

STERLING FINANCIAL CORP /WA/  
Form 424B3  
October 25, 2011

Filed Pursuant to Rule 424(B)(3)  
Registration Statement No. 333-169579

PROSPECTUS SUPPLEMENT  
(To Prospectus dated November 16, 2010)

STERLING FINANCIAL CORPORATION

---

RECENT DEVELOPMENTS

We have attached to this prospectus supplement our Current Report on Form 8-K filed with the Securities and Exchange Commission on October 25, 2011.

---

October 25, 2011

---

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

---

FORM 8-K

CURRENT REPORT

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

Date of Report (Date of earliest event reported): October 25, 2011

---

STERLING FINANCIAL CORPORATION  
(Exact name of registrant as specified in its charter)

Washington  
(State or other jurisdiction of  
incorporation or organization)

001-34696  
(Commission File Number)

91-1572822  
(I.R.S. Employer  
Identification No.)

111 North Wall Street, Spokane, Washington 99201  
(Address of principal executive offices) (Zip Code)

(509) 458-3711  
(Registrant's telephone number, including area code)

Not Applicable  
(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))



INFORMATION TO BE INCLUDED IN THE REPORT

Item 2.02. Results of Operations and Financial Condition.

On October 25, 2011, Sterling Financial Corporation ("Sterling") issued a press release regarding its results of operations and financial condition for the quarter ended September 30, 2011. The text of the press release is included as Exhibit 99.1 to this report. The information included in the press release is considered to be "furnished" under the Securities Exchange Act of 1934. Sterling will include final financial statements and additional analyses for the period ended September 30, 2011, as part of its quarterly report on Form 10-Q covering that period.

Item 9.01. Financial Statements and Exhibits.

(d) The following exhibit is being furnished herewith:

Exhibit No.	Exhibit Description
99.1	Press release text of Sterling Financial Corporation dated October 25, 2011.

---

S I G N A T U R E

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

STERLING FINANCIAL CORPORATION  
(Registrant)

October 25, 2011  
Date

By: /s/ Patrick J. Rusnak  
Patrick J. Rusnak  
Chief Financial Officer

EXHIBIT INDEX

Exhibit No. Exhibit Description

99.1 Press release text of Sterling Financial Corporation dated October 25, 2011.

---

Exhibit 99.1

Sterling Financial Corporation of Spokane, Wash. Reports Third Quarter 2011 Earnings and Operating Results

SPOKANE, Wash.--(BUSINESS WIRE)--October 25, 2011--Sterling Financial Corporation (NASDAQ:STSA), the bank holding company of Sterling Savings Bank, today announced results for the quarter ended September 30, 2011. For the quarter, Sterling recorded net income available to common shareholders of \$11.3 million, or \$0.18 per diluted common share, compared to \$7.6 million, or \$0.12 per diluted common share, for the second quarter of 2011.

Sterling's prior year third quarter results included a net loss of \$48.0 million and a one-time, non-cash increase to income available to common shareholders of \$84.3 million related to the conversion of preferred stock held by the U.S. Treasury into common shares in connection with Sterling's \$730 million recapitalization completed during that quarter. As a result, Sterling reported third quarter 2010 net income available to common shareholders of \$33.6 million, or \$1.31 per diluted common share (with the per share amount adjusted for a 1-for-66 reverse stock split in November 2010).

Following are selected financial highlights for the third quarter of 2011:

- Third consecutive quarter of positive earnings and earnings growth.
- Classified assets declined by \$103.3 million, or 17 percent, for the quarter.
- Net interest margin expanded to 3.34 percent, improving 3 basis points for the quarter, and 57 basis points over the third quarter of 2010.
- Deposit funding costs declined 5 basis points as transaction, savings and money market deposit accounts ("MMDA") average balances increased by \$81.5 million, or 2 percent, compared to the linked quarter.
- Noninterest expenses declined by \$5.0 million, or 5 percent, from the linked quarter and declined \$7.6 million, or 8 percent from the third quarter of last year.
- Tier 1 leverage ratio increased to 11.1 percent.

Greg Seibly, Sterling's president and chief executive officer noted, "This marks the third successive quarter of improved earnings growth. The results in the third quarter were driven by continued focus on our primary operating objectives: improving our deposit mix, reducing problem assets, originating quality loans and expense control. With lower levels of nonperforming assets, we were able to reduce the level of loan loss provision, OREO expense, and nonaccrual interest reversals from the linked quarter, all of which contributed to improved earnings during the quarter. Additionally, earnings benefited from higher income from mortgage banking operations and lower operating expenses, resulting in net income growth of \$3.8 million, or 50 percent, over last quarter."

#### Balance Sheet Management

Seibly continued, "We reported another quarter of solid loan originations. We were able to offset declines in the construction portfolio with expansion of the multifamily portfolio, which increased 22 percent for the quarter and more than doubled over the past 12 months. This is a result of a strategy implemented last year to bolster our loan portfolio with increased focus on the multifamily segment."

Sept 30, 2011

June 30, 2011

Sept 30, 2010

Edgar Filing: STERLING FINANCIAL CORP /WA/ - Form 424B3

	Amount	% of Loans	Amount	% of Loans	Amount	% of Loans	Annual % Change
			(in thousands)				
Total assets	\$9,175,874		\$9,241,595		\$10,030,043		-9%
Investments and MBS	2,448,423		2,496,056		2,722,917		-10%
Loans receivable:							
Residential real estate	701,921	13%	712,638	13%	752,763	13%	-7%
Multifamily real estate	990,707	18%	811,917	14%	445,193	8%	123%
Commercial real estate	1,287,381	23%	1,324,058	24%	1,326,971	22%	-3%
Construction	221,611	4%	308,273	6%	720,140	12%	-69%
Consumer	683,972	12%	703,675	13%	787,193	13%	-13%
Commercial banking	1,729,626	30%	1,741,819	30%	1,885,570	32%	-8%
Gross loans receivable	\$5,615,218	100%	\$5,602,380	100%	\$ 5,917,830	100%	-5%

---



Loan originations for the third quarter of 2011 were \$893.6 million, including portfolio loan originations of \$348.4 million, representing an increase in portfolio originations of 225 percent over the year-ago period. This growth in originations was primarily within the multifamily portfolio, with originations of \$203.6 million for the third quarter of 2011, compared to zero in the third quarter of 2010. Commercial banking loan originations were \$96.8 million during the third quarter of 2011, compared to \$24.6 million in the third quarter of 2010, representing an increase of 294 percent. The impact of the strong originations on the total loan portfolio were partially offset by reductions due to resolutions of nonperforming loans.

	Sept 30, 2011	June 30, 2011	Sept 30, 2010	Annual % Change
	(in thousands)			
Deposits:				
Retail:				
Transaction	\$1,675,741	\$1,572,771	\$1,495,495	12%
Savings and MMDA	1,814,682	1,710,527	1,533,666	18%
Time deposits	2,150,998	2,279,025	3,002,924	-28%
Total retail	5,641,421	5,562,323	6,032,085	-6%
Public	466,423	561,651	559,626	-17%
Brokered	371,396	480,024	317,503	17%
Total deposits	\$6,479,240	\$6,603,998	\$6,909,214	-6%
Gross loans to deposits	87%	85%	86%	1%
				Annual Basis Point Change
Funding costs:				
Cost of deposits	0.86%	0.91%	1.27%	(41)
Total funding liabilities	1.27%	1.31%	1.69%	(42)

During the quarter, Sterling continued its strategy of repositioning its deposit base by allowing higher-rate CDs to run off in order to reduce funding costs, resulting in a reduction of deposit costs of 41 basis points compared to the same period last year. Retail transaction, savings and MMDA account balances grew by 15 percent year-over-year, while retail time deposits, public deposits and brokered deposits, in the aggregate, declined by 23 percent.

At September 30, 2011, Sterling had total shareholders' equity of \$859.5 million, compared to \$807.6 million at June 30, 2011, and \$845.0 million at September 30, 2010. Sterling's ratio of shareholders' equity to total assets was 9.4 percent at September 30, 2011, compared to 8.7 percent at June 30, 2011. The Tier 1 leverage ratio increased to 11.1 percent at September 30, 2011, from 10.9 percent at June 30, 2011. Tangible common equity to tangible assets increased to 9.2 percent at September 30, 2011, from 8.6 percent at June 30, 2011.

## Operating Results

## Net Interest Income

Sterling reported net interest income of \$74.8 million for the quarter ended September 30, 2011, unchanged from the linked quarter and up from \$67.4 million for the same period a year ago.

	Sept 30, 2011	Three Months Ended June 30, 2011 (in thousands)	Sept 30, 2010
Net interest income	\$ 74,836	\$ 74,807	\$ 67,435
Net interest margin (tax equivalent)	3.34%	3.31%	2.77%
Loan yield	5.47%	5.33%	5.02%

Interest income on loans was \$82.0 million for the third quarter of 2011, compared to \$79.7 million for the linked quarter, reflecting higher loan yields. Contributing to the higher loan yields was the lower level of interest reversal on nonperforming loans. Reversal of interest income on nonperforming loans reduced the net interest margin by 26 basis points for the third quarter of 2011, compared to 42 basis points for the linked quarter and 70 basis points for the same period a year ago.

Interest income on mortgage backed securities was \$16.7 million for the third quarter of 2011, compared to \$19.9 million for the linked quarter. The reduction was a result of lower yields and lower balances due to the sale of longer duration, higher yielding securities during the linked quarter.

Interest expense of \$26.5 million was down \$1.0 million, or 4 percent, compared to the linked quarter. Total funding costs were 1.27 percent for the third quarter of 2011, compared to 1.31 percent for the second quarter of 2011, and 1.69 percent for the same period a year ago. The decrease is a result of replacing higher cost CDs with lower cost retail transaction accounts.

## Noninterest Income

For the third quarter of 2011, noninterest income was \$29.1 million, compared to \$34.3 million for the linked quarter and \$39.7 million for the same period a year ago. The decrease on a linked quarter basis was a result of Sterling not recording securities gains as no securities were sold during the third quarter of 2011, and of a fair value write down of the mortgage servicing rights asset.

For the quarter ended September 30, 2011, income from mortgage banking operations was \$16.4 million, up from \$10.8 million for the linked quarter, and down from \$19.4 million from the same period a year ago. The increase over the linked quarter is a result of higher levels of mortgage refinance activity in the historically low interest rate environment. Similarly, due to a decline in prevailing interest rates, Sterling recorded a fair value write down of \$5.1 million on its mortgage servicing rights asset, which resulted in negative loan servicing fees for the third quarter of 2011. The table below presents residential loan originations and sales for the periods indicated.

	Sept 30, 2011	Three Months Ended June 30, 2011	Sept 30, 2010	Annual % Change
--	------------------	--	------------------	--------------------

(in thousands)

Loan originations - residential real estate for sale	\$545,278	\$457,123	\$703,220	-22%
Loan sales - residential	475,034	398,120	520,612	-9%
				Annual Basis Point Change
Margin - residential loan sales	2.66%	2.21%	2.47%	19

Fees and service charges income contributed \$12.3 million to noninterest income for the third quarter of 2011, compared to \$12.9 million in the linked quarter and \$13.8 million in the same period a year ago. The reduction in fees and service charges income is primarily related to lower non-sufficient funds fees due to implementation of provisions related to the Dodd-Frank Act.

During the quarter ended September 30, 2011, Sterling did not record a gain on sales of securities, compared to a gain of \$8.3 million during the linked quarter and \$7.0 million for the same period a year ago.

For the quarter ended September 30, 2011, other noninterest income was \$3.5 million, compared to \$11,000 for the linked quarter, and a loss of \$1.0 million for the third quarter a year ago. The difference is primarily the result of higher gains on sales of loans, primarily SBA loans, for the third quarter of 2011.

#### Noninterest Expense

Noninterest expense was \$86.6 million for the third quarter of 2011, compared to \$91.6 million in the linked quarter and \$94.2 million for the same period a year ago. The decrease compared to the linked quarter was primarily the result of lower expenses related to other-real-estate-owned (OREO), which decreased by \$3.7 million. The \$7.6 million reduction of noninterest expense compared to the third quarter of last year primarily reflects lower expenses for professional fees and lower Federal Deposit Insurance Corporation deposit insurance premiums.

Included in other noninterest expense, data processing expense was \$5.7 million for the third quarter of 2011, compared to \$6.6 million for the linked quarter. During the linked quarter, Sterling completed the conversion to a new core operating system and is expected to support future growth and reduce associated operating expenses going forward. In connection with the core conversion, Sterling incurred \$1.2 million of non-recurring implementation expenses for the third quarter of 2011 and \$2.3 million for the second quarter of 2011.

#### Income Taxes

For the third quarter of 2011, Sterling did not recognize any federal or state tax expense, as the income tax expense for the quarter was offset by a reduction in the deferred tax valuation allowance.

Sterling uses an estimate of future earnings and an evaluation of its loss carryback ability and tax planning strategies to determine whether it is more likely than not that it will realize the benefit of its deferred tax asset. Sterling determined that it did not meet the required threshold as of September 30, 2011, and accordingly, a full valuation reserve was recorded against the net deferred tax asset. As of September 30, 2011, the reserved deferred tax asset was approximately \$335 million, including approximately \$288 million of net operating loss and tax credit carryforwards.

With regard to the deferred tax asset, the benefits of Sterling's accumulated tax losses would be reduced in the event of an "ownership change," as determined under Section 382 of the Internal Revenue Code. In order to preserve the benefits of these tax losses, during 2010 Sterling's shareholders approved a protective amendment to the restated articles of incorporation and Sterling's board adopted a tax preservation rights plan, both of which restrict certain stock transfers that would result in investors acquiring more than 4.95 percent of Sterling's total outstanding common stock.

#### Credit Quality

Seibly commented, "Our delinquencies, nonaccrual loans and classified assets are less than half of what they were a year ago. We continue our focus on getting asset quality issues behind us. During the third quarter, classified assets were reduced 17 percent, coming off the heels of the second quarter when they were reduced by 26 percent. We expect the pace of resolutions to continue through the remainder of the year."

For the third quarter of 2011, Sterling reported a provision for credit losses of \$6.0 million, compared to \$10.0 million for the linked quarter and \$60.9 million for the same period a year ago. Net charge-offs for the third quarter of 2011 declined to \$29.9 million, compared to \$33.4 million for the linked quarter, and \$77.1 million for the same period a year ago. The loan loss allowance at September 30, 2011 was \$186.2 million, or 3.32 percent, of total loans, compared to \$212.1 million, or 3.79 percent, of total loans at June 30, 2011.

The reduction in the allowance as a percent of total loans reflects the continued improvement in asset quality metrics and charge-offs during the quarter. At September 30, 2011, classified assets were \$500.5 million, a reduction of \$103.3 million, or 17 percent, from June 30, 2011, and down \$821.8 million, or 62 percent, from September 30, 2010. These reductions were a result of improved risk ratings, sales of OREO, and net charge-offs. Nonperforming assets were \$434.7 million at September 30, 2011, compared to \$497.5 million at June 30, 2011, and \$965.8 million at September 30, 2010, representing reductions of 13 percent and 55 percent, respectively. At September 30, 2011, nonperforming assets as a percentage of total assets were 4.74 percent, compared to 5.38 percent at June 30, 2011, and 9.63 percent at September 30, 2010.

As of September 30, 2011, OREO, which is included in nonperforming assets, was \$111.6 million, compared to \$101.4 million at June 30, 2011 and \$156.8 million at September 30, 2010. During the third quarter of 2011, Sterling sold 163 properties with a carrying value of \$40.8 million.

The following table presents an analysis of Sterling's nonperforming assets by loan category and geographic region as of the dates indicated.

Nonperforming Asset Analysis	Sept 30, 2011		June 30, 2011		Sept 30, 2010	
Residential construction	(in thousands)					
Puget Sound	\$ 15,535	4%	\$ 21,121	4%	\$ 87,431	9%
Portland, OR	13,553	3%	21,014	4%	59,506	6%
Vancouver, WA	1,401	0%	1,829	0%	14,307	1%
Northern California	4,565	1%	5,387	1%	15,658	2%
Southern California	1,533	0%	1,652	0%	5,168	1%
Bend, OR	381	0%	993	0%	9,183	1%
Other						