective immediately, but others are being phased in over time. The Dodd-Frank Act requires various regulators, including the banking regulators, to adopt numerous regulations, not all of which have been finalized. Accordingly, in many instances, the precise requirements of the Dodd-Frank Act are not yet known.

Further, new statutes, regulations and guidance are considered regularly that could contain wide-ranging potential changes to the competitive landscape for financial institutions operating and doing business in the United States. We cannot predict whether or in what form any proposed statute, regulation or other guidance will be adopted or promulgated, or the extent to which our business may be affected. Any change in policies, whether by the Federal Reserve, the WDFI, the FDIC, the Washington legislature or the United States Congress, could have a material adverse impact on us and our operations and shareholders. In addition, the Federal Reserve, the WDFI and the FDIC have significant discretion in connection with their supervisory and enforcement activities and examination policies, including, among other things, policies with respect to the Bank's capital levels, the classification of assets and establishment of adequate loan loss reserves for regulatory purposes.

Our operations and earnings will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. In addition to its role as the regulator of savings and loan holding companies, the Federal Reserve has, and is likely to continue to have, an important impact on the operating results of financial institutions through its power to implement national monetary and fiscal policy including, among other things, actions taken in order to curb inflation or combat a recession. The Federal Reserve affects the levels of bank loans, investments and deposits through its control over the issuance of United States government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which banks are subject. In recent years, in response to the financial crisis, the Federal Reserve has created several innovative programs to stabilize certain financial institutions, to help ensure the availability of credit and to purchase financial assets through programs such as quantitative easing or “QE”. Quantitative easing has had a significant impact on the market for mortgage-backed securities and by some accounts has stimulated the national economy. We believe these policies have had a beneficial effect on the Company and the mortgage banking industry as a whole. We cannot predict the nature or impact of future changes in monetary and fiscal policies of the Federal Reserve.

The Company is currently operating under a cease and desist order issued by our primary federal regulator, the Federal Reserve, as described below under "Company Order." Under the cease and desist order, we are required to notify, and in certain cases receive the permission of, the Federal Reserve prior to taking certain actions.

Company Order

Table of Contents

The Company is currently operating under an Order to Cease and Desist issued by the OTS on May 18, 2009 and now administered by the Federal Reserve. Under the Company Order, HomeStreet, Inc. agreed to refrain from engaging in all unsafe and unsound practices that had resulted in the operation of HomeStreet, Inc. with low earnings and inadequate capital. In addition, for so long as the Company Order remains in place, HomeStreet, Inc. has also agreed to not do any of the following without the consent of the Federal Reserve:

- pay dividends or make any other capital distributions;
- incur, issue, renew, repurchase, make payments on or roll over any debt (including payments on trust preferred securities);
- increase any current lines of credit;
- guarantee the debt of any entity;
- make any "golden parachute" or "prohibited indemnification payments" unless we have complied with certain statutory and regulatory requirements; and
- make changes in our Board of Directors or senior executive officers without meeting certain prior notification requirements.

Pursuant to the Company Order, we developed a plan to manage our liquidity, capital and risk profile, and to address our financial obligations, including deferring interest payments on the TruPS, without relying on dividends from the Bank. Following the closing of our initial public offering in February 2012 and the subsequent contribution of $55.0 million to the Bank on February 24, 2012 with an additional $10.0 million contributed on April 26, 2012, we retained capital at the Company that management believes is adequate to meet the needs of the Company without requiring additional dividends from the Bank for the near future.

The Company Order will remain in effect until terminated, modified or suspended by the Federal Reserve. We are currently in compliance with the Company Order, although the requirements imposed by the Company Order do not include quantitative capital ratio or asset quality targets. We send quarterly status reports to the Federal Reserve at their request. While management believes that the Company Order will be lifted, we cannot give assurance as to the timing of such action.

Consent Agreement/Memorandum of Understanding

The Bank had previously consented to the issuance by the FDIC and the WDFI of an Order to Cease and Desist dated May 8, 2009. The Bank Order was terminated on March 26, 2012. Also on March 26, 2012, the Bank entered into a MOU with the FDIC and the WDFI. The MOU was terminated on December 27, 2012.

Regulation of the Company

General

Because we have made an election under Section 10(1) of the Home Owners' Loan Act ("HOLA") for the Bank to be treated as a "savings association" for purposes of Section 10 of HOLA, the Company is registered as a savings and loan holding company with the Federal Reserve and is subject to Federal Reserve regulations, examinations, supervision and reporting requirements relating to savings and loan holding companies. Among other things, the Federal Reserve is authorized to restrict or prohibit activities that are determined to be a serious risk to the financial safety, soundness or stability of a subsidiary savings bank. Unlike bank holding companies, savings and loan holding companies have not been subject to any specific regulatory capital ratios, although they have been subject to review by the Federal Reserve and approval of capital levels as part of its examination process. However, under the Dodd-Frank Act, the Company will become subject to capital requirements. Our continued ability to use the provisions of Section 10(1) of HOLA - which allow the Company to be registered as a savings and loan holding company rather than as a bank holding company - is conditioned upon the Bank's continued qualification as a qualified thrift lender under the Qualified Thrift Lender test set forth in HOLA. See "- Regulation and Supervision of HomeStreet Bank - Qualified Thrift Lender Test." Since the Bank is chartered under Washington law, the WDFI has authority to regulate the Company generally relating to its conduct affecting the Bank. As a subsidiary of a savings and loan holding company, the Bank is subject to certain restrictions in its dealings with the Company and affiliates thereof.

Numerous provisions of the Dodd-Frank Act affect the Company and its business and operations. Some of the provisions are:

- New capital requirements for savings and loan holding companies.
- All holding companies of depository institutions are required to serve as a source of strength for their depository subsidiaries.

- The Federal Reserve is given heightened authority to examine, regulate and take action with respect to all of a holding company's subsidiaries.

The Company is a unitary savings and loan holding company within the meaning of federal law. Generally, companies that become savings and loan holding companies following the May 4, 1999 grandfather date in the Gramm-Leach-Bliley Act of 1999 may engage only in the activities permitted for financial institution holding companies as well as activities that are permitted for multiple savings and loan holding companies. Because the Company became a savings and loan holding company prior to that grandfather date, the activities in which the Company and its subsidiaries (other than the Bank and its subsidiaries) may engage generally are not restricted by HOLA. If, however, we are acquired by a non-financial company, or if we acquire another savings association subsidiary (and become a multiple savings and loan holding company), we will terminate our “grandfathered” unitary savings and loan holding company status and become subject to certain limitations on the types of business activities in which we could engage. The Company may not engage in any activity or render any service for or on behalf of the Bank for the purpose of or with the effect of evading any law or regulation applicable to the Bank.

Because the Bank is treated as a savings association subsidiary of a savings and loan holding company, we must give the Federal Reserve at least 30 days' advance notice of the proposed declaration of a dividend by the Bank. In addition, the financial impact of a holding company on its subsidiary institution is a matter that is evaluated by the Federal Reserve, and the Federal Reserve has authority to order cessation of activities or divestiture of subsidiaries deemed to pose a threat to the safety and soundness of the Bank.

As described above, the Company Order prohibits us, among other things, from (1) paying any dividends or making any other capital distributions, (2) incurring, issuing, renewing, repurchasing, making payment on or rolling over any debt, (3) increasing any current lines of credit or (4) guaranteeing the debt of any entity, in each case without the prior written approval of the Federal Reserve.

Capital / Source of Strength

Under the Dodd-Frank Act, capital requirements will be imposed on savings and loan holding companies such as the Company. See “Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements - Proposed Capital Regulations.”

Regulations and historical practice of the Federal Reserve have required bank holding companies to serve as a “source of strength” for their subsidiary banks. The Dodd-Frank Act codifies this requirement and extends it to all companies that control an insured depository institution. Accordingly, the Company is now required to act as a source of strength for the Bank. The appropriate federal banking regulators are required by the Dodd-Frank Act to issue final rules to carry out this requirement but have not yet done so.

Restrictions Applicable to Savings and Loan Holding Companies

Federal law prohibits a savings and loan holding company, including the Company, directly or indirectly (or through one or more subsidiaries), from acquiring:

- control (as defined under HOLA) of another savings institution (or a holding company parent) without prior written approval of the Federal Reserve;
- through merger, consolidation or purchase of assets, another savings institution or a holding company thereof, or acquiring all or substantially all of the assets of such institution (or a holding company) without prior Federal Reserve or FDIC approval;
- with certain exceptions, more than 5.0% of the voting shares of a non-subsidiary savings association or a non-subsidiary holding company; or
- control of any depository institution not insured by the FDIC (except through a merger with and into the holding company's savings institution subsidiary that is approved by the FDIC).

In evaluating applications by holding companies to acquire savings associations, the Federal Reserve must consider the financial and managerial resources and future prospects of the company and institution involved, the effect of the acquisition on the risk to the insurance funds, the convenience and needs of the community and competitive factors.

A savings and loan holding company generally may not acquire as a separate subsidiary a savings association in a different state from where its current savings association is located, except:

- in the case of certain emergency acquisitions approved by the FDIC;

9

Table of Contents

- if such holding company controls a savings association that operated a home or branch office in such additional state as of March 5, 1987; or
- if the laws of the state in which the savings association to be acquired is located specifically authorize a savings association chartered by that state to be acquired by a savings institution chartered by the state where the acquiring savings association or savings and loan holding company is located, or by a holding company that controls such a state-chartered association.

Acquisition of Control

Under the federal Change in Bank Control Act, a notice must be submitted to the Federal Reserve if any person (including a company), or group acting in concert, seeks to acquire “control” of a savings and loan holding company. An acquisition of control can occur upon the acquisition of 10.0% or more of the voting stock of a savings and loan holding company or as otherwise defined by the Federal Reserve. Under the Change in Bank Control Act, the Federal Reserve has 60 days from the filing of a complete notice to act (the 60-day period may be extended), taking into consideration certain factors, including the financial and managerial resources of the acquirer and the antitrust effects of the acquisition. Any company that so acquires control would then be subject to regulation as a savings and loan holding company. Control can also exist if an individual or company has, or exercises, directly or indirectly or by acting in concert with others, a controlling influence over the Bank. Washington law also imposes certain limitations on the ability of persons and entities to acquire control of banking institutions and their parent companies.

Change in Management

Pursuant to the Company Order, we are required to give 30 days prior written notice to the Federal Reserve before adding or replacing a director, employing any person as a senior executive officer or changing the responsibility of any senior executive officer so that such person would assume a different senior executive position. Our regulators then have the opportunity to disapprove any such appointment.

Dividend Policy

Under Washington law, the Company is generally permitted to make a distribution, including payments of dividends, only if, after giving effect to the distribution, in the judgment of the board of directors, (1) the Company would be able to pay its debts as they become due in the ordinary course of business and (2) the Company's total assets would at least equal the sum of its total liabilities plus the amount that would be needed if the Company were to be dissolved at the time of the distribution to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the distribution.

The Company Order prohibits us from paying dividends or making other capital distributions without the prior written consent of the Federal Reserve. In addition, the Company's ability to pay dividends to shareholders is significantly dependent on the Bank's ability to pay dividends to the Company.

Compensation Policies

Compensation policies and practices at HomeStreet, Inc. and HomeStreet Bank are subject to regulation by their respective banking regulators and the SEC.

Guidance on Sound Incentive Compensation Policies. Effective on June 25, 2010, the Office of the Comptroller of the Currency, the Federal Reserve, the FDIC and the OTS adopted Sound Incentive Compensation Policies Final Guidance (the “Final Guidance”) designed to help ensure that incentive compensation policies at banking organizations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organization.

The Final Guidance applies to senior executives and others who are responsible for oversight of HomeStreet's company-wide activities and material business lines, as well as other employees who, either individually or as a part of a group, have the ability to expose the Bank to material amounts of risk.

Dodd-Frank Act. In addition to the Final Guidance, the Dodd-Frank Act contains a number of provisions relating to compensation applying to public companies such as the Company. The Dodd-Frank Act added a new Section 14A(a) to the Exchange Act that requires companies to include a separate non-binding resolution subject to shareholder vote in their proxy materials approving the executive compensation disclosed in the materials. In addition, a new Section 14A(b) to the Exchange Act requires any proxy or consent solicitation materials for a meeting seeking shareholder approval of an acquisition, merger, consolidation or disposition of all or substantially all of the company's assets to include a separate non-binding shareholder

Table of Contents

resolution approving certain "golden parachute" payments made in connection with the transaction. A new Section 10D to the Exchange Act requires the SEC to direct the national securities exchanges to require companies to implement a policy to "claw back" certain executive payments that were made based on improper financial statements.

In addition, Section 956 of the Dodd-Frank Act requires certain regulators (including the FDIC, SEC and Federal Reserve) to adopt requirements or guidelines prohibiting excessive compensation or compensation that could lead to material loss as well as rules relating to disclosure of compensation. On April 14, 2011, these regulators published a joint proposed rulemaking to implement Section 956 of Dodd-Frank for depository institutions, their holding companies and various other financial institutions with $1 billion or more in assets. Section 956 prohibits incentive-based compensation arrangements which encourage inappropriate risk taking by covered financial institutions and are deemed to be excessive, or that may lead to material losses. The proposed rule would (1) prohibit incentive-based compensation arrangements for covered persons that would encourage inappropriate risks by providing excess compensation, (2) prohibit incentive-based compensation arrangements for covered persons that would expose the institution to inappropriate risks by providing compensation that could lead to a material financial loss, (3) require policies and procedures for incentive-based compensation arrangements that are commensurate with the size and complexity of the institutions and (4) require annual reports on incentive compensation structures to the institution's appropriate federal regulator.

FDIC Regulations. We are further restricted in our ability to make certain "golden parachute" and "indemnification" payments under Part 359 of the FDIC regulations, and the FDIC also regulates payments to executives under Part 364 of its regulations relating to excessive executive compensation.

Emerging Growth Company

We are an "Emerging Growth Company," as defined in the Jumpstart Our Business Startups Act (the "JOBS Act"), and are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not Emerging Growth Companies. These include, but are not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from certain requirements under the Dodd-Frank Act, including the requirement to hold a non-binding advisory vote on executive compensation and the requirement to obtain stockholder approval of any golden parachute payments not previously approved. We currently intend to take advantage of some or all of these reporting exemptions until we are no longer qualify as an Emerging Growth Company.

We will remain an Emerging Growth Company for up to five years from the end of the year of our initial public offering, or until (1) we have total annual gross revenues of at least $1 billion, (2) we qualify as a large accelerated filer, or (3) we issue more than $1 billion in nonconvertible debt in a three year period.

Regulation and Supervision of HomeStreet Bank

General

As a savings bank chartered under the laws of the State of Washington, HomeStreet Bank is subject to applicable provisions of Washington law and regulations of the WDFI. As a state-chartered savings bank that is not a member of the Federal Reserve System, the Bank's primary federal regulator is the FDIC. It is subject to regulation and examination by the WDFI and the FDIC, as well as enforcement actions initiated by the WDFI and the FDIC, and its deposits are insured by the FDIC.

Washington Banking Regulation

As a Washington savings bank, the Bank's operations and activities are substantially regulated by Washington law and regulations, which govern, among other things, the Bank's ability to take deposits and pay interest, to make loans on or invest in residential and other real estate, to make consumer and commercial loans, to invest in securities, to offer various banking services to its customers and to establish branch offices. Under state law, savings banks in Washington also generally have, subject to certain limitations or approvals, all of the powers that Washington chartered commercial banks have under Washington law and that federal savings banks and national banks have under federal laws and regulations.

Washington law also governs numerous corporate activities relating to the Bank, including the Bank's ability to pay dividends, to engage in merger activities and to amend its articles of incorporation, as well as limitations on change of control of the Bank. Under Washington law, the board of directors of the Bank may not declare a cash dividend on its capital stock if payment of such dividend would cause its net worth to be reduced below the net worth requirements, if any, imposed by the WDFI and dividends may not be paid in an amount greater than its retained earnings without the approval of the WDFI. These restrictions are in addition to restrictions imposed by federal law. Mergers involving the Bank and sales or acquisitions of its branches are

Table of Contents

generally subject to the approval of the WDFI. No person or entity may acquire control of the Bank until 30 days after filing an application with the WDFI, who has the authority to disapprove the application. Washington law defines “control” of an entity to mean directly or indirectly, alone or in concert with others, to own, control or hold the power to vote 25.0% or more of the outstanding stock or voting power of the entity. Any amendment to the Bank's articles of incorporation requires the approval of the WDFI.

The Bank is subject to periodic examination by and reporting requirements of the WDFI, as well as enforcement actions initiated by the WDFI. The WDFI's enforcement powers include the issuance of orders compelling or restricting conduct by the Bank and the authority to bring actions to remove the Bank's directors, officers and employees. The WDFI has authority to place the Bank under supervisory direction or to take possession of the Bank and to appoint the FDIC as receiver.

Dodd-Frank Act

Numerous provisions of the Dodd-Frank Act affect the Bank and its business and operations. For example, the Dodd-Frank Act broadened the base for FDIC insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution. The Dodd-Frank Act also permanently increased the maximum amount of deposit insurance for banks, savings institutions and credit unions to $250,000 per depositor.

In addition, under the Dodd-Frank Act:

- The requirements relating to the Bank's capital have been modified.
- In order to prevent abusive residential lending practices, new responsibilities are imposed on parties engaged in residential mortgage origination, brokerage and lending, and securitizers of mortgages and other asset-backed securities are required, subject to certain exemptions, to retain not less than five percent of the credit risk of the mortgages or other assets backing the securities.
- Restrictions on affiliate and insider transactions are expanded.
- Restrictions on management compensation and related governance have been enhanced.
- A federal Consumer Financial Protection Bureau ("CFPB") is created with a broad authority to regulate consumer financial products and services.
- Restrictions are imposed on the amount of interchange fees that certain debit card issuers may charge.
- Restrictions on banking entities from engaging in proprietary trading or owning interests in or sponsoring hedge funds or private equity funds (the Volcker Rule), and requiring sponsors of asset-backed securities ("ABS") to retain an ownership stake in the ABS.

In part because not all of the regulations implementing the Dodd-Frank Act have yet been finalized, it is difficult to predict at this time what specific impact the Dodd-Frank Act and the final rules and regulations will have on community banks. However, it is expected that at a minimum they will increase our operating and compliance costs and could increase our interest expense. Any additional changes in our regulation and oversight, whether in the form of new laws, rules and regulations, could make compliance more difficult or expensive or otherwise materially adversely affect our business, financial condition or prospects. The provisions of the Dodd-Frank Act and the subsequent exercise by regulators of their revised and expanded powers thereunder could materially and negatively impact the profitability of our business, the value of assets we hold or the collateral available for our loans, require changes to business practices or force us to discontinue businesses and expose us to additional costs, taxes, liabilities, enforcement actions and reputational risk.

Insurance of Deposit Accounts and Regulation by the FDIC

The FDIC is the Bank's principal federal bank regulator. As such, the FDIC is authorized to conduct examinations of and to require reporting by the Bank. The FDIC may prohibit the Bank from engaging in any activity determined by law, regulation or order to pose a serious risk to the institution, and may take a variety of enforcement actions in the event the Bank violates a law, regulation or order, engages in an unsafe or unsound practice or under certain other circumstances. The FDIC also has the authority to appoint itself as receiver of the Bank or to terminate the Bank's deposit insurance if it were to determine that the Bank has engaged in unsafe or unsound practices or is in an unsafe or unsound condition.

The Bank is a member of the Deposit Insurance Fund ("DIF") administered by the FDIC, which insures customer deposit accounts. Under the Dodd-Frank Act, the amount of federal deposit insurance coverage was permanently increased from $100,000 to $250,000, per depositor, for each account ownership category at each depository institution. This change made permanent the coverage increases that had been in effect since October 2008. The unlimited FDIC insurance for non-interest bearing transaction accounts that had been available since 2008 was discontinued as of December 31, 2012.

In order to maintain the DIF, member institutions, such as the Bank, are assessed insurance premiums. In light of the stresses that have occurred on the DIF in recent years and increases in insurance coverage, assessments have risen sharply.

The Dodd-Frank Act requires the FDIC to make numerous changes to the DIF and the manner in which assessments are calculated. The minimum ratio of assets in the DIF to the total of estimated insured deposits was increased from 1.15% to 1.35%, and the FDIC is given until September 30, 2020 to meet the reserve ratio. In December 2010, the FDIC adopted a final rule setting the reserve ratio of the DIF at 2.0%. As required by the Dodd-Frank Act, assessments are now based on an insured institution's average consolidated assets less tangible equity capital.

For the purpose of determining an institution's assessment rate, each institution is provided an assessment risk assignment, which is generally based on the risk that the institution presents to the DIF. Insured institutions with assets of less than $10 billion are placed in one of four risk categories. These risk categories are generally determined based on an institution's capital levels and its supervisory evaluation. These institutions generally have an assessment rate that can range from 2.5 to 45 basis points. However, the FDIC does have flexibility to adopt assessment rates without additional rule-making provided that the total base assessment rate increase or decrease does not exceed 2 basis points. In the future, if the reserve ratio reaches certain levels, these assessment rates will generally be lowered. As of December 31, 2012, the Bank's assessment rate was 14 basis points on average assets less average tangible equity capital. Beginning in January 2013, the Bank's assessment rate declined from 14 to 9 basis points.

In addition, all FDIC-insured institutions are required to pay a pro rata portion of the interest due on obligations issued by the Financing Corporation to fund the closing and disposal of failed thrift institutions by the Resolution Trust Corporation. The Financing Corporation rate is adjusted quarterly to reflect changes in assessment bases of the DIF. These assessments will continue until the Financing Corporation bonds mature in 2019. The annual rate for the first quarter of 2013 is 0.64 basis points.

The FDIC may terminate the deposit insurance of any insured depository institution, including the Bank, if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, order or any written condition imposed by the FDIC in connection with an application or other request or in connection with a written agreement with the FDIC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance if the FDIC finds that the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC.

Qualified Thrift Lender Test

A savings association can comply with the Qualified Thrift Lender test either by meeting the Qualified Thrift Lender test set forth in the HOLA and its implementing regulations or by qualifying as a domestic building and loan association as defined in Section 7701(a)(19) of the Internal Revenue Code of 1986 and implementing regulations.

To qualify under the HOLA test, the Bank is required to maintain at least 65% of its “portfolio assets” in “qualified thrift investments” in at least nine months of the most recent 12-month period. “Portfolio assets” are total assets less (1) specified liquid assets up to 20% of total assets, (2) intangibles, including goodwill, and (3) the value of the property used to conduct business. “Qualified thrift investments” primarily consists of residential mortgages and related investments, including certain mortgage-backed securities, home equity loans, credit card loans, student loans and small business loans.

To qualify under the Internal Revenue Code test, a savings association must meet both a “business operations” test and a “60% of assets” test. The business operations test requires the business of a savings association to consist primarily of acquiring the savings of the public and investing in loans. The 60% of assets test requires that at least 60% of a savings association's assets must consist of residential real property loans and certain other traditional thrift assets.

While the Bank is eligible to qualify as a qualified thrift lender under the HOLA test, it is not clear due to statutory ambiguities that the Bank is eligible to qualify under the Internal Revenue Code test. As noted above, it is necessary for the Bank to qualify as a qualified thrift lender only under one of these two tests.

As of December 31, 2012, the Bank held approximately 99% of its portfolio assets in qualified thrift investments and had more than $1.4 billion of its portfolio assets in qualified thrift investments for each of the 12 months ending

December 31, 2012. Therefore, the Bank qualified under the HOLA test. A savings association subsidiary of a savings and loan holding company that does not meet the Qualified Thrift Lender test must comply with the following restrictions on its operations:

Table of Contents

- the association may not engage in any new activity or make any new investment, directly or indirectly, unless the activity or investment is also permissible for a national bank;
- the branching powers of the association are restricted to those of a national bank located in the association's home state; and
- payment of dividends by the association is subject to the rules regarding payment of dividends by a national bank and must be necessary for its parent company to meet its obligations and must receive regulatory approval.

Further, an institution which fails to comply with the qualified thrift lender test is also subject to possible agency enforcement action as a violation of law under the HOLA. In addition, if the institution does not requalify under HOLA test within three years after failing the test, the institution would be prohibited from engaging in any activity not permissible for a national bank and would have to repay any outstanding advances from the FHLB as promptly as possible. Within one year of the date that a savings association ceases to meet the Qualified Thrift Lender test, any company that controls the association must register as and be deemed to be a bank holding company subject to all of the provisions of the Bank Holding Company Act of 1956 and other statutes applicable to bank holding companies. There are certain limited exceptions to these requirements.

Capital and Prompt Corrective Action Requirements

Capital Requirements

Federally insured depository institutions, such as the Bank, are required to maintain a minimum level of regulatory capital. "Total capital" generally means the sum of Tier 1 capital and Tier 2 capital. The FDIC regulations recognize two types, or tiers, of capital: "core capital," or Tier 1 capital, and "supplementary capital," or Tier 2 capital. Tier 1 capital generally includes common shareholders' equity and noncumulative perpetual preferred stock, less most intangible assets. Tier 2 capital, which is recognized up to 100% of Tier 1 capital for risk-based capital purposes (after any deductions for disallowed intangibles and disallowed deferred tax assets), includes such items as qualifying general loan loss reserves (up to 1.25% of risk-weighted assets), cumulative perpetual preferred stock, long-term preferred stock (original maturity of at least 20 years), certain perpetual preferred stock, hybrid capital instruments including mandatory convertible debt, term subordinated debt, intermediate-term preferred stock (original average maturity of at least five years) and net unrealized holding gains on equity securities (subject to certain limitations); provided, however, the amount of term subordinated debt and intermediate term preferred stock that may be included in Tier 2 capital for risk-based capital purposes is limited to 50.0% of Tier 1 capital.

The FDIC currently measures a bank's capital using the (1) total risk-based capital ratio, (2) Tier 1 risk-based capital ratio and (3) Tier 1 capital leverage ratio. The risk-based measures are based on ratios of qualifying capital to risk-weighted assets. To determine risk-weighted assets, assets are placed in one of five categories and given a percentage weight based on the relative risk of that category. In addition, certain off-balance-sheet items are converted to balance-sheet credit equivalent amounts, and each amount is then assigned to one of the five categories. In evaluating the adequacy of a bank's capital, the FDIC may also consider other factors that may affect the bank's financial condition, such as interest rate risk exposure, liquidity, funding and market risks, the quality and level of earnings, concentration of credit risk, risks arising from nontraditional activities, loan and investment quality, the effectiveness of loan and investment policies, and management's ability to monitor and control financial operating risks.

Prompt Corrective Action Regulations

Section 38 of the Federal Deposit Insurance Act establishes a framework of supervisory actions for insured depository institutions that are not adequately capitalized, also known as "prompt corrective action" regulations. All of the federal banking agencies have promulgated substantially similar regulations to implement a system of prompt corrective action. The framework for the type of supervisory action is based on a determination of a bank's capital category as follows:

- in order to be considered "well capitalized," a bank must have a total risk-based capital ratio of 10.0% or more, a Tier 1 risk-based capital ratio of 6.0% or more, a leverage capital ratio of 5.0% or more, and must not be subject to any written agreement, order or capital directive to meet and maintain a specific capital level for any capital measure;
- in order to be considered "adequately capitalized," a bank must have a total risk-based capital ratio of 8.0% or more, a Tier 1 risk-based capital ratio of 4.0% or more, and a leverage capital ratio of 4.0% or more (or, a leverage ratio of at

least 3.0% if the institution has a composite CAMELS (Capital adequacy, asset quality, management quality, earnings, liquidity and sensitivity to market risk) rating of 1 and is not experiencing or anticipating any significant growth);

- a bank is “undercapitalized” if it has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio that is less than 4.0%, or a leverage capital ratio that is less than 4.0% (or a leverage ratio of at least 3.0% under certain circumstances);

- a bank is “significantly undercapitalized” if it has a total risk-based capital ratio that is less than 6.0%, a Tier 1 risk-based capital ratio that is less than 3.0% or a leverage capital ratio that is less than 3.0%; and
- a bank is “critically undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%.

Additionally, a bank, based upon its capital levels, that is classified as “well capitalized,” “adequately capitalized” or “undercapitalized” may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for a hearing, determines that an unsafe or unsound condition, or an unsafe or unsound practice, warrants such treatment.

At each successive lower capital category, an insured bank is subject to increasingly severe supervisory actions. These actions include, but are not limited to, restrictions on asset growth, interest rates paid on deposits, branching, allowable transactions with affiliates, ability to pay bonuses and raises to senior executives and pursuing new lines of business. Additionally, all “undercapitalized” banks are required to implement capital restoration plans to restore capital to at least the “adequately capitalized” level, and the FDIC is generally required to close “critically undercapitalized” banks within a 90-day period.

Proposed Capital Regulations

The Dodd-Frank Act requires the federal banking regulators to issue new capital regulations. On June 12, 2012, federal banking regulators (including the FRB and the FDIC) jointly announced that they were seeking comment on three sets of proposed regulations relating to capital (the ”Proposed Rules”). The Proposed Rules would apply to both depository institutions and their holding companies. Although parts of the Proposed Rules would apply only to large, complex financial institutions, substantial portions of the Proposed Rules would apply to the Bank and the Company. The Proposed Rules include requirements contemplated by the Dodd-Frank Act as well as certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010, which standards are commonly referred to as “Basel III.”

Under the Proposed Rules, both the Bank and the Company would be required to meet certain minimum capital requirements. The Proposed Rules introduce a new capital ratio of common equity Tier 1 capital to risk-based assets. Common equity Tier 1 capital would consist of retained earnings and common stock instruments, subject to certain adjustments. Both the Company and the Bank would be required to meet a common equity Tier 1 capital ratio of 4.5% as well as a common equity Tier 1 capital “conservation buffer” of 2.5%. An institution that does not meet the conservation buffer would be subject to restrictions on certain activities including payment of dividends, stock repurchases and discretionary bonuses to executive officers. In addition, both the Company and the Bank would be subject to a Tier 1 leverage ratio of 4.0%, a Tier 1 risk-based ratio of 6.0% and a total risk-based ratio of 8.0%. The Prompt Corrective Action rules would be modified to include a common equity Tier 1 capital component and to increase certain other capital requirements for the various thresholds. For example, the requirements for the Bank to be considered well-capitalized would be a 5.0% Tier 1 leverage ratio, a 6.5% common equity Tier 1 risk-based capital ratio, an 8.0% Tier 1 risk-based ratio and a 10.0% total risk-based capital ratio. To be adequately capitalized, those ratios would be 4.0%, 4.5%, 6.0% and 8.0%, respectively.

The Proposed Rules would make changes in the methods of calculating certain risk-based assets, which would in turn affect the calculation of risk-based ratios. Higher or more sensitive risk weights would be assigned to various categories of assets, including residential mortgages, commercial real estate, credit facilities that finance the acquisition, development or construction of real property, certain exposures or credits that are 90 days past due or on nonaccrual, foreign exposures, certain corporate exposures and securitization exposures. In addition, the Proposed Rules would modify the manner in which certain capital elements are determined, including but not limited to, the phasing out of trust preferred securities as a component of Tier 1 capital and requiring certain deductions related to mortgage servicing rights and deferred tax assets.

The new required capital ratios and the enhanced Prompt Corrective Action rules would generally be phased in and would take full effect on January 1, 2015. The conservation buffer would be phased in beginning in 2016 and would take full effect on January 1, 2019. The new calculations of risk-weighted assets would take effect on January 1, 2015. Various other modifications may have later phase-in and full-implementation dates.

We cannot predict at this time when or in what form final rules will be adopted.

Limitations on Transactions with Affiliates

Transactions between the Bank and any affiliate are governed by Sections 23A and 23B of the Federal Reserve Act. An affiliate of the Bank is any company or entity which controls, is controlled by or is under common control with the Bank but which is not a subsidiary of the Bank. The Company and its non-bank subsidiaries are affiliates of the Bank. Generally, Section 23A limits the extent to which the Bank or its subsidiaries may engage in “covered transactions” with any one affiliate to an amount equal to 10.0% of the Bank's capital stock and surplus, and imposes an aggregate limit on all such transactions with all affiliates in an amount equal to 20.0% of such capital stock and surplus. Section 23B applies to “covered transactions” as well as certain other transactions and requires that all transactions be on terms substantially the same, or at least as favorable to the Bank, as those provided to a non-affiliate. The term “covered transaction” includes the making of loans to an affiliate, the purchase of or investment in the securities issued by an affiliate, the purchase of assets from an affiliate, the acceptance of securities issued by an affiliate as collateral security for a loan or extension of credit to any person or company, or the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

In addition, Sections 22(g) and (h) of the Federal Reserve Act place restrictions on loans, derivatives, repurchase agreements and securities lending to executive officers, directors and principal shareholders of the Bank and its affiliates.

Standards for Safety and Soundness

The federal banking regulatory agencies have prescribed, by regulation, a set of guidelines for all insured depository institutions prescribing safety and soundness standards. These guidelines establish general standards for internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings standards, compensation, fees and benefits. In general, the guidelines require appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines before capital becomes impaired. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal shareholder.

Each insured depository institution must implement a comprehensive written information security program that includes administrative, technical and physical safeguards appropriate to the institution's size and complexity and the nature and scope of its activities. The information security program also must be designed to ensure the security and confidentiality of customer information, protect against any unanticipated threats or hazards to the security or integrity of such information, protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer and ensure the proper disposal of customer and consumer information. Each insured depository institution must also develop and implement a risk-based response program to address incidents of unauthorized access to customer information in customer information systems. If the FDIC determines that the Bank fails to meet any standard prescribed by the guidelines, it may require the Bank to submit an acceptable plan to achieve compliance with the standard. The Bank maintains a program to meet the information security requirements and believes it is currently in compliance with this regulation.

Real Estate Lending Standards

FDIC regulations require the Bank to adopt and maintain written policies that establish appropriate limits and standards for real estate loans. These standards, which must be consistent with safe and sound banking practices, must establish loan portfolio diversification standards, prudent underwriting standards (including loan-to-value ratio limits) that are clear and measurable, loan administration procedures and documentation, approval and reporting requirements. The Bank is obligated to monitor conditions in its real estate markets to ensure that its standards continue to be appropriate for current market conditions. The Bank's board of directors is required to review and approve the Bank's standards at least annually.

The FDIC has published guidelines for compliance with these regulations, including supervisory limitations on loan-to-value ratios for different categories of real estate loans. Under the guidelines, the aggregate amount of all loans in excess of the supervisory loan-to-value ratios should not exceed 100.0% of total capital, and the total of all loans for commercial, agricultural, multifamily or other non-one-to-four family residential properties in excess of such ratios should not exceed 30.0% of total capital. Loans in excess of the supervisory loan-to-value ratio limitations must be identified in the Bank's records and reported at least quarterly to the Bank's board of directors.

Guidance on Real Estate Concentrations

On December 6, 2006, the federal banking agencies issued guidance on sound risk management practices for concentrations in commercial real estate lending. The particular focus is on exposure to commercial real estate loans that are dependent on the cash flow from the real estate held as collateral and that are likely to be sensitive to conditions in the commercial real estate market (as opposed to real estate collateral held as a secondary source of repayment or as an abundance of caution). The purpose of the guidance is not to limit a bank's commercial real estate lending but to guide banks in developing risk management practices and capital levels commensurate with the level and nature of real estate concentrations. The FDIC and other bank regulatory agencies may focus their supervisory resources on institutions that may have significant commercial real estate loan concentration risk. A bank that has experienced rapid growth in commercial real estate lending, has notable exposure to a specific type of commercial real estate loan or is approaching or exceeding the following supervisory criteria may be identified for further supervisory analysis with respect to real estate concentration risk:

Table of Contents

- total reported loans for construction, land development and other land represent 100.0% or more of the bank's risk-based capital; or
- total commercial real estate loans (as defined in the guidance) represent 300.0% or more of the bank's risk-based capital and the outstanding balance of the bank's commercial real estate loan portfolio has increased 50.0% or more during the prior 36 months.

The strength of an institution's lending and risk management practices with respect to such concentrations will be taken into account in supervisory evaluation of capital adequacy.

On March 17, 2008, the FDIC issued a release to re-emphasize the importance of strong capital and loan loss allowance levels and credit risk management practices for institutions with concentrated commercial real estate exposures. The FDIC stated that institutions with significant construction and development and commercial real estate loan concentrations should (1) increase or maintain strong capital levels, (2) ensure that loan loss allowances are appropriately strong, (3) manage construction and development and commercial real estate loan portfolios closely, (4) maintain updated financial and analytical information on their borrowers and collateral and (5) bolster the loan workout infrastructure.

Risk Retention

The Dodd-Frank Act requires that, subject to certain exemptions, securitizers of mortgage and other asset-backed securities retain not less than five percent of the credit risk of the mortgages or other assets. In April 2011, the federal banking regulators, together with the SEC, the Federal Housing Finance Agency and the Department of Housing and Urban Development, published proposed regulations implementing this requirement. Generally, the proposed regulations provide various ways in which the retention of risk requirement can be satisfied and also describe exemptions from the retention requirements for various types of assets, including mortgages. Final regulations have not been adopted.

Activities and Investments of Insured State-Chartered Financial Institutions

Federal law generally prohibits FDIC-insured state banks from engaging as a principal in activities, and from making equity investments, other than those that are permissible for national banks. An insured state bank is not prohibited from, among other things, (1) acquiring or retaining a majority interest in certain subsidiaries, (2) investing as a limited partner in a partnership the sole purpose of which is direct or indirect investment in the acquisition, rehabilitation or new construction of a qualified housing project, provided that such limited partnership investments may not exceed 2.0% of the bank's total assets, (3) acquiring up to 10.0% of the voting stock of a company that solely provides or reinsures directors', trustees' and officers' liability insurance coverage or bankers' blanket bond group insurance coverage for insured depository institutions and (4) acquiring or retaining the voting shares of a depository institution if certain requirements are met.

Washington State has enacted a law regarding financial institution parity. The law generally provides that Washington-chartered savings banks may exercise any of the powers of Washington-chartered commercial banks, national banks or federally-chartered savings banks, subject to the approval of the Director of the WDFI in certain situations.

Environmental Issues Associated With Real Estate Lending

The Comprehensive Environmental Response, Compensation and Liability Act, or the CERCLA, is a federal statute that generally imposes strict liability on all prior and present “owners and operators” of sites containing hazardous waste. However, Congress has acted to protect secured creditors by providing that the term “owner and operator” excludes a person whose ownership is limited to protecting its security interest in the site. Since the enactment of the CERCLA, this “secured creditor” exemption has been the subject of judicial interpretations which have left open the possibility that lenders could be liable for cleanup costs on contaminated property that they hold as collateral for a loan. To the extent that legal uncertainty exists in this area, all creditors, including the Bank, that have made loans secured by properties with potential hazardous waste contamination (such as petroleum contamination) could be subject to liability for cleanup costs, which costs often substantially exceed the value of the collateral property.

Reserves Requirements

The Bank is subject to Federal Reserve regulations pursuant to which depositary institutions may be required to maintain non-interest-earning reserves against their deposit accounts and certain other liabilities. Currently, reserves must be maintained against transaction accounts (primarily negotiable order of withdrawal and regular checking accounts). The regulations generally require that reserves be maintained in the amount of 3.0% of the aggregate of transaction accounts over $12.4 million up to $79.5 million in 2013 and 10% of the accounts over $79.5 million. Net transaction accounts up to $12.4 million are exempt from reserve requirements.

Table of Contents

Federal Home Loan Bank System

The Federal Home Loan Bank system consists of twelve regional Federal Home Loan Banks. Among other benefits, each of these serves as a reserve or central bank for its members within its assigned region. Each Federal Home Loan Bank is financed primarily from the sale of consolidated obligations of the Federal Home Loan Bank system. Each of the Federal Home Loan Banks makes available loans or advances to its members in compliance with the policies and procedures established by its board of directors. The Bank is a member of the Federal Home Loan Bank of Seattle ("FHLB"). As a member, the Bank is required to own stock in the FHLB and currently owns $36.4 million of stock in the FHLB. The Federal Housing Finance Agency (the “Finance Agency”) is the primary regulator of the FHLB, and the Finance Agency classified the FHLB as undercapitalized in August 2009. In October 2010, the FHLB entered into a Stipulation and Consent to The Issuance of a Consent Order with the Finance Agency, which sets forth requirements for capital management, asset composition and other operating and risk management improvements. In September 2012, the Finance Agency reclassified the FHLB as adequately capitalized but the FHLB remains subject to the Consent Order. As such, Finance Agency approval will continue to be required for all repurchases, redemptions, and dividend payments on capital stock.

Community Reinvestment Act of 1977

Banks are subject to the provisions of the CRA of 1977, which requires the appropriate federal bank regulatory agency to assess a bank's record in meeting the credit needs of the assessment areas serviced by the bank, including low and moderate income neighborhoods. The regulatory agency's assessment of the bank's record is made available to the public. Further, these assessments are considered by regulators when evaluating mergers, acquisitions and applications to open or relocate a branch or facility. The Bank currently has a rating of “Outstanding” under the CRA.

Dividends

Dividends from the Bank constitute an important source of funds for dividends that may be paid by the Company to shareholders. The amount of dividends payable by the Bank to the Company depends upon the Bank's earnings and capital position and is limited by federal and state laws. According to Washington law, the Bank may not declare or pay a cash dividend on its capital stock if this would cause its net worth to be reduced below the net worth requirements, if any, imposed by the WDFI. In addition, dividends on the Bank's capital stock may not be paid in an amount greater than its retained earnings without the approval of the WDFI.

The amount of dividends actually paid during any one period will be strongly affected by the Bank's policy of maintaining a strong capital position. Because the Bank is treated as a savings association subsidiary of a savings and loan holding company, it must give the Federal Reserve at least 30 days' advance notice of the proposed declaration of a dividend on its guaranty, permanent or other non-withdrawable stock. Federal law prohibits an insured depository institution from paying a cash dividend if this would cause the institution to be “undercapitalized,” as defined in the prompt corrective action regulations. Moreover, the federal bank regulatory agencies have the general authority to limit the dividends paid by insured banks if such payments are deemed to constitute an unsafe and unsound practice.

The Company had previously elected to defer the payment of interest on its outstanding TruPS, and therefore had been prohibited from declaring or paying dividends or distributions on, and from making liquidation payments with respect to, its common stock until it is current on all interest payments due. On March 12, 2013, the Federal Reserve approved the Company's request to make its interest payments current on its outstanding TruPS and the Company subsequently paid all deferred and current interest owed on its outstanding TruPS on March 15, 2013. However, the Company remains subject to a cease and desist order, which restricts the Company from making cash dividends or distributions to shareholders without regulatory consent.

Liquidity

The Bank is required to maintain a sufficient amount of liquid assets to ensure its safe and sound operation. See “Management's Discussion and Analysis - Liquidity Risk and Capital Resources.”

Compensation

The Bank is subject to regulation of its compensation practices. See “Regulation and Supervision - Regulation of the Company - Compensation Policies.”

Bank Secrecy Act and USA Patriot Act

18

The Company and the Bank are subject to the Bank Secrecy Act, as amended by the USA PATRIOT Act, which gives the federal government powers to address money laundering and terrorist threats through enhanced domestic security measures, expanded surveillance powers and mandatory transaction reporting obligations. By way of example, the Bank Secrecy Act imposes an affirmative obligation on the Bank to report currency transactions that exceed certain thresholds and to report other transactions determined to be suspicious.

Like all United States companies and individuals, the Company and the Bank are prohibited from transacting business with certain individuals and entities named on the Office of Foreign Asset Control's list of Specially Designated Nationals and Blocked Persons. Failure to comply may result in fines and other penalties. The Office of Foreign Asset Control ("OFAC") has issued guidance directed at financial institutions in which it asserted that it may, in its discretion, examine institutions determined to be high-risk or to be lacking in their efforts to comply with these prohibitions.

The Bank maintains a program to meet the requirements of the Bank Secrecy Act, USA PATRIOT Act and OFAC and believes it is currently in compliance with these requirements.

Identity Theft

Section 315 of the Fair and Accurate Credit Transactions Act ("FACT Act") requires each financial institution or creditor to develop and implement a written Identity Theft Prevention Program to detect, prevent and mitigate identity theft "red flags" in connection with the opening of certain accounts or certain existing accounts.

The Bank maintains a program to meet the requirements of Section 315 of the FACT Act and believes it is currently in compliance with these requirements.

Consumer Protection Laws and Regulations

The Bank and its affiliates are subject to a broad array of federal and state consumer protection laws and regulations that govern almost every aspect of its business relationships with consumers. While this list is not exhaustive, these include the Truth-in-Lending Act, the Truth in Savings Act, the Electronic Fund Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Secure and Fair Enforcement in Mortgage Licensing Act, the Real Estate Settlement Procedures Act, the Home Mortgage Disclosure Act, the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, the Service Members' Civil Relief Act, the Right to Financial Privacy Act, the Home Ownership and Equity Protection Act, the Consumer Leasing Act, the Fair Credit Billing Act, the Homeowners Protection Act, the Check Clearing for the 21st Century Act, laws governing flood insurance, laws governing consumer protections in connection with the sale of insurance, federal and state laws prohibiting unfair and deceptive business practices, foreclosure laws and various regulations that implement some or all of the foregoing. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, collecting loans and providing other services. Failure to comply with these laws and regulations can subject the Bank to various penalties, including but not limited to, enforcement actions, injunctions, fines, civil liability, criminal penalties, punitive damages and the loss of certain contractual rights. The Bank has a compliance governance structure in place to help ensure its compliance with these requirements.

The Dodd-Frank Act established the CFPB as a new independent bureau within the Federal Reserve system that is responsible for regulating consumer financial products and services under federal consumer financial laws. The CFPB has broad rulemaking authority with respect to these laws and exclusive examination and primary enforcement authority with respect to banks with assets of $10 billion or more.

The Dodd-Frank Act also contains a variety of provisions intended to reform consumer mortgage practices. The provisions include (1) a requirement that lenders make a determination that at the time a residential mortgage loan is consummated the consumer has a reasonable ability to repay the loan and related costs, (2) a ban on loan originator compensation based on the interest rate or other terms of the loan (other than the amount of the principal), (3) a ban on prepayment penalties for certain types of loans, (4) bans on arbitration provisions in mortgage loans and (5) requirements for enhanced disclosures in connection with the making of a loan. The Dodd-Frank Act also imposes a variety of requirements on entities that service mortgage loans.

The Dodd-Frank Act contains provisions further regulating payment card transactions. The Dodd-Frank Act required the Federal Reserve to adopt regulations limiting any interchange fee for a debit transaction to an amount which is "reasonable and proportional" to the costs incurred by the issuer. The Federal Reserve has adopted final regulations limiting the amount of debit interchange fees that large bank issuers may charge or receive on their debit card transactions. There is an exemption from the rules for issuers with assets of less than $10 billion and the Federal Reserve has stated that it will monitor and report to

Table of Contents

Congress on the effectiveness of the exemption. Nevertheless, it is unclear whether such smaller issuers (which include the Bank) will, as a practical matter, be able to avoid the impact of the regulations.
Several of the CFPB rules were issued in January 2013, and we continue to analyze their requirements to determine the impact of the rules to our businesses. During 2013, we expect the CFPB to focus its rulemaking efforts on integrating disclosure requirements for lenders and settlement agents and expanding the scope of information lenders must report in connection with mortgage and other housing-related loan applications.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") implemented a broad range of corporate governance and accounting measures to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of disclosures under federal securities laws. We are subject to Sarbanes-Oxley because we are required to file periodic reports with the SEC under the Securities Exchange Act of 1934. Among other things, Sarbanes-Oxley and/or its implementing regulations established membership requirements and additional responsibilities for our audit committee, imposed restrictions on the relationship between us and our outside auditors (including restrictions on the types of non-audit services our auditors may provide to us), imposed additional responsibilities for our external financial statements on our chief executive officer and chief accounting officer, expanded the disclosure requirements for our corporate insiders, required our management to evaluate our disclosure controls and procedures and our internal control over financial reporting, and required our independent registered public accounting firm to issue a report on our internal control over financial reporting.

Future Legislation or Regulation

In light of recent conditions in the United States economy and the financial services industry, the Obama administration, Congress, the regulators and various states continue to focus attention on the financial services industry. Additional proposals that affect the industry have been and will likely continue to be introduced. We cannot predict whether any of these proposals will be enacted or adopted or, if they are, the effect they would have on our business, our operations or our financial condition.

Table of Contents

ITEM 1A RISK FACTORS

This Annual Report on Form 10-K contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this report.

We have in the past and may again in the future be subject to certain specific regulatory constraints on the activities of the Bank and the Company, which could result in us not being as profitable as banks that are not subject to such conditions.

Between 2009 and 2012, both the Bank and the Company operated under specific regulatory restrictions on their operations. These restrictions were intended to preserve and strengthen the Bank's capital adequacy and improve its asset quality, among other things, and limited our ability to pay cash dividends or to renew or incur debt. The Company remains subject to a cease and desist order imposed on May 8, 2009. The Bank operated under a cease and desist order from May 8, 2009 until March 26, 2012, when that order was replaced with a MOU. On December 27, 2012, the FDIC determined that the MOU was no longer necessary and, as a result, terminated the MOU. However, we cannot offer assurances that we can avoid the adverse conditions that caused us to fall below desirable performance levels, and if that were to happen, we may again become subject to more stringent regulatory orders and other regulatory enforcement actions. Further, while we believe that the Company Order will be lifted, we cannot assure that it will be lifted or when it will be lifted.

We have incurred substantial losses in the recent past and we cannot assure you that we will remain profitable.

We sustained significant losses in the past and we cannot assure that we will remain profitable in the future. Our ability to remain profitable depends primarily on our ability to originate loans and either sell them into the secondary market or hold them in our loan portfolio and collect interest and principal as they come due. When loans become nonperforming or their ultimate collection is in doubt, our income is adversely affected.

HomeStreet is restricted from paying cash dividends under current regulatory orders.

Although the FDIC and the Washington Department of Financial Institutions have terminated both the cease and desist order and the MOU that formerly applied to the Bank, the Company remains subject to a cease and desist order which restricts the Company from, among other things, paying cash dividends or making distributions to shareholders without regulatory approval. As a result, we may not be able to declare or pay dividends on our common stock in the near future unless we are able to get the requisite regulatory approval or the cease and desist order is terminated. Additionally, federal banking regulators are in the process of increasing capital requirements on banks and bank savings and holding companies, and any such increase may have the effect of reducing our ability to pay dividends even if this existing restriction may otherwise have been alleviated.

Difficult market conditions have adversely affected and may continue to have an adverse effect on our business.

During the period from early 2008 through most of 2011, the United States economy in general, and the financial institutions sector in particular, experienced a severe downturn owing to a number of factors that affected virtually every aspect of our business. While these conditions appear to have moderated, considerable uncertainty continues to affect our business, and thus raises significant risk as to our ability to maintain profitability.

In particular, we may face risks related to market conditions that may negatively impact our business opportunities and plans, such as:

•

- uncertainty related to increased regulation and aggressive governmental enforcement in the financial sector generally and the mortgage banking business specifically, including increased costs of compliance;
- the models we use to assess the creditworthiness of our customers may prove less reliable than we had anticipated in predicting future behaviors which may impair our ability to make good underwriting decisions;
- challenges in accurately estimating the ability of our borrowers to repay their loans if our forecasts of economic conditions and other economic predictions are not accurate;
- further increases in FDIC insurance premiums due to additional depletion of that agency's insurance funds;
- restrictions in our ability to engage in routine funding transactions due to the commercial soundness of other financial institutions and government sponsored entities ("GSEs"); and
- uncertainty regarding future political developments and fiscal policy.

If recovery from the economic recession slows or if we experience another recessionary dip, our ability to access capital and our business, financial condition and results of operations may be adversely impacted.

Table of Contents

A change in federal monetary policy could adversely impact our mortgage banking revenues.

In September 2012, the Federal Reserve Board's Oversight Management Committee expanded its standing monetary policy, known as “quantitative easing,” to provide for a purchases by the Federal Reserve of up to $40 billion per month of mortgage-backed securities in the secondary market. This program, which is intended to bolster the U.S. economy by retaining relatively low interest rates to promote increased spending, was adopted in 2008 and originally provided for the repurchase of only treasury securities. The inclusion of mortgage-backed securities was intended to have the effect of maintaining historically low mortgage interest rates. Because a substantial portion of our revenues and our net income historically have been, and in the foreseeable future are expected to be, derived from gain on the origination and sale of mortgage loans and on the continuing servicing of those loans, the Federal Reserve's policy may have had, and in the future may continue to have, the effect of supporting higher revenues than might otherwise be available. Contrarily, a reduction in or termination of this policy, absent a significant rebound in employment and real wages, would likely reduce mortgage originations throughout the United States, including ours. Such an event could likely reduce our mortgage origination revenues, which could have a material adverse impact upon our business.

An important information technology systems provider was recently identified as having internal control deficiencies, which could give rise to significant risks to the Bank and the Company.

In the first quarter of 2012, we were notified that the provider of one of the Bank's critical information technology and transaction processing systems was identified as posing a significant risk to banking operations for that vendor's clients. That vendor has been criticized for, among other things, an unsatisfactory risk management system, the lack of a compliance culture and a lack of internal controls. That vendor has encountered a significant cyberattack and related computer fraud, and there have been indications that in the absence of a prompt remediation of known and unknown deficiencies, that vendor's systems may create enhanced risk for users.

The Bank does not use this system that was the subject of the cyberattack; however, the Bank uses this vendor for a wide variety of important functions, and given their progress in remediating these issues, and subject to the vendor's continued progress, we have plans to increase our reliance on this vendor and its products and services. Our Board of Directors, as well as the Bank’s Board of Directors, were briefed on this development and provided quarterly updates on the vendor's Matter Requiring Attention ("MRA") remediation efforts. At December 31, 2012, all but one of the outstanding MRA actions have been completed by the vendor. Banking regulators are assessing the effectiveness of the MRA activities. If these concerns have not been addressed effectively, the Bank could experience a number of potentially materially adverse consequences, including:

- greater than normal exposure to compliance problems, which could lead to adverse regulatory actions, including potential enforcement actions;
- the need to replace one or more of our information systems providers, which could lead to increased costs, disruptions in our relationships with one or more customers, management distractions, and other difficulties;
- potential claims by customers, including class action claims, resulting from actual or alleged compromises of consumer or business financial information;
- difficulties in maintaining an adequate system of internal controls and procedures and internal control over financial reporting;
- the loss of confidence of one or more of our customers, or reputational harm associated with the use of these systems, particularly if our customers experience actual difficulties, losses or attacks; and
- a dispute with this vendor over the adequacy of the products and services for which we contracted, potentially including increases in legal fees and other litigation costs.

A failure in or breach of our security systems or infrastructure, or those of our third party vendors and other service providers, resulting from cyber-attacks, could disrupt our businesses, result in the disclosure or misuse of confidential or proprietary information, damage our reputation, increase our costs and cause losses.

Information security risks for financial institutions have generally increased in recent years in part because of the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists, activists, and other external parties. Those parties also may attempt to fraudulently induce employees, customers, or other users of our systems to disclose confidential information in order to gain access to our data or that of our customers. Our operations rely on the secure processing, transmission and storage of confidential information in our computer systems and networks, either managed directly by us or through our data processing vendors. In addition, to access our products and services, our customers may use personal smartphones, tablet PC's, and other mobile devices that are beyond our control systems. Although we believe we have robust information security procedures and controls, our technologies, systems, networks, and our customers' devices may become the target of cyber-attacks or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of Company or our customers' confidential, proprietary and other information, or otherwise disrupt the Company's or its customers' or other third parties' business operations.

Third parties with which we do business or that facilitate our business activities, including exchanges, clearing houses, financial intermediaries or vendors that provide services or security solutions for our operations, could also be sources of operational and information security risk to us, including from breakdowns or failures of their own systems or capacity constraints.

To date we have not experienced any material losses relating to cyber-attacks or other information security breaches, but there can be no assurance that we will not suffer such attacks and losses in the future. Our risk and exposure to these matters remains heightened because of, among other things, the evolving nature of these threats, our plans to continue to implement our Internet banking and mobile banking channel, our expanding operations and the outsourcing of a significant portion of our business operations. As a result, cybersecurity and the continued development and enhancement of our controls, processes and practices designed to protect customer information, our systems, computers, software, data and networks from attack, damage or unauthorized access remain a priority for the Company. As cyber threats continue to evolve, we may be required to expend significant additional resources to insure, to continue to modify or enhance our protective measures or to investigate and remediate important information security vulnerabilities.

Disruptions or failures in the physical infrastructure or operating systems that support our businesses and customers, or cyber-attacks or security breaches of the networks, systems or devices that our customers use to access our products and services could result in customer attrition, financial losses, the inability of our customers to transact business with us, violations of applicable privacy and other laws, regulatory fines, penalties or intervention, reputational damage, reimbursement or other compensation costs, and/or additional compliance costs, any of which could materially and adversely affect our results of operations or financial condition.

A substantial portion of our revenue is derived from residential mortgage lending which is a market sector that has experienced significant volatility.

A substantial portion of our consolidated net revenues (net interest income plus noninterest income) are derived from originating and selling residential mortgages. Residential mortgage lending in general has experienced substantial volatility in recent years. Moreover, a significant increase in interest rates may materially and adversely affect both our loan origination volume and the value of the collateral securing our outstanding loans, may increase rates of borrower default, and may otherwise adversely affect our business.

The significant concentration of real estate secured loans in our portfolio has had and may continue to have a negative impact on our asset quality and profitability.

Substantially all of our loans are secured by real property. Our real estate secured lending is generally sensitive to national, regional and local economic conditions, making loss levels difficult to predict. Declines in real estate sales and prices, significant increases in interest rates, and a degeneration in prevailing economic conditions may result in higher than expected loan delinquencies, foreclosures, problem loans, OREO, net charge-offs and provisions for credit and OREO losses. Although real estate prices have recently stabilized in markets in which we operate, if market values decline, the collateral for our loans may provide less security and our ability to recover the principal, interest and costs due on defaulted loans by selling the underlying real estate will be diminished, leaving us more likely to suffer additional losses on defaulted loans. Such declines may have a greater effect on our earnings and capital than on the earnings and capital of financial institutions whose loan portfolios are more geographically diversified.

Worsening conditions in the real estate market and higher than normal delinquency and default rates on loans could cause other adverse consequences for us, including:

- the reduction of cash flows and capital resources, as we are required to make cash advances to meet contractual obligations to investors, process foreclosures, and maintain, repair and market foreclosed properties;
- declining mortgage servicing fee revenues because we recognize these revenues only upon collection;
- increasing loan servicing costs;
- declining fair value on our mortgage servicing rights; and

Table of Contents

- declining fair values and liquidity of securities held in our investment portfolio that are collateralized by mortgage obligations.

Our allowance for loan losses may prove inadequate or we may be negatively affected by credit risk exposures. Future additions to our allowance for loan losses will reduce our earnings.

Our business depends on the creditworthiness of our customers. As with most financial institutions, we maintain an allowance for loan losses to provide for defaults and nonperformance, which represents management's best estimate of probable incurred losses inherent in the loan portfolio. Management's estimate is the result of our continuing evaluation of specific credit risks and loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions, industry concentrations and other factors that may indicate future loan losses. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and judgment and requires us to make estimates of current credit risks and future trends, all of which may undergo material changes. Generally, our nonperforming loans and OREO reflect operating difficulties of individual borrowers and weaknesses in the economies of the markets we serve. This allowance may not be adequate to cover actual losses, and future provisions for losses could materially and adversely affect our financial condition, results of operations and cash flows.

We may incur significant losses as a result of ineffective hedging of interest rate risk related to our loans sold with a reservation of servicing rights.

The value our single family mortgage servicing rights (“MSRs”) changes with fluctuations in interest rates, among other things, reflecting the changing expectations of mortgage prepayment activity. To mitigate potential losses of fair value of single family MSRs related to changes in interest rates, we actively hedge this risk with derivative financial instruments. Hedging is a complex process, requiring sophisticated models, experienced and skilled personnel and continual monitoring. Changes in the value of our hedging instruments may not correlate with changes in the value of our single family MSRs, and we could incur a net valuation loss as a result of our hedging activities. Following the expansion of our single family mortgage operations in early 2012 through the addition of a significant number of single family mortgage origination personnel, the volume of our MSRs has increased. The increase in volume in turn increases our exposure to the risks associated with the impact of interest rate fluctuations on MSRs.

The fair value of our single family loans held for sale is subject to substantial interest rate risk.

A substantial portion of our single family loans are sold into the secondary market. We are exposed to the risk of decreases in the fair value of our single family loans held for sale as a result of changes in interest rates. We use derivative financial instruments to hedge this risk; however our hedging strategies, techniques and judgments may not be effective and may not anticipate every event that would affect the fair value of our single family loans held for sale. Our inability to effectively reduce the risk of fluctuations in the fair value of our single family loans could negatively affect our results of operations due to decreases in the fair value of these assets.

Our real estate lending also exposes us to environmental liabilities.

In the course of our business, it is necessary to foreclose and take title to real estate, which could subject us to environmental liabilities with respect to these properties. Hazardous substances or waste, contaminants, pollutants or sources thereof may be discovered on properties during our ownership or after a sale to a third party. We could be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances or chemical releases at such properties. The costs associated with investigation or remediation activities could be substantial and could substantially exceed the value of the real property. In addition, as the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. We may be unable to recover costs from any third party. These occurrences may materially reduce the value of the affected property, and we may find it difficult or impossible to use or sell the property prior to or following any environmental remediation. If we ever become subject to significant environmental liabilities, our business, financial condition and results of operations could be materially and adversely affected.

If we breach any of the representations or warranties we make to a purchaser when we sell mortgage loans, we may be liable to the purchaser for unpaid principal and interest on the loan.

Table of Contents

When we sell mortgage loans in the ordinary course of business, we are required to make certain representations and warranties to the purchaser about the mortgage loans and the manner in which they were originated. Our loan sale agreements require us to repurchase mortgage loans if we have breached any of these representations or warranties, in which case we may be required to repurchase such loan and record a loss upon repurchase and/or bear any subsequent loss on the loan. We may not have any remedies available to us against a third party for such losses, or the remedies available to us may not be as broad as the remedies available to the purchaser of the mortgage loan against us. In addition, if there are remedies against a third party available to us, we face further risk that such third party may not have the financial capacity to perform remedies that otherwise may be available to us. Therefore, if a purchaser enforces remedies against us, we may not be able to recover our losses from a third party and may be required to bear the full amount of the related loss. If repurchase and indemnity demands increase, our liquidity, results of operations and financial condition will be adversely affected.

If we breach any representations and warranties or fail to follow guidelines when originating a FHA/HUD-insured loan or a VA-guaranteed loan, we may lose the insurance or guarantee on the loan and suffer losses and/or pay penalties.

We originate and purchase, sell and thereafter service single family loans that are insured by FHA/HUD or guaranteed by the VA. We certify to the FHA/HUD and the VA that the loans meet their requirements and guidelines. The FHA/HUD and VA audit loans that are insured or guaranteed under their programs, including audits of our processes and procedures as well as individual loan documentation. Violations of guidelines can result in monetary penalties or require us to provide indemnifications against loss or loans declared ineligible for their programs. In the past, monetary penalties and losses from indemnifications have not created material losses to the Bank. As a result of the housing crisis, the FHA/HUD has stepped up enforcement initiatives. In addition to regular FHA/HUD audits, HUD's Inspector General has become active in enforcing FHA regulations with respect to individual loans and has partnered with the Department of Justice ("DOJ") in filing lawsuits against lenders for systemic violations. The penalties resulting from such lawsuits can be much more severe, since systemic violations can be applied to groups of loans and penalties may be subject to treble damages. The DOJ has used the Federal False Claims Act in prosecuting these lawsuits. Because of our significant origination of FHA/HUD insured and VA guaranteed loans, if the DOJ were to find potential violations by the Bank, we could be subject to material monetary penalties and/or losses, and may even be subject to lawsuits alleging systemic violations which could result in treble damages.

We may face risk of loss if we purchase loans from a seller that fails to satisfy its indemnification obligations.

We generally receive representations and warranties from the originators and sellers from whom we purchase loans and servicing rights such that if a loan defaults and there has been a breach of such representations and warranties, we may be able to pursue a remedy against the seller of the loan for the unpaid principal and interest on the defaulted loan. However, if the originator and/or seller breach such representations and warranties and does not have the financial capacity to pay the related damages, we may be subject to the risk of loss for such loan as the originator or seller may not be able to pay such damages or repurchase loans when called upon by us to do so. Currently, we only purchase loans from Windermere Mortgage Services Series LLC, an affiliated business arrangement with certain Windermere real estate brokerage franchise owners.

The proposed restructuring of Fannie Mae and Freddie Mac and changes in existing government-sponsored and federal mortgage programs could negatively affect our business.

We originate and purchase, sell and thereafter service single family and multifamily mortgages under the Fannie Mae, and to a lesser extent the Freddie Mac, single family purchase programs and the Fannie Mae multifamily DUS program. Since the nationwide downturn in residential mortgage lending that began in 2007 and the placement of Fannie Mae and Freddie Mac into conservatorship, Congress and various executive branch agencies have offered a wide range of proposals aimed at restructuring these agencies. None of these proposals have yet been defined with any specificity, and so we cannot predict how any such initiative would impact our business. However, any restructuring of Fannie Mae and Freddie Mac that restricts their loan purchase programs may have a material adverse effect on our business and results of operations. Moreover, we have recorded on our balance sheet an intangible asset (mortgage servicing rights, or MSRs) relating to our right to service single and multifamily loans sold to Fannie Mae and Freddie Mac. That MSR asset was valued at $95.5 million at December 31, 2012. Changes in Fannie Mae's and Freddie Mac's policies and operations that adversely affect our single family residential loan and DUS mortgage servicing assets may require us to record impairment charges to the value of these assets, and significant impairment charges could be material and adversely affect our business.

Through our wholly owned subsidiary HomeStreet Capital Corporation, we participate as a lender in the DUS program. Fannie Mae delegates responsibility for originating, underwriting and servicing mortgages, and we assume a limited portion of the risk of loss during the remaining term on each commercial mortgage loan that we sell to Fannie Mae. In the year ended December 31, 2012 we originated $112.1 million in loans through the DUS program.

Table of Contents

Fannie Mae and Freddie Mac are under conservatorship with the Federal Housing Finance Agency. On February 11, 2011, the Obama administration presented Congress with a report titled “Reforming America's Housing Finance Market, A Report to Congress,” outlining its proposals for reforming America's housing finance market with the goal of scaling back the role of the U.S. government in, and promoting the return of private capital to, the mortgage markets and ultimately winding down Fannie Mae and Freddie Mac. Without mentioning a specific time frame, the report calls for the reduction of the role of Fannie Mae and Freddie Mac in the mortgage markets by, among other things, reducing conforming loan limits, increasing guarantee fees and requiring larger down payments by borrowers. The report presents three options for the long-term structure of housing finance, all of which call for the unwinding of Fannie Mae and Freddie Mac and a reduced role of the government in the mortgage market. In August 2012, the Treasury Department entered into amendments to its senior preferred stock purchase agreements with each of Fannie Mae and Freddie Mac that require those agencies to reduce the amount of mortgage assets they hold, setting a cap of $650 billion for December 31, 2012 and requiring a decrease of at least 15% per year for each year thereafter, to a minimum of $250 billion, as a step toward winding down those agencies. We cannot be certain if or when Fannie Mae and Freddie Mac ultimately will be wound down, if or when additional reform of the housing finance market will be implemented or what the future role of the U.S. government will be in the mortgage market, and, accordingly, we will not be able to determine the impact that any such reform may have on us until a definitive reform plan is adopted.

In addition, our ability to generate income through mortgage sales to institutional investors depends in part on programs sponsored by Fannie Mae, Freddie Mac and Ginnie Mae, which facilitate the issuance of mortgage-backed securities in the secondary market. Any discontinuation of, or significant reduction in, the operation of those programs could have a material adverse effect on our loan origination and mortgage sales as well as our results of operations. Also, any significant adverse change in the level of activity in the secondary market or the underwriting criteria of these entities could negatively impact our results of business, operations and cash flows. Further, the Dodd-Frank Act imposes a requirement that private securitizers of mortgage and other asset backed securities retain, subject to certain exemptions, not less than five percent of the credit risk of the mortgages or other assets backing the securities.

The lending qualification and limits of FHA and VA may also be subject to changes that may limit our origination of loans guaranteed or insured by the agencies in the future.

A significant portion of our residential mortgage origination volume is derived from FHA and VA lending programs. FHA loan limits increased from $506,000 to $567,500 effective November 2011 in our primary markets in King, Pierce and Snohomish Counties, substantially above the limit of $417,000 that existed prior to February 2009. FHA loan limits also increased for other markets in which we operate. The FHA mutual mortgage insurance premiums changed in June 2012, with the premium collected at closing or financed in the loan amount increasing from 1.00% to 1.75%, while the annual premium increased from 1.15% to 1.25%. As a result, conventional financing has become more affordable and more attractive relative to FHA financing for high loan-to-value borrowers who can afford the 5.0% minimum down payment required for conventional loans.

Fluctuations in interest rates could adversely affect the value of our assets and reduce our net interest income and noninterest income thereby adversely affecting our earnings and profitability.

Our earnings are highly dependent on the difference between the interest earned on loans and investments and the interest paid on deposits and borrowings. Changes in market interest rates impact the rates earned on loans and investment securities and the rates paid on deposits and borrowings. In addition, changes to market interest rates may impact the level of loans, deposits and investments and the credit quality of existing loans. Changes in interest rates also affect demand for our residential loan products and the revenue realized on the sale of loans. A decrease in the volume of loans sold can decrease our revenues and net income. These rates may be affected by many factors beyond our control, including general and economic conditions and the monetary and fiscal policies of various governmental and regulatory authorities. Changes in interest rates may negatively impact our ability to attract deposits, make loans and achieve satisfactory interest rate spreads, which could adversely affect our financial condition or results of operations. Changes in interest rates may reduce our mortgage revenues, which would negatively impact our noninterest income.

Our securities portfolio includes securities that are insured or guaranteed by U.S. government agencies or government-sponsored enterprises and other securities that are sensitive to interest rate fluctuations. The unrealized gains or losses in our available-for-sale portfolio are reported as a separate component of shareholders' equity until realized upon sale. As a result, future interest rate fluctuations may impact shareholders' equity, causing material fluctuations from quarter to quarter. Failure to hold our securities until maturity or until market conditions are favorable for a sale could adversely affect our financial condition.

A significant portion of our noninterest income is derived from originating residential mortgage loans and selling them into the secondary market. That business has benefited from a long period of historically low interest rates. To the extent interest rates rise, particularly if they rise substantially or quickly, we may experience a reduction in mortgage refinancing and financing of new home purchases. These factors may negatively affect our mortgage loan origination volume and adversely affect our noninterest income.

Our mortgage servicing rights carry interest rate risk because the total amount of servicing fees earned, as well as changes in fair-market value, fluctuate based on expected loan prepayments (affecting the expected average life of a portfolio of residential mortgage servicing rights). The rate of prepayment of residential mortgage loans may be influenced by changing national and regional economic trends, such as recessions or depressed real estate markets, as well as the difference between interest rates on existing residential mortgage loans relative to prevailing residential mortgage rates. Changes in prepayment rates are therefore difficult for us to predict. An increase in the general level of interest rates may adversely affect the ability of some borrowers to pay the interest and principal of their obligations. During periods of declining interest rates, many residential borrowers refinance their mortgage loans. The loan administration fee income related to the residential mortgage loan servicing rights corresponding to a mortgage loan deceases as mortgage loans are prepaid. Consequently, the fair value of portfolios of residential mortgage loan servicing rights tend to decrease during periods of declining interest rates, because greater prepayments can be expected and, as a result, the amount of loan administration income received also decreases.

We may be required to recognize impairment with respect to investment securities, including the FHLB stock we hold.

Our securities portfolio currently includes securities with unrecognized losses. We may continue to observe declines in the fair market value of these securities. We evaluate the securities portfolio for any other than temporary impairment each reporting period. In addition, as a condition of membership in the FHLB, we are required to purchase and hold a certain amount of FHLB stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB. Our FHLB stock is carried at cost and is subject to recoverability testing under applicable accounting standards. Future negative changes to the financial condition of the FHLB may require us to recognize an impairment charge with respect to such holdings. The FHLB is currently subject to a Consent Order issued by its primary regulator, the Federal Housing Finance Agency.

We are subject to extensive regulation that has restricted and could further restrict our activities, including capital distributions, and impose financial requirements or limitations on the conduct of our business.

Our operations are subject to extensive regulation by federal, state and local governmental authorities, including the FDIC, the WDFI and the Federal Reserve, 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 and regulations to which we are subject are evolving and change frequently. Changes to those laws, rules and regulations are also sometimes retroactively applied. Furthermore, the on-site examination cycle for an institution in our circumstances is frequent and extensive. Examination findings by the regulatory agencies may result in adverse consequences to the Company or the Bank. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the authority to restrict our operations, adversely reclassify our assets, determine the level of deposit premiums assessed and require us to increase our allowance for loan losses.

New legislation, case law or regulatory action regarding foreclosures, forced mortgage principal reduction, or bankruptcy laws may negatively impact our business.

Recently, new legislation, case law and regulations have been proposed and enacted, and courts have issued decisions in recent cases carrying precedential weight in areas we conduct business which, among other things, could allow judges to modify the terms of residential mortgages in bankruptcy proceedings and could hinder our ability to foreclose promptly on defaulted mortgage loans or expand assignee liability for certain violations in the mortgage loan origination process, any or all of which could adversely affect our business or result in our being held responsible for violations in the mortgage loan origination process. Congress and various regulatory authorities have proposed programs that would require a reduction in principal balances of "underwater" residential mortgages, which if implemented would tend to reduce loan servicing income and which might adversely affect the carrying values of portfolio loans. These legislative and regulatory proposals generally have focused primarily, if not exclusively, on residential mortgage origination, but we cannot offer assurances as to which, if any, of these initiatives may be adopted or, if adopted, to what extent they would affect our business. Any such initiatives may limit our ability to take actions that may be essential to preserve the value of the mortgage loans we service or hold for investment. Any restriction on our ability to foreclose on a loan, any requirement that we forego a portion of the amount otherwise due on a loan or any requirement that we modify any original loan terms may require us to advance principal, interest, tax and insurance payments, which would negatively impact our business, financial condition, liquidity and results of operations. Given the relatively high percentage of our business that derives from originating residential mortgages, any such actions are likely to

Table of Contents

have a significant impact on our business, and the effects we experience will likely be disproportionately high in comparison to financial institutions whose residential mortgage lending is more attenuated.

In addition, recent court cases in Oregon and Washington have challenged whether Mortgage Electronic Registration Systems, Inc. (“MERS”) meets the statutory definition of deed of trust beneficiary under applicable state laws. Based on decisions handed down by courts in Oregon, we and other servicers of MERS related loans have elected to foreclose through judicial procedures in Oregon, resulting in increased foreclosure costs, longer foreclosure timelines and additional delays. If the Oregon case law is upheld on appeal, and/or if the Washington courts issue a similar decision in the cases pending before them, our foreclosure costs and foreclosure timelines may continue to increase, which in turn, could increase our single family loan delinquencies and adversely affect our cost of doing business and results of operations.

We are unable to predict whether U.S. federal, state or local authorities, or other pertinent bodies, will enact legislation, laws, rules, regulations, handbooks, guidelines or similar provisions that will affect our business or require changes in our practices in the future, and any such changes could adversely affect our cost of doing business and profitability. See “Regulation and Supervision - Regulation and Supervision of HomeStreet Bank” in Item 1 of this Form 10-K.

The Dodd-Frank Act is expected to increase our costs of operations and may have a material negative effect on us.

The Dodd-Frank Act significantly changes the laws as they apply to financial institutions and revises and expands the rulemaking, supervisory and enforcement authority of federal banking regulators. It is also expected to have a material impact on our relationships with current and future customers.

Some of these changes are effective immediately, though many are being phased in gradually. In addition, the statute in many instances calls for regulatory rulemaking to implement its provisions, not all of which have been completed, so the precise contours of the law and its effects on us cannot yet be fully understood. The provisions of the Dodd-Frank Act and the subsequent exercise by regulators of their revised and expanded powers thereunder could materially and negatively impact the profitability of our business, the value of assets we hold or the collateral available for our loans, require changes to business practices or force us to discontinue businesses and expose us to additional costs, taxes, liabilities, enforcement actions and reputational risk. See “Regulation and Supervision” in Item 1 of this Form 10-K.

We will be subject to more stringent capital requirements.

On June 12, 2012, the U.S. federal banking regulators (including the Federal Reserve and FDIC) jointly announced that they were seeking comment on three sets of proposed regulations relating to capital (the “Proposed Rules”), a substantial portion of which would apply to the Bank and the Company. The Proposed Rules include requirements contemplated by the Dodd-Frank Act as well as certain standards initially adopted by the Basel Committee on Banking Supervision, which standards are commonly referred to as “Basel III.”

The strength and stability of other financial institutions may adversely affect our business.

Our counterparty risk exposure is affected by the actions and creditworthiness of other financial institutions with which we do business. Negative impacts to our counterparty financial institutions could affect our ability to engage in routine funding transactions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. Many of these types of transactions can expose us to credit risk in the event of default by a direct or indirect counterparty or client.

If other financial institutions in our markets dispose of real estate collateral at below-market or distressed prices, such actions may increase our losses and have a material adverse effect our financial condition and results of operations.

Our accounting policies and methods are fundamental to how we report our financial condition and results of operations, and we use estimates in determining the fair value of certain of our assets, which estimates may prove to be imprecise and result in significant changes in valuation.

A portion of our assets are carried on the balance sheet at fair value, including investment securities available for sale, mortgage servicing rights related to single family loans and single family loans held for sale. Generally, for assets that are reported at fair value, we use quoted market prices or internal valuation models that utilize observable market data inputs to estimate their fair value. In certain cases, observable market prices and data may not be readily available or their availability may be diminished due to market conditions. We use financial models to value certain of these assets. These models are complex and use asset-specific collateral data and market inputs for interest rates. Although we have processes and procedures in place governing internal valuation models and their testing and calibration, such assumptions are complex as we must make judgments about the effect of matters that are inherently uncertain. Different assumptions could result in significant changes in valuation, which in turn could affect earnings or result in significant changes in the dollar amount of assets reported on the balance sheet.

Our operations could be interrupted if our third-party service and technology providers experience difficulty, terminate their services or fail to comply with banking regulations

We depend, and will continue to depend, to a significant extent, on a number of relationships with third-party service and technology providers. Specifically, we receive core systems processing, essential web hosting and other Internet systems and deposit and other processing services from third-party service providers. If these third-party service providers experience difficulties or terminate their services and we are unable to replace them with other service providers, our operations could be interrupted and our operating expenses may be materially increased. If an interruption were to continue for a significant period of time, our business financial condition and results of operations could be materially adversely affected.

We continually encounter technological change, and we may have fewer resources than many of our competitors to continue to invest in technological improvements.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our clients by using technology to provide products and services that will satisfy client demands for convenience, as well as to create additional efficiencies in our operations. Many national vendors provide turn-key services to community banks, such as internet banking and remote deposit capture that allow smaller banks to compete with institutions that have substantially greater resources to invest in technological improvements. We may not be able, however, to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

In addition, because of the demand for technology-driven products, banks are increasingly contracting with third party vendors to provide data processing and core banking functions. The use of technology-related products, services, delivery channels and processes exposes a bank to various risks, particularly transaction, strategic, reputation and compliance risks. There can be no assurance that we will be able to successfully manage the risks associated with our increased dependency on technology.

The network and computer systems on which we depend could fail or experience security breaches.

Our computer systems could be vulnerable to unforeseen problems. Because we conduct a part of our business over the Internet and outsource several critical functions to third parties, operations will depend on our ability, as well as the ability of third-party service providers, to protect computer systems and network infrastructure against damage from fire, power loss, telecommunications failure, physical break-ins or similar catastrophic events. Any damage or failure that causes interruptions in operations could have a material adverse effect on our business, financial condition and results of operations.

In addition, a significant barrier to online financial transactions is the secure transmission of confidential information over public networks. Our Internet banking system relies on encryption and authentication technology to provide the security and authentication necessary to effect secure transmission of confidential information. Advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms our third-party service providers use to protect customer transaction data. If any such compromise of security were to occur, it could have a material adverse effect on our business, financial condition and results of operations.

Federal, state and local consumer lending laws may restrict our ability to originate or increase our risk of liability with respect to certain mortgage loans and could increase our cost of doing business.

Federal, state and local laws have been adopted that are intended to eliminate certain lending practices considered “predatory” or “unfair and deceptive practices.” These laws prohibit practices such as steering borrowers away from more affordable products, selling unnecessary insurance to borrowers, repeatedly refinancing loans, and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. It is our policy not to make predatory loans or engage in deceptive practices, but these laws create the potential for liability with respect to our lending, servicing, loan investment and deposit taking activities. They increase our cost of doing business, and ultimately may prevent us from making certain loans and cause us to reduce the average percentage rate or the points and fees on loans that we do make.

Table of Contents

Some provisions of our articles of incorporation and bylaws and certain provisions of Washington law may deter takeover attempts, which may limit the opportunity of our shareholders to sell their shares at a favorable price.

Some provisions of our articles of incorporation and bylaws may have the effect of deterring or delaying attempts by our shareholders to remove or replace management, to commence proxy contests, or to effect changes in control. These provisions include:

- a classified board of directors so that only approximately one third of our board of directors is elected each year;
- elimination of cumulative voting in the election of directors;
- procedures for advance notification of shareholder nominations and proposals;
- the ability of our board of directors to amend our bylaws without shareholder approval; and
- the ability of our board of directors to issue shares of preferred stock without shareholder approval upon the terms and conditions and with the rights, privileges and preferences as the board of directors may determine.

In addition, as a Washington corporation, we are subject to Washington law which imposes restrictions on some transactions between a corporation and certain significant shareholders. These provisions, alone or together, could have the effect of deterring or delaying changes in incumbent management, proxy contests or changes in control.

ITEM 1B UNRESOLVED STAFF COMMENTS

None.

ITEM 2 PROPERTIES

We lease principal offices, which are located in office space in downtown Seattle at 601 Union Street, Suite 2000, Seattle, WA 98101. This office lease provides sufficient space to conduct the management of our business. In addition, we currently lease space for all 46 of our office locations. Our branches include separate lending and retail banking facilities, as well as combined facilities, primarily located in Washington, Oregon, Idaho and Hawaii.

ITEM 3 LEGAL PROCEEDINGS

Because the nature of our business involves the collection of numerous accounts, the validity of liens and compliance with various state and federal lending laws, we are subject to various legal proceedings in the ordinary course of our business related to foreclosures, bankruptcies, condemnation and quiet title actions and alleged statutory and regulatory violations. We are also subject to legal proceedings in the ordinary course of business related to employment matters. We do not expect that these proceedings, taken as a whole, will have a material adverse effect on our business, financial position or our results of operations. There are currently no matters that, in the opinion of management, would have a material adverse effect on our consolidated financial position, results of operation or liquidity, or for which there would be a reasonable possibility of such a loss based on information known at this time.

ITEM 4 MINE SAFETY DISCLOSURES

Not applicable.

Table of Contents

PART II

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

Our common stock began trading on the NASDAQ Capital Market on February 10, 2012 under the symbol “HMST.” Prior to that date, our common stock was not publicly traded. The following table sets forth, for the periods indicated, the high and low (other than our initial public offering price of $11.00 per share) reported sales prices per share of the common stock as reported on the NASDAQ Global Select Market, our principal trading market (as adjusted to reflect the 2-for-1 forward stock split effective March 6, 2012 and the 2-for-1 forward stock split effective November 5, 2012).

| | High | Low |
|---|---|---|
| For the year ended December 31, 2012 | | |
| First quarter ended March 31 | $14.99 | $11.33 |
| Second quarter ended June 30 | $17.77 | $13.30 |
| Third quarter ended September 30 | $19.75 | $15.39 |
| Fourth quarter ended December 31 | $26.97 | $18.55 |

As of February 28, 2013, there were 153 shareholders of record of our common stock.

Dividend Policy

HomeStreet, Inc. has not paid cash dividends on our stock since April 2008.

The amount and timing of any future dividends have not been determined. The payment of dividends will depend upon a number of factors, including capital requirements, the Company’s and the Bank’s financial condition and results of operations, tax considerations, statutory and regulatory limitations, general economic conditions and certain restrictions described below.

The Company is currently subject to a cease and desist order from the Federal Reserve that prohibits us from declaring, making or paying any dividends on our common stock without the prior written consent of the Federal Reserve. See “Regulation and Supervision — Company Order” for information on that regulatory restriction. Washington law also imposes certain restrictions on the ability of the Company to pay dividends. See “Regulation and Supervision — Regulation of the Company — Dividend Policy.”

Our outstanding TruPS also restrict the payment of dividends to the Company's shareholders under the terms of their indentures. We have issued $61.9 million in junior subordinated debentures in connection with the sale of TruPS by the HomeStreet Statutory Trusts. The related indenture agreements, guarantees and declarations of trust for each statutory trust prohibit us, subject to limited exceptions, from declaring or paying any dividends or distributions on, or redeeming, repurchasing, acquiring or making any liquidation payments with respect to, any of our capital stock at any time when (1) an event of default has occurred or is occurring under such debentures (2) we are in default with respect to payment of any obligations under such guarantee or (3) we have deferred payment of interest on the outstanding junior subordinated debentures, which deferral of interest is permitted by the terms of the indentures from time to time for up to five years. We had deferred payment of interest on all of the junior subordinated debentures for each quarter since December 15, 2008. However, on March 12, 2013, the Federal Reserve granted our request to pay all interest previously deferred, which we subsequently paid (along with current interest due) on March 15, 2013.

Our ability to pay dividends will also depend, in large part, upon receipt of dividends from the Bank. We will have limited sources of income other than dividends from the Bank and earnings from the investment of proceeds from our initial public offering of common stock that we retained.

For the foregoing reasons, there can be no assurance that we will pay dividends on our common stock in any future period.

Sales of Unregistered Securities

Not applicable.

Stock Repurchases in the Fourth Quarter

Table of Contents

Not applicable.

Equity Compensation Plan Information

The following table gives information about our common stock that may be issued upon the exercise of options, warrants and rights under all of our existing equity compensation plans as of December 31, 2012, including the 2010 Equity Incentive Plan, the 2011 HomeStreet, Inc. Equity Compensation Plan for Non-Employee Directors and the retention grants made in 2010 outside of the 2010 Equity Incentive Plan but subject to the terms and conditions of that plan.

| Plan Category | (a) Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights | | (b) Weighted Average Exercise Price of Outstanding Options, Warrants, and Rights | (c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) | |
|---|---|---|---|---|---|
| Plans approved by shareholders | 631,366 | (1) | $12.22 | 275,838 | (2)(3)(4) |
| Plans not approved by shareholders (5) | 418,000 | | $0.77 | N/A | |
| Total | 1,049,366 | | $7.66 | 275,838 | |

(1) Consists of option grants awarded pursuant to the 2010 Equity Incentive Plan.

(2) Consists of 112,370 shares remaining under the 2010 Equity Incentive Plan and 163,468 shares remaining under the 2011 HomeStreet, Inc. Equity Compensation Plan for Non-Employee Directors. (the "2011 Plan"). In 2012, the Company awarded 4,532 shares under the 2011 Plan, out of a total of 168,000 shares available for issuance under the 2011 Plan.

(3) The 2010 Equity Incentive Plan was passed by shareholders in January 2010 but did not become effective until the completion of our initial public offering in February 2012. Following our initial public offering, the number of shares available for issuance under the 2010 Equity Incentive Plan, giving effect to our 2-for-1 forward stock splits in March 2012 and November 2012, was 1,412,712. This amount was established by our Board of Directors, which determined that it will not issue equity grants under the 2010 Equity Incentive Plan in an amount that would cause the combined amount of awards granted pursuant to the 2010 Equity Incentive Plan and the 2010 retention equity awards to exceed 10% of the number of shares outstanding immediately following the closing of our initial public offering.

(4) During 2012, the Company awarded 223,974 restricted stock awards, of which 188,143 have vested, and 1,402 performance stock awards, all of which have vested, under the 2010 Equity Incentive Plan.

(5) Consists of retention equity awards granted in 2010 outside of the 2010 Equity Incentive Plan but subject to its terms and conditions.

Table of Contents

Stock Performance Graph

This performance graph shall not be deemed "soliciting material" or to be "filed" with the SEC for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (Exchange Act), or otherwise subject to the liabilities under that Section, and shall not be deemed to be incorporated by reference into any filing of HomeStreet, Inc. under the Securities Act of 1933, as amended, or the Exchange Act.
The following graph shows a comparison from February 10, 2012 (the date our common stock commenced trading on the NASDAQ Global Select Market) through December 31, 2012 of the cumulative total return for our common stock, the KBW Bank Index (BKX) and the Russell 2000 (RUT) Index. The graph assumes that $100 was invested at the market close on February 10, 2012 in the common stock of HomeStreet, Inc., the KBW Bank Index and the Russell 2000 Index and data for the KBW Bank Index and the Russell 2000 Index assumes reinvestments of dividends. The stock price performance of the following graph is not necessarily indicative of future stock price performance.

Table of Contents

## ITEM 6 SELECTED FINANCIAL DATA

The data set forth below should be read in conjunction with Item 7, "Management's Discussion and Analysis of Consolidated Financial Condition and Results of Operations," and the Consolidated Financial Statements and Notes thereto appearing at Item 8 of this report.

The following table sets forth selected historical consolidated financial and other data for us at and for each of the periods ended as described below. The selected historical consolidated financial data as of December 31, 2012 and 2011 and for each of the years ended December 31, 2012, 2011 and 2010 have been derived from, and should be read together with, our audited consolidated financial statements and related notes included elsewhere in this Form 10-K. The selected historical consolidated financial data as of December 31, 2010, 2009 and 2008 and for each of the years ended December 31, 2009 and 2008 have been derived from our audited consolidated financial statements for those years, which are not included in this Form 10-K. You should read the summary selected historical consolidated financial and other data presented below in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our financial statements and the notes thereto, which are included elsewhere in this Form 10-K. We have prepared our unaudited information on the same basis as our audited consolidated financial statements and have included, in our opinion, all adjustments that we consider necessary for a fair presentation of the financial information set forth in that information.

| | At or for the Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| (dollars in thousands, except share data) | 2012 | 2011 | 2010 | 2009 | 2008 |
| Income statement data (for the period ended): | | | | | |
| Net interest income | $60,743 | $48,494 | $39,276 | $31,502 | $75,885 |
| Provision for loan losses | 11,500 | 3,300 | 37,300 | 153,515 | 34,411 |
| Noninterest income | 237,534 | 97,205 | 90,474 | 59,230 | 40,346 |
| Noninterest expense | 183,105 | 126,494 | 126,000 | 94,448 | 70,189 |
| Net income (loss) before taxes | 103,672 | 15,905 | (33,550) | (157,231) | 11,631 |
| Income tax expense (benefit) | 21,546 | (214) | 697 | (46,955) | 3,202 |
| Net income (loss) | $82,126 | $16,119 | $(34,247) | $(110,276) | $8,429 |
| Basic earnings (loss) per common share(1) | $6.17 | $2.98 | $(6.34) | $(20.41) | $1.56 |
| Diluted earnings (loss) per common share (1) | $5.98 | $2.80 | $(6.34) | $(20.41) | $1.56 |
| Common shares outstanding (1) | 14,382,638 | 5,403,498 | 5,403,498 | 5,403,498 | 5,403,498 |
| Weighted average common shares: | | | | | |
| Basic | 13,312,939 | 5,403,498 | 5,403,498 | 5,403,498 | 5,394,596 |
| Diluted | 13,739,398 | 5,748,342 | 5,403,498 | 5,403,498 | 5,401,430 |
| Shareholders' equity per share | $18.34 | $15.99 | $10.88 | $17.01 | $38.14 |
| Dividends per share | $— | $— | $— | $— | $0.23 |
| Financial position (at year end): | | | | | |
| Cash and cash equivalents | $25,285 | $263,302 | $72,639 | $217,103 | $270,577 |
| Investment securities available for sale | 416,329 | 329,047 | 313,513 | 657,840 | 56,337 |
| Loans held for sale (2) | 620,799 | 150,409 | 212,602 | 57,046 | 48,636 |
| Loans held for investment, net | 1,308,974 | 1,300,873 | 1,538,521 | 1,964,994 | 2,425,887 |
| Mortgage servicing rights (2) | 95,493 | 77,281 | 87,232 | 78,372 | 57,699 |
| Other real estate owned | 23,941 | 38,572 | 170,455 | 107,782 | 20,905 |

| | | | | | |
|---|---|---|---|---|---|
| Total assets | 2,631,230 | 2,264,957 | 2,485,697 | 3,209,536 | 2,958,911 |
| Deposits | 1,976,835 | 2,009,755 | 2,129,742 | 2,332,333 | 1,911,311 |
| FHLB advances | 259,090 | 57,919 | 165,869 | 677,840 | 705,764 |
| Equity | $263,762 | $86,407 | $58,789 | $91,896 | $206,103 |

Table of Contents

| | At or for the Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| (dollars in thousands, except share data) | 2012 | 2011 | 2010 | 2009 | 2008 |
| Financial position (averages): | | | | | |
| Investment securities available for sale | $410,819 | $306,813 | $457,930 | $372,320 | $119,720 |
| Loans held for investment | 1,303,010 | 1,477,976 | 1,868,035 | 2,307,215 | 2,519,811 |
| Total interest earning assets | 2,166,827 | 2,069,858 | 2,642,693 | 3,056,755 | 2,762,723 |
| Total interest bearing deposits | 1,644,859 | 1,814,464 | 2,071,237 | 2,012,971 | 1,557,533 |
| FHLB advances | 93,325 | 93,755 | 382,083 | 685,715 | 734,989 |
| Total interest bearing liabilities | 1,817,847 | 1,970,725 | 2,522,767 | 2,776,163 | 2,485,786 |
| Shareholders' equity | $209,629 | $68,537 | $89,267 | $160,145 | $203,358 |
| Financial performance: | | | | | |
| Return on average common shareholders' equity (3) | 39.18 % | 23.52 % | (38.00 )% | (68.86 )% | 4.14 % |
| Return on average assets | 3.43 % | 0.70 % | (1.19 )% | (3.47 )% | 0.29 % |
| Net interest margin (4) | 2.89 % | 2.36 % | 1.50 % | 1.04 % | 2.78 % |
| Efficiency ratio (5) | 61.39 % | 86.82 % | 97.24 % | 104.10 % | 60.39 % |
| Operating efficiency ratio (7) | 58.01 % | 66.04 % | 73.56 % | 92.55 % | 59.06 % |
| Credit quality: | | | | | |
| Allowance for credit losses | $27,751 | $42,800 | $64,566 | $110,422 | $58,587 |
| Allowance for credit losses/total loans | 2.07 % | 3.18 % | 4.02 % | 5.32 % | 2.36 % |
| Allowance for loan losses/nonaccrual loans | 92.20 % | 55.81 % | 56.69 % | 29.25 % | 77.72 % |
| Total nonaccrual loans (6) | $29,892 | $76,484 | $113,210 | $374,218 | $75,385 |
| Nonaccrual loans/total loans | 2.23 % | 5.69 % | 7.06 % | 18.04 % | 3.03 % |
| Other real estate owned | $23,941 | $38,572 | $170,455 | $107,782 | $20,905 |
| Total nonperforming assets | $53,833 | $115,056 | $283,665 | $482,000 | $96,290 |
| Nonperforming assets/total assets | 2.05 % | 5.08 % | 11.41 % | 15.02 % | 3.25 % |
| Net charge-offs | $26,549 | $25,066 | $83,156 | $101,680 | $14,628 |
| Regulatory capital ratios for the bank: | | | | | |
| Tier 1 leverage capital (to average assets) | 11.78 % | 6.04 % | 4.52 % | 4.53 % | 8.70 % |
| Tier 1 risk-based capital (to risk-weighted assets) | 18.05 % | 9.88 % | 6.88 % | 7.19 % | 10.53 % |
| Total risk-based capital (to risk-weighted assets) | 19.31 % | 11.15 % | 8.16 % | 8.50 % | 11.79 % |
| SUPPLEMENTAL DATA: | | | | | |
| Loans serviced for others: | | | | | |
| Single family | $8,870,688 | $6,885,285 | $6,343,158 | $5,820,946 | $4,695,804 |
| Multifamily | 727,118 | 758,535 | 776,671 | 810,910 | 822,512 |
| Other | 53,235 | 56,785 | 58,765 | 69,839 | 74,230 |
| Total loans serviced for others | $9,651,041 | $7,700,605 | $7,178,594 | $6,701,695 | $5,592,546 |
| Loan origination activity: | | | | | |
| Single family | $4,901,459 | $1,721,264 | $2,069,144 | $2,727,457 | $1,735,897 |
| Other | 255,049 | 150,401 | 120,058 | 124,433 | 817,438 |

| | | | | | |
|---|---|---|---|---|---|
| Total loan origination activity | $5,156,508 | $1,871,665 | $2,189,202 | $2,851,890 | $2,553,335 |

(1) Share and per share data shown after giving effect to the 2-for-1 forward stock splits effective March 6, 2012 and November 5, 2012 , as well as the 1-for-2.5 reverse stock split effective July 19, 2011.

(2) On January 1, 2010 we elected to carry mortgage servicing rights related to single family loans at fair value, and elected to carry single family mortgage loans held for sale using the fair value option.
(3) Net earnings (loss) available to common shareholders divided by average common shareholders' equity.
(4) Net interest income divided by total average earning assets on a tax equivalent basis.
(5) The efficiency ratio is noninterest expense divided by total revenue (net interest income and noninterest income).
(6) Generally, loans are placed on nonaccrual status when they are 90 or more days past due.
(7) We include an operating efficiency ratio that is not calculated based on accounting principles generally accepted in the United States ("GAAP"), but which we believe provides important information regarding our results of operations. Our calculation of the operating efficiency ratio is computed by dividing noninterest expense less costs related to OREO (gains (losses) on sales, valuation allowance adjustments, and maintenance and taxes) by total revenue (net interest income and noninterest income). Management uses this non-GAAP measurement as part of its assessment of performance in managing noninterest expense. We believe that costs related to OREO are more appropriately considered as credit-related costs rather than as an indication of our operating efficiency. The follow table provides a reconciliation of non-GAAP to GAAP measurement.

| | At or for the Year Ended December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | | 2011 | | 2010 | | 2009 | | 2008 | |
| Efficiency ratio | 61.39 | % | 86.82 | % | 97.24 | % | 104.10 | % | 60.39 | % |
| Less impact of OREO expenses | 3.38 | % | 20.78 | % | 23.68 | % | 11.55 | % | 1.33 | % |
| Operating efficiency ratio | 58.01 | % | 66.04 | % | 73.56 | % | 92.55 | % | 59.06 | % |

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

The following discussion should be read in conjunction with the "Selected Consolidated Financial Data" and the Consolidated Financial Statements and the related Notes included in Items 6 and 8 of this Form 10-K. The following discussion contains statements using the words "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "potential," "should," "will" and "would" and similar expressions (or the negative of these terms) generally identify forward-looking statements. Such statements involve inherent risks and uncertainties, many of which are difficult to predict and are generally beyond the control of the Company and are subject to risks and uncertainties, including, but not limited to, those discussed below and elsewhere in this Form 10-K, particularly in Item 1A "Risk Factors" that could cause actual results to differ significantly from those projected. Although we believe that expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We do not intend to update any of the forward-looking statements after the date of this Form 10-K to conform these statements to actual results or changes in our expectations. Readers are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this Form 10-K.

This report contains forward-looking statements. For a discussion about such statements, including the risks and uncertainties inherent therein, see "Forward-Looking Statements." Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the Consolidated Financial Statements and Notes presented elsewhere in this annual report on Form 10-K.

### Management's Overview of 2012 Financial Performance

We are a 91-year-old diversified financial services company headquartered in Seattle, Washington, serving consumers and businesses primarily in the Pacific Northwest and Hawaii. The Company is principally engaged in real estate lending, including mortgage banking activities, and retail and commercial banking operations. Our primary subsidiaries are HomeStreet Bank (the "Bank") and HomeStreet Capital Corporation. HomeStreet Bank is a Washington state-chartered savings bank that provides residential and commercial loans, deposit products and services, non-deposit investment products, and cash management services. HomeStreet Bank's primary loan products include single family residential mortgages, loans secured by commercial real estate, loans for residential and commercial real estate construction, and commercial business loans. HomeStreet Capital Corporation, a Washington corporation, originates, sells and services multifamily mortgage loans under the Fannie Mae Delegated Underwriting and Servicing Program ("DUS®) (DUS® is a registered trademark of Fannie Mae.) in conjunction with HomeStreet Bank. Doing business as HomeStreet Insurance, we provide insurance products and services for consumers and businesses. We additionally offer single family home loans through our partial ownership in an affiliated business arrangement known as Windermere Mortgage Services Series LLC ("WMS LLC").

We generate revenue through positive "net interest income" and by earning "noninterest income." Net interest income is primarily the difference between our interest income earned on loans and investment securities less the interest we pay on deposits and other borrowings. We earn noninterest income from the origination, sale and servicing of loans and fees earned on deposit services and investment and insurance sales.

At December 31, 2012, we had total assets of $2.63 billion, net loans held for investment of $1.31 billion, deposits of $1.98 billion and shareholders' equity of $263.8 million. At December 31, 2011, we had total assets of $2.26 billion, net loans held for investment of $1.30 billion, deposits of $2.01 billion and shareholders' equity of $86.4 million.

Our reported net income of $82.1 million for the year ended 2012 marked a significant increase in profitability, reflecting our success in growing our mortgage lending business and our commercial and consumer businesses. As discussed below, during 2012 we improved or expanded major components of our business, including recapitalizing the Company; upgrading the Bank's regulatory standing; expanding our mortgage origination capacity and market share; improving the quality of our deposits; bolstering our processing, compliance and risk management capabilities; and achieving significantly improved results of operations.

The Board of Directors twice approved 2-for-1 forward splits of the Company's common stock that were effective on March 6, 2012 and November 5, 2012, respectively. Shares outstanding and per share information have been adjusted to reflect the stock splits.

Financial Performance

For 2012, we achieved record net income of $82.1 million, or $5.98 per diluted share, compared to $16.1 million, or $2.80 per share, for 2011. Return on average equity was 39.18% for 2012, compared to 23.52% for 2011, while the return on average assets was 3.43% for 2012, compared to 0.70% for 2011.

Our record net income in 2012 resulted from a $152.6 million increase in net revenue compared to 2011. Our strong revenue growth in 2012 mostly reflected the significant growth in mortgage loan origination and sale activities driven by high mortgage production volume and strong secondary market profit margins that persisted throughout 2012. We also continued to expand our mortgage production capacity by increasing our mortgage origination and support personnel by 146% during the year.

Net interest income, on a tax equivalent basis, was $62.6 million in 2012, an increase of $13.8 million, or 28.2%, compared to net interest income of $48.8 million in 2011. Our net interest margin for 2012 improved to 2.89% from 2.36% for 2011. The improvement in our net interest income and net interest margin in large part reflects the execution of our deposit product and pricing strategy, as growth in transaction and savings account balances more than offset maturities of higher yielding certificates of deposit. Additionally, higher average balances of loans held for sale from increased loan production and higher average balances of investment securities from the use of proceeds from our initial public offering increased our average balances of interest earning assets in 2012.

Provision for credit losses was $11.5 million in 2012, compared to $3.3 million in 2011. Asset quality trends improved during the year as nonaccrual loans declined to $29.9 million at December 31, 2012, a decrease of $46.6 million, or 60.9%, from $76.5 million at December 31, 2011. Loan delinquencies also decreased, with total loans past due decreasing to 6.58% of loans held for investment at December 31, 2012, compared to 10.38% at December 31, 2011. Overall, the allowance for credit losses decreased to $27.8 million, or 2.07% of loans held for investment at December 31, 2012, down from $42.8 million, or 3.18% of total loans held for investment at December 31, 2011.

Noninterest income was $237.5 million in 2012, an increase of $140.3 million, or 144%, from $97.2 million in 2011. Our noninterest income is heavily dependent upon our single family mortgage banking activities, which are comprised of mortgage origination and sale activities and mortgage servicing activities. The increase in noninterest income is predominantly due to higher net gain on mortgage loan origination and sale activities, which totaled $210.2 million in 2012 compared to $48.5 million in 2011, an increase of $161.7 million, or 334%, year-over-year. This income was partially offset by a $21.9 million decrease in mortgage servicing income in 2012 compared to prior year, primarily due to mortgage servicing rights ("MSRs") risk management results.

Noninterest expense was $183.1 million in 2012, an increase of $56.6 million, or 44.8%, from $126.5 million in 2011. Noninterest expense increased primarily due to salaries and related costs, which increased $66.3 million in 2012 compared to 2011, primarily higher incentive compensation, including commissions to lending personnel, driven by growth in single family closed loan production volume and increased headcount as we invested in growth and diversification. This increase was partially offset by lower other real estate owned ("OREO") expenses, which was $10.1 million in 2012, a decrease of $20.2 million from OREO expense of $30.3 million in 2011.

Income tax expense was $21.5 million in 2012 compared to an income tax benefit of $214 thousand in 2011. The Company's 2012 tax expense is based on the Company's annual effective income tax rate plus discrete benefits recognized during the year. The Company's effective tax rate for the year of 21% differs from the federal statutory rate of 35% primarily due to a $14.4 million tax benefit related to the reversal of the Company's beginning of year valuation allowance against deferred tax assets during the second quarter of 2012, tax exempt income and state income taxes in Oregon, Hawaii and Idaho.

Asset Quality

Management believes that the Company’s allowance for loan losses is at a level appropriate to cover estimated incurred losses inherent within the loans held for investment portfolio. Our credit risk profile has improved since December 31, 2011 as illustrated by the credit trends below.

We recorded an $11.5 million provision for credit losses in 2012 compared to $3.3 million in 2011. Net charge-offs were $26.5 million in 2012 compared to $25.1 million in 2011. The allowance for loan losses (which excludes the allowance for unfunded commitments) decreased to $27.6 million at December 31, 2012, or 2.06% of loans held for investment, compared to $42.7 million, or 3.17% of total loans held for investment, at December 31, 2011. The decrease in the allowance for loan losses since December 31, 2011 primarily reflects reductions in specific reserves from charge-offs related to the resolution of certain nonaccrual loans as they were transferred to OREO. Additionally, the overall credit quality of our loan portfolio improved during 2012 as reflected in decreased nonaccrual loans and total loan delinquencies.

Table of Contents

Nonperforming assets decreased to $53.8 million at December 31, 2012, from $115.1 million at December 31, 2011. Nonaccrual loans declined to $29.9 million at December 31, 2012, compared to $76.5 million at December 31, 2011. Past due loans totaled $88.2 million, or 6.58% of total loans, at December 31, 2012, compared to $139.9 million, or 10.38% of total loans, at December 31, 2011. OREO balances decreased to $23.9 million at December 31, 2012, compared to $38.6 million at December 31, 2011. In April 2012, bankruptcy courts affirmed the Company’s settlement of collection litigation related to two nonperforming construction/land development loans with aggregate carrying values of $26.6 million. As a result, we charged off $11.8 million related to these two loans, transferred the estimated net recovery value of $18.8 million to OREO and subsequently sold the properties.

Expansion of Mortgage Banking Operations

During 2012, we expanded our mortgage origination capacity, accelerating our strategic plan to increase mortgage origination volume and market share by hiring 389 mortgage origination and support personnel, a significant portion of whom were previously employed in Washington and Idaho by MetLife Home Loans. This number included MetLife's former Pacific Northwest regional sales manager and its regional builder services manager, as well as regional and branch managers, loan officers and related production support staff. In 2012, we opened 15 new mortgage loan origination offices in Washington, Oregon and Idaho to accommodate the expansion of these operations.

Capital

We improved our Bank regulatory capital ratios during 2012, increasing our Tier 1 leverage and total risk-based capital ratios to 11.78% and 19.31%, compared with 6.04% and 11.15% at December 31, 2011, respectively. This improvement reflects the completion of our initial public offering of common stock as well as our earnings in 2012.

On February 15, 2012, we completed our initial public offering of 8,723,632 shares of common stock for an initial offering price of $11.00 per share (after giving effect to the 2-for-1 forward stock split effective March 6, 2012 and the 2-for-1 forward stock split effective November 5, 2012). The net increase in HomeStreet's capital was $86.4 million, of which $55.0 million was contributed to the Bank on February 24, 2012 with an additional $10.0 million contributed on April 26, 2012.

Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with the accounting principles generally accepted in the United States ("U.S. GAAP") requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expense in the financial statements. Various elements of our accounting policies, by their nature, involve the application of highly sensitive and judgmental estimates and assumptions. Some of these policies and estimates relate to matters that are highly complex and contain inherent uncertainties. It is possible that, in some instances, different estimates and assumptions could reasonably have been made and used by management, instead of those we applied, which might have produced different results that could have had a material effect on the financial statements.

We have identified the following accounting policies and estimates that, due to the inherent judgments and assumptions and the potential sensitivity of the financial statements to those judgments and assumptions, are critical to an understanding of our financial statements. We believe that the judgments, estimates and assumptions used in the preparation of the Company's financial statements are appropriate. For a further description of our accounting policies, see Note 1–Summary of Significant Accounting Policies in the financial statement to this Form 10-K.

Allowance for Loan Losses

The allowance for loan losses represents management's estimate of incurred credit losses inherent within our loan portfolio. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses in those future periods.

We employ a disciplined process and methodology to establish our allowance for loan losses that has two basic components: first, an asset-specific component involving the identification of impaired loans and the measurement of impairment for each individual loan identified; and second, a formula-based component for estimating probable principal losses for all other loans.

An asset-specific allowance for impaired loans is established based on the amount of impairment calculated on those loans and charging off amounts determined to be uncollectable. A loan is considered impaired when it is probable that all contractual

Table of Contents

principal and interest payments due will not be collected substantially in accordance with the terms of the loan agreement. Factors we consider in determining whether a loan is impaired include payment status, collateral value, borrower financial condition, guarantor support and the probability of collecting scheduled principal and interest payments when due.

When a loan is identified as impaired, impairment is measured as the difference between the recorded investment in the loan and the present value of expected future cash flows discounted at the loan’s effective interest rate or based on the loan’s observable market price. For impaired collateral-dependent loans, impairment is measured as the difference between the recorded investment in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with our appraisal policy, the fair value of impaired collateral-dependent loans is based upon independent third-party appraisals or on collateral valuations prepared by in-house appraisers, which generally are updated every six months. We require an independent third-party appraisal at least annually for substandard loans and other real estate owned ("OREO"). Once a third-party appraisal is six months old, or if our chief appraiser determines that market conditions, changes to the property, changes in intended use of the property or other factors indicate that an appraisal is no longer reliable, we perform an internal collateral valuation to assess whether a change in collateral value requires an additional adjustment to carrying value. A collateral valuation is a restricted-use report prepared by our internal appraisal staff in accordance with our appraisal policy. Upon the receipt of an updated appraisal or collateral valuation, loan impairments are remeasured and recorded. If the calculated impairment is determined to be permanent, fixed or nonrecoverable, the impairment will be charged off. Loans designated as impaired are generally placed on nonaccrual and remain in that status until all principal and interest payments are current and the prospects for future payments in accordance with the loan agreement are reasonably assured, at which point the loan is returned to accrual status. See "Credit Risk Management – Asset Quality and Nonperforming Assets” discussions within Management's Discussion and Analysis of this Form 10-K.

In estimating the formula-based component of the allowance for loan losses, loans are segregated into homogeneous loan classes. Loans are designated into loan classes based on loans pooled by product types and similar risk characteristics or areas of risk concentration. Credit loss assumptions are estimated using a model that categorizes loan pools based on loan type and asset quality rating ("AQR") or delinquency bucket. This model calculates an expected loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by AQR or delinquency buckets using one-year analysis periods, and the potential severity of loss, based on the aggregate net lifetime losses incurred per loan class.

The formula-based component of the allowance for loan losses also considers qualitative factors for each loan class, including the following changes in:

- lending policies and procedures;
- international, national, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets;
- the nature of the loan portfolio, including the terms of the loans;
- the experience, ability and depth of the lending management and other relevant staff;
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans;
- the quality of our loan review and process;
- the value of underlying collateral for collateral-dependent loans;
- the existence and effect of any concentrations of credit and changes in the level of such concentrations; and
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

Qualitative factors are expressed in basis points and are adjusted downward or upward based on management’s judgment as to the potential loss impact of each qualitative factor to a particular loan pool at the date of the analysis.

Additionally, our credit administration department continually monitors conditions that affect the carrying values of our collateral, including local and regional economic factors as well as asset-specific factors such as tax values, comparable sales and other factors that affect or suggest changes in the actual collateral values. They also monitor and adjust for changes in comparable sales or competing projects, changes in zoning or entitlement status, changes in occupancy rates for income properties and similar factors. If we deem such factors to be significant, we generally perform an internal collateral valuation or will order an independent appraisal sooner than required under our appraisal policy.

Table of Contents

The provision for loan losses recorded through earnings is based on management's assessment of the amount necessary to maintain the allowance for loan losses at a level appropriate to cover probable incurred losses inherent within the loans held for investment portfolio. The amount of provision and the corresponding level of allowance for loan losses are based on our evaluation of the collectability of the loan portfolio based on historical loss experience and other significant qualitative factors.

The allowance for loan losses, as reported in our consolidated statements of financial condition, is adjusted by a provision for loan losses, which is recognized in earnings, and reduced by the charge-off of loan amounts, net of recoveries. For further information on fair value measurements, see Note 5–Loans and Credit Quality in the notes to the financial statements of this Form 10-K.

Fair Value of Financial Instruments, Single Family MSRs and OREO

A portion of our assets are carried at fair value, including mortgage servicing rights, single family loans held for sale, interest rate lock commitments, investment securities available for sale and derivatives used in our hedging programs. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value is based on quoted market prices, when available. In certain cases where a quoted price for an asset or liability is not available, the Company uses valuation models to estimate its fair value. These models incorporate inputs such as forward yield curves, loan prepayment assumptions, expected loss assumptions, market volatilities, and pricing spreads utilizing market-based inputs where readily available. We believe our valuation methods are appropriate and consistent with those that would be used by other market participants. However, imprecision in estimating unobservable inputs and other factors may result in these fair value measurements not reflecting the amount realized in an actual sale or transfer of the asset or liability in a current market exchange.

A three-level valuation hierarchy has been established under ASC 820 for disclosure of fair value measurements. The valuation hierarchy is based on the observability of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. The levels are defined as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability for substantially the full term of the financial instrument.
- Level 3 – Unobservable inputs for the asset or liability. These inputs reflect the Company's assumptions of what market participants would use in pricing the asset or liability.

Significant judgment is required to determine whether certain assets and liabilities measured at fair value are included in Level 2 or Level 3. When making this judgment, we consider all available information, including observable market data, indications of market liquidity and orderliness, and our understanding of the valuation techniques and significant inputs used. The classification of Level 2 or Level 3 is based upon the specific facts and circumstances of each instrument or instrument category and judgments are made regarding the significance of the Level 3 inputs to an instrument's fair value measurement in its entirety. If Level 3 inputs are considered significant, the instrument is classified as Level 3.

The following is a summary of the assets and liabilities recorded at fair value on a recurring basis and where the amounts are measured using significant Level 3 inputs. The fair value of the remaining assets and liabilities were measured using valuation methodologies involving market-based or market-derived information, collectively Level 1 and 2 measurements.

Table of Contents

| | At December 31, | | | |
|---|---|---|---|---|
| | 2012 | | 2011 | |
| (in millions) | Total Balance | Level 3 | Total Balance | Level 3 |
| Assets carried at fair value | $1,135.0 | $109.9 | $543.5 | $70.2 |
| As a percentage of total assets | 43 % | 4 % | 24 % | 3 % |
| Liabilities carried at fair value | $12.1 | $— | $11.4 | $— |
| As a percentage of total liabilities | 1 % | NM | 1 % | NM |

NM = not meaningful

As of December 31, 2012, our Level 3 recurring fair value measurements consisted of single family MSRs and interest rate lock commitments.

On a quarterly basis, our Asset/Liability Management Committee ("ALCO") and the Finance Committee of the Bank's Board of Directors review the significant inputs used in Level 3 measurements. Additionally, at least annually ALCO obtains an independent review of the MSR valuation process and procedures, including a review of the model architecture and the valuation assumptions. The Finance Committee of the Board provides oversight and approves the Company’s Asset/Liability Management Policy. We obtain an MSR valuation from an independent valuation firm at least quarterly to assist with the validation of the results and the reasonableness of the assumptions used in measuring fair value.

In addition to the recurring fair value measurements shown above, from time to time the Company may have certain nonrecurring fair value measurements. These fair value measurements usually result from the application of lower of cost or fair value accounting or impairment of individual assets. As of December 31, 2012 and 2011, the Company's Level 3 nonrecurring fair value measurements, totaling $50.8 million and $86.9 million, respectively, were based on the appraised value of collateral used as the basis for the valuation of collateral dependent loans held for investment and OREO.

Real estate valuations are overseen by our appraisal department, which is independent of our lending and credit administration functions. The appraisal department maintains the appraisal policy and recommends changes to the policy subject to approval by the Credit Committee of the Company's Board of Directors and Company's Loan Committee (the "Loan Committee"), established by the Credit Committee of the Company's Board of Directors and comprised of certain of the Company's management. Appraisals are prepared by independent third-party appraisers and our internal appraisers. Single family appraisals are generally reviewed by our single family loan underwriters. Single family appraisals with unusual, higher risk or complex characteristics, as well as commercial real estate appraisals, are reviewed by our appraisal department.

For further information on the fair value of financial instruments, single family MSRs and OREO, see Note 1–Summary of Significant Accounting Policies, Note 12 –Mortgage Banking Operations  and Note 17–Fair Value Measurements in the notes to the financial statements of this Form 10-K.

Income Taxes

In establishing an income tax provision, we must make judgments and interpretations about the application of inherently complex tax laws. We must also make estimates about when in the future certain items will affect taxable income. Our interpretations may be subject to review during examination by taxing authorities and disputes may arise over the respective tax positions. We monitor tax authorities and revise our estimates of accrued income taxes due to changes in income tax laws and their interpretation by the courts and regulatory authorities on a quarterly basis. Revisions of our estimate of accrued income taxes also may result from our own income tax planning and strategies and from the resolution of income tax controversies. Such revisions in our estimates may be material to our operating results for any given reporting period.

Income taxes are accounted for using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, a deferred tax asset or liability is determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

The Company records net deferred tax assets to the extent it is believed that these assets will more likely than not be realized. In making such determination, management considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations.

Table of Contents

After reviewing and weighing all of the positive and negative evidence, if the positive evidence outweighs the negative evidence, then the Company does not record a valuation allowance for deferred tax assets. If the negative evidence outweighs the positive evidence, then a valuation allowance for all or a portion of the deferred tax assets is recorded.

The Company recognizes interest and penalties related to unrecognized tax benefits as income tax expense in the consolidated statements of operations. Accrued interest and penalties are included within the related tax liability line in the consolidated statements of financial condition. For further information regarding income taxes, see Note 14–Income Taxes to the financial statements of this Form 10-K.

Results of Operations

| | For the year ended December 31, | | |
|---|---|---|---|
| (in thousands, except per share data and ratios) | 2012 | 2011 | 2010 |
| Selected statement of operations data | | | |
| Total net revenue | $298,277 | $145,699 | $129,750 |
| Total noninterest expense | 183,105 | 126,494 | 126,000 |
| Provision for credit losses | 11,500 | 3,300 | 37,300 |
| Income tax expense (benefit) | 21,546 | (214) | 697 |
| Net income (loss) | 82,126 | 16,119 | (34,247) |
| Financial performance | | | |
| Diluted earnings per common share | $5.98 | $2.80 | $(6.34) |
| Return on average common shareholders’ equity | 39.18% | 23.52% | (38.00)% |
| Return on average assets | 3.43% | 0.70% | (1.19)% |
| Net interest margin | 2.89% | 2.36% | 1.50% |
| Capital ratios (Bank only) | | | |
| Tier 1 leverage capital (to average assets) | 11.78% | 6.04% | 4.52% |
| Tier 1 risk-based capital (to risk-weighted assets) | 18.05% | 9.88% | 6.88% |
| Total risk-based capital (to risk-weighted assets) | 19.31% | 11.15% | 8.16% |

Comparison of the year ended 2012 to the year ended 2011

For the year ended 2012, we reported record net income of $82.1 million, an increase of $66.0 million, or 409%, compared to net income of $16.1 million in 2011. The increase in net income was driven by record single family mortgage closed loan production as the Company continued to grow its mortgage origination and production capacity and strong secondary market profit margins that persisted throughout 2012.

In the fourth quarter of 2012, we identified an error in the fair value measurement of single family loans held for sale that understated the recorded amount of the loans, thereby delaying the recognition of a portion of the secondary marketing gains until the time that the loans are sold, which generally occurs in the month following loan funding. The correction of this accounting error resulted in an increase to loans held for sale and a related increase to net gain on mortgage loan origination and sale activities in our consolidated statements of financial condition and consolidated statements of operations of $1.3 million at and for the year ended December 31, 2012, representing a correction of the cumulative effect of the error for prior years, which was deemed immaterial.

Average Balances and Rates

Average balances, together with the total dollar amounts of interest income and expense, on a tax equivalent basis related to such balances and the weighted average rates, for years ended December 31, 2012 and 2011 were as follows:

Table of Contents

| (in thousands) | Year Ended December 31, 2012 Average Balance | Interest | Average Yield/Cost | | 2011 Average Balance | Interest | Average Yield/Cost | |
|---|---|---|---|---|---|---|---|---|
| Assets: | | | | | | | | |
| Interest-earning assets: (1) | | | | | | | | |
| Cash & cash equivalents | $94,478 | $231 | 0.24 | % | $159,031 | $465 | 0.29 | % |
| Investment securities | 410,819 | 11,064 | 2.69 | | 306,813 | 7,083 | 2.31 | |
| Loans held for sale | 358,520 | 12,713 | 3.54 | | 126,038 | 5,602 | 4.44 | |
| Loans held for investment | 1,303,010 | 58,490 | 4.49 | | 1,477,976 | 66,342 | 4.49 | |
| Total interest-earning assets | 2,166,827 | 82,498 | 3.81 | | 2,069,858 | 79,492 | 3.84 | |
| Noninterest-earning assets (2) | 225,704 | | | | 229,943 | | | |
| Total assets | $2,392,531 | | | | $2,299,801 | | | |
| Liabilities and shareholders' equity: | | | | | | | | |
| Deposits: | | | | | | | | |
| Interest-bearing demand accounts | $151,029 | 498 | 0.33 | % | $129,254 | 575 | 0.44 | % |
| Savings accounts | 90,246 | 395 | 0.44 | | 57,513 | 335 | 0.58 | |
| Money market accounts | 613,546 | 3,243 | 0.53 | | 450,362 | 3,018 | 0.67 | |
| Certificate accounts | 790,038 | 12,605 | 1.60 | | 1,177,335 | 20,887 | 1.77 | |
| Deposits | 1,644,859 | 16,741 | 1.02 | | 1,814,464 | 24,815 | 1.37 | |
| FHLB advances | 93,325 | 1,788 | 1.91 | | 93,755 | 3,821 | 4.08 | |
| Securities sold under agreements to repurchase | 17,806 | 70 | 0.39 | | — | — | — | |
| Long-term debt | 61,857 | 1,333 | 2.16 | | 62,506 | 2,046 | 3.27 | |
| Other borrowings | — | 16 | — | | — | 16 | — | |
| Total interest-bearing liabilities | 1,817,847 | 19,948 | 1.10 | | 1,970,725 | 30,698 | 1.56 | |
| Other noninterest-bearing liabilities | 365,055 | | | | 260,539 | | | |
| Total liabilities | 2,182,902 | | | | 2,231,264 | | | |
| Shareholders' equity | 209,629 | | | | 68,537 | | | |
| Total liabilities and shareholders' equity | $2,392,531 | | | | $2,299,801 | | | |
| Net interest income (3) | | $62,550 | | | | $48,794 | | |
| Net interest spread | | | 2.71 | % | | | 2.28 | % |
| Impact of noninterest-bearing sources | | | 0.18 | % | | | 0.08 | % |
| Net interest margin | | | 2.89 | % | | | 2.36 | % |

(1) The average balances of nonaccrual assets and related income, if any, are included in their respective categories.
(2) Includes loan balances that have been foreclosed and are now reclassified to other real estate owned.
(3) Includes taxable-equivalent adjustments primarily related to tax-exempt income on certain loans and securities of $1.8 million and $300 thousand for the years ended 2012 and 2011, respectively. The estimated federal statutory tax rate was 36% for the periods presented.

We do not include interest collected on nonaccrual loans in interest income. When we place a loan on nonaccrual status, we reverse the accrued unpaid interest receivable against interest income and amortization of any net deferred fees is suspended. Additionally, if a nonaccrual loan is placed back on accrual status or paid off, the accumulated interest collected on the loan is recognized at the time the loan is removed from nonaccrual status. The net decrease to interest income due to adjustments made for nonaccrual loans, including the effect of additional interest income that would have been recorded during the period if the loans had been accruing, was $1.1 million and $4.9 million for the years ended December 31, 2012 and 2011, respectively.

Table of Contents

Rate and Volume Analysis

The following table presents the extent to which changes in interest rates and changes in the volume of our interest-earning assets and interest-bearing liabilities have affected our interest income and interest expense, excluding interest income from nonaccrual loans. Information is provided in each category with respect to: (1) changes attributable to changes in volume (changes in volume multiplied by prior rate), (2) changes attributable to changes in rate (changes in rate multiplied by prior volume), (3) changes attributable to changes in rate and volume (change in rate multiplied by change in volume), which were allocated in proportion to the percentage change in average volume and average rate and included in the relevant column and (4) the net change.

| | Year Ended December 31, 2012 vs. 2011 Increase (Decrease) Due to | | |
|---|---|---|---|
| (in thousands) | Rate | Volume | Total Change |
| Assets: | | | |
| Interest-earning assets: | | | |
| Cash & cash equivalents | $(67) | $(167) | $(234) |
| Investment securities | 1,312 | 2,669 | 3,981 |
| Loans held for sale | (1,339) | 8,450 | 7,111 |
| Total loans held for investment | 2 | (7,854) | (7,852) |
| Total interest-earning assets | (92) | 3,098 | 3,006 |
| Liabilities: | | | |
| Deposits: | | | |
| Interest-bearing demand accounts | (164) | 87 | (77) |
| Savings accounts | (98) | 158 | 60 |
| Money market accounts | (723) | 948 | 225 |
| Certificate accounts | (1,941) | (6,341) | (8,282) |
| Total interest-bearing deposits | (2,926) | (5,148) | (8,074) |
| FHLB advances | (2,015) | (18) | (2,033) |
| Securities sold under agreements to repurchase | — | 70 | 70 |
| Long-term debt | (692) | (21) | (713) |
| Total interest-bearing liabilities | (5,633) | (5,117) | (10,750) |
| Total changes in net interest income | $5,541 | $8,215 | $13,756 |

Net Interest Income

Our profitability depends significantly on net interest income, which is the difference between income earned on our interest-earning assets, primarily loans and investment securities, and interest paid on interest-bearing liabilities. Our interest-bearing liabilities consist primarily of deposits and borrowed funds, including our outstanding trust preferred securities and advances from the FHLB.

Net interest income on a tax equivalent basis was $62.6 million for the year ended December 31, 2012, an increase of $13.8 million, or 28.2%, from $48.8 million for the year ended December 31, 2011. During 2012, total interest income increased $3.0 million from 2011, while total interest expense declined $10.8 million from 2011. The net interest margin for the year ended December 31, 2012 improved to 2.89% from 2.36% in 2011. Total average interest-earning assets increased in 2012 as higher mortgage production volumes resulted in a higher average balance of loans held for sale, partially offset by a decrease in cash and cash equivalents which was used to fund loans held for sale production.

Average balances of investment securities increased primarily as a result of the investment of proceeds from our initial public offering. Total average interest-bearing deposit balances declined from 2011, mostly reflecting our deposit and pricing strategy, resulting in a managed reduction of higher-cost certificates of deposit and replacement with transaction and savings deposits.

Table of Contents

Total interest income on a tax equivalent basis of $82.5 million in 2012 increased $3.0 million, or 3.8%, from $79.5 million in 2011, primarily driven by increased average interest-earning assets. Our average balance of loans held for sale increased by $232.5 million, or 184%, due primarily to our increased closed loan volume during 2012. The increase in interest income also reflects a higher average balance of investment securities, which increased $104.0 million, or 33.9%, in 2012 from 2011. We invested proceeds from the sale of loans and our initial public offering in investment securities with a shift towards higher-yielding municipal securities, resulting in an increase in yield on investment securities of 38 basis points. These increases were partially offset by a decrease in the average balance of loans held for investment, which decreased $175.0 million, or 11.8%, compared to 2011 and a lower yield on average loans held for sale, which decreased 90 basis points as mortgage interest rates declined during 2012.

Total interest expense of $19.9 million in 2012 decreased $10.8 million, or 35.0%, from $30.7 million in 2011. This decrease was primarily due to a $387.3 million, or 32.9%, decline in the average balance of higher-yielding certificates of deposit, partially offset by an increase in lower cost transaction and savings deposits as we expand our deposit and lending branch network. Also contributing to the decrease in interest expense was the restructuring of FHLB advances, prepaying certain long-term advances and using short-term FHLB advances to meet short-term mortgage origination and sales funding needs, which contributed to a 217 basis point decline in interest cost on FHLB advances.

Provision for Loan Losses

Our loan loss provision expense for 2012 was $11.5 million compared to $3.3 million for 2011. Asset quality trends continue to improve as our nonperforming assets ("NPAs") of $53.8 million at December 31, 2012 declined from $115.1 million at December 31, 2011. Nonaccrual loans of $29.9 million at December 31, 2012 declined $46.6 million, or 60.9%, from $76.5 million at December 31, 2011.

Net charge-offs of $26.5 million for 2012 were up $1.5 million from net charge-offs of $25.1 million for 2011. Net charge-offs during 2012 included an $11.8 million charge-off related to the settlement of collection litigation and resolution of certain related nonperforming construction/land development loans with aggregate carrying values of $26.6 million. For a more detailed discussion on our allowance for loan losses and related provision for loan losses, see Credit Risk Management within Management’s Discussion and Analysis in this Form 10-K.

Noninterest Income

Noninterest income was $237.5 million for the year ended December 31, 2012, an increase of $140.3 million, or 144%, from 2011. Our noninterest income is heavily dependent upon our single family mortgage banking activities, which are comprised of mortgage origination and sale activities and mortgage servicing activities. The level of our mortgage banking activity fluctuates and is influenced by mortgage interest rates, the economy, employment and housing affordability, among other factors. Noninterest income in 2012 benefited from increased single family loan production, as borrowers continued to take advantage of historically low mortgage interest rates, and the expansion of our mortgage lending operations. Our single family mortgage banking closed loan originations designated for sale increased to $4.67 billion in 2012 from $1.70 billion in 2011 as we continue to grow our mortgage origination and production capacity and increased our mortgage lending and support personnel by 146% during 2012. The increase in noninterest income, predominantly due to higher net gain on mortgage loan origination and sale activities, is detailed in the tables below.

Noninterest income consisted of the following:

Table of Contents

| (in thousands) | Year Ended December 31, 2012 | 2011 | Dollar Change | Percentage Change |
|---|---|---|---|---|
| Noninterest income | | | | |