WESTAMERICA BANCORPORATION
Form 10-Q
November 02, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018

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: 001-09383

WESTAMERICA BANCORPORATION

(Exact Name of Registrant as Specified in Its Charter)

CALIFORNIA	94-2156203
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

1108 FIFTH AVENUE, SAN RAFAEL, CALIFORNIA 94901

(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code (707) 863-6000

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 No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer
Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

Title of Class	Shares outstanding as of October 29, 2018
Common Stock, No Par Value	26,727,416

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FORWARD-LOOKING STATEMENTS

This report on Form 10-Q contains forward-looking statements about Westamerica Bancorporation (the “Company”) for which it claims the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, future credit quality and performance, the appropriateness of the allowance for loan losses, loan growth or reduction, mitigation of risk in the Company’s loan and investment securities portfolios, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of the Company or its management or board of directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes", "anticipates", "expects", “estimates”, "intends", "targeted", "projected", “forecast”, "continue", "remain", "will", "should", "may" and other similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

These forward-looking statements are based on Management’s current knowledge and belief and include information concerning the Company’s possible or assumed future financial condition and results of operations. A number of factors, some of which are beyond the Company’s ability to predict or control, could cause future results to differ materially from those contemplated. These factors include but are not limited to (1) the length and severity of difficulties in the global, national and California economies and the effects of government efforts to address those difficulties; (2) liquidity levels in capital markets; (3) fluctuations in asset prices including, but not limited to stocks, bonds, real estate, and commodities; (4) the effect of acquisitions and integration of acquired businesses; (5) economic uncertainty created by terrorist threats and attacks on the United States, the actions taken in response, and the uncertain effect of these events on the national and regional economies; (6) changes in the interest rate environment; (7) changes in the regulatory environment; (8) competitive pressure in the banking industry; (9) operational risks including a failure or breach in data processing or security systems or those of third party vendors and other service providers, including as a result of cyber attacks or fraud; (10) volatility of interest rate sensitive loans, deposits and investments; (11) asset/liability management risks and liquidity risks; (12) the effect of natural disasters, including earthquakes, fire, flood, drought, and other disasters, on the uninsured value of the Company’s assets and of loan collateral, the financial condition of debtors and issuers of investment securities, the economic conditions affecting the Company’s market place, and commodities and asset values; (13) changes in the securities markets and (14) the outcome of contingencies, such as legal proceedings. However, the reader should not consider the above-mentioned factors to be a complete set of all potential risks or uncertainties.

Forward-looking statements speak only as of the date they are made. The Company undertakes no obligation to update any forward-looking statements in this report to reflect circumstances or events that occur after the date forward looking statements are made, except as may be required by law. The reader is directed to the Company's annual report on Form 10-K for the year ended December 31, 2017, for further discussion of factors which could affect the Company's business and cause actual results to differ materially from those expressed in any forward-looking statement made in this report.

PART I - FINANCIAL INFORMATION

Item 1 **Financial Statements**

WESTAMERICA BANCORPORATION

CONSOLIDATED BALANCE SHEETS

(unaudited)

(In thousands)

	At September 30, 2018	At December 31, 2017
Assets:		
Cash and due from banks	$522,660	$575,002
Equity securities	1,734	1,800
Debt securities available for sale	2,478,908	2,191,707
Debt securities held to maturity, with fair values of: $1,002,648 at September 30, 2018 and $1,155,342 at December 31, 2017	1,025,699	1,158,864
Loans	1,196,955	1,287,982
Allowance for loan losses	(22,027)	(23,009)
Loans, net of allowance for loan losses	1,174,928	1,264,973
Other real estate owned	620	1,426
Premises and equipment, net	35,391	35,301
Identifiable intangibles, net	2,376	3,850
Goodwill	121,673	121,673
Other assets	165,474	158,450
Total Assets	$5,529,463	$5,513,046
Liabilities:		
Noninterest-bearing deposits	$2,211,028	$2,197,526
Interest-bearing deposits	2,624,809	2,630,087
Total deposits	4,835,837	4,827,613
Short-term borrowed funds	61,756	58,471
Other liabilities	39,279	36,723
Total Liabilities	4,936,872	4,922,807

Contingencies (Note 10)

Shareholders' Equity:

Common stock (no par value), authorized - 150,000 shares Issued and outstanding: 26,727 at September 30, 2018 and 26,425 at December 31, 2017	447,785	431,734
Deferred compensation	1,395	1,533
Accumulated other comprehensive loss	(54,066)	(16,832)
Retained earnings	197,477	173,804
Total Shareholders' Equity	592,591	590,239
Total Liabilities and Shareholders' Equity	$5,529,463	$5,513,046

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(unaudited)

	For the Three Months Ended September 30,		For the Nine Months	
	2018	2017	2018	2017
	(In thousands, except per share data)			
Interest and Loan Fee Income:				
Loans	$14,593	$15,082	$44,247	$46,330
Equity securities	85	70	256	214
Debt securities available for sale	15,644	11,277	43,518	32,091
Debt securities held to maturity	5,931	6,716	18,321	20,997
Total Interest and Loan Fee Income	36,253	33,145	106,342	99,632
Interest Expense:				
Deposits	518	461	1,417	1,395
Short-term borrowed funds	9	12	28	34
Total Interest Expense	527	473	1,445	1,429
Net Interest and Loan Fee Income	35,726	32,672	104,897	98,203
Reversal of Provision for Loan Losses	-	-	-	(1,900)
Net Interest and Loan Fee Income After Reversal of Provision for Loan Losses	35,726	32,672	104,897	100,103
Noninterest Income:				
Service charges on deposit accounts	4,615	4,989	14,012	14,857
Merchant processing services	2,464	2,153	7,190	6,080
Debit card fees	1,656	1,784	4,959	4,851
Trust fees	733	718	2,202	2,136
ATM processing fees	687	684	2,049	1,914
Other service fees	665	652	1,946	1,964
Life insurance gains	585	-	585	-
Financial services commissions	132	148	387	484
Equity securities losses	(16)	-	(66)	-
Other noninterest income	1,007	1,420	2,988	4,042
Total Noninterest Income	12,528	12,548	36,252	36,328
Noninterest Expense:				
Salaries and related benefits	13,415	12,816	39,952	38,867
Occupancy and equipment	4,809	4,907	14,365	14,571
Loss contingency	3,500	-	3,500	-
Outsourced data processing services	2,292	2,383	6,930	6,710
Professional fees	621	512	2,277	1,533
Amortization of identifiable intangibles	451	760	1,474	2,322

Courier service	448	451	1,333	1,310
Other noninterest expense	1,469	2,285	5,365	7,812
Total Noninterest Expense	27,005	24,114	75,196	73,125
Income Before Income Taxes	21,249	21,106	65,953	63,306
Provision for income taxes	4,256	6,089	13,444	17,441
Net Income	$16,993	$15,017	$52,509	$45,865
Average Common Shares Outstanding	26,701	26,309	26,622	26,260
Average Diluted Common Shares Outstanding	26,815	26,404	26,736	26,379
Per Common Share Data:				
Basic earnings	$0.64	$0.57	$1.97	$1.75
Diluted earnings	0.63	0.57	1.96	1.74
Dividends paid	0.40	0.39	1.20	1.17

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited)

	For the Three Months		For the Nine Months	
	Ended September 30,			
	2018	2017	2018	2017
	(In thousands)			
Net income	$16,993	$15,017	$52,509	$45,865
Other comprehensive (loss) income:				
Changes in unrealized gains on debt securities available for sale	(5,915)	4,179	(47,915)	11,413
Deferred tax benefit(expense)	1,749	(1,757)	14,164	(4,799)
Changes in unrealized gains on debt securities available for sale, net of tax	(4,166)	2,422	(33,751)	6,614
Post-retirement benefit transition obligation amortization	-	15	-	45
Deferred tax expense	-	(6)	-	(18)
Post-retirement benefit transition obligation amortization, net of tax	-	9	-	27
Total other comprehensive (loss) income	(4,166)	2,431	(33,751)	6,641
Total comprehensive income	$12,827	$17,448	$18,758	$52,506

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(unaudited)

	Common Shares Outstanding	Common Stock	Deferred Compensation	Accumulated Other Comprehensive (Loss) Income	Retained Earnings	Total
	(In thousands)					
Balance, December 31, 2016	25,907	$404,606	$ 1,533	$ (10,074)	$165,302	$561,367
Net income for the period					45,865	45,865
Other comprehensive income				6,641		6,641
Exercise of stock options	403	18,988				18,988
Restricted stock activity	13	707				707
Stock based compensation		1,368				1,368
Stock awarded to employees	2	76				76
Retirement of common stock	(6)	(90)			(224)	(314)
Dividends					(30,741)	(30,741)
Balance, September 30, 2017	26,319	$425,655	$ 1,533	$ (3,433)	$180,202	$603,957
Balance, December 31, 2017	26,425	$431,734	$ 1,533	$ (16,832)	$173,804	$590,239
Cumulative effect of equity securities losses reclassified				142	(142)	-
Adjusted Balance, January 1, 2018	26,425	431,734	1,533	(16,690)	173,662	590,239
Reclass stranded tax effects resulting from the Tax Cuts and Jobs Act				(3,625)	3,625	-
Net income for the period					52,509	52,509
Other comprehensive loss				(33,751)		(33,751)
Exercise of stock options	289	13,245				13,245
Restricted stock activity	20	1,281	(138)			1,143
Stock based compensation		1,575				1,575
Stock awarded to employees	2	99				99
Retirement of common stock	(9)	(149)			(375)	(524)
Dividends					(31,944)	(31,944)
Balance, September 30, 2018	26,727	$447,785	$ 1,395	$ (54,066)	$197,477	$592,591

See accompanying notes to unaudited consolidated financial statements.

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WESTAMERICA BANCORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	For the Nine Months Ended September 30,	
	2018	2017
	(In thousands)	
Operating Activities:		
Net income	$52,509	$45,865
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	18,964	18,807
Reversal of provision for loan losses	-	(1,900)
Net amortization of deferred loan (fees) cost	(181)	34
(Increase) decrease in interest income receivable	(177)	713
Life insurance premiums paid	(609)	(126)
Increase in other assets	(1,287)	(2,088)
Increase in income taxes payable	7,760	2,461
(Increase) decrease in net deferred tax asset	(1,345)	895
Stock option compensation expense	1,575	1,368
Increase (decrease) in interest expense payable	5	(8)
Increase (decrease) in other liabilities	3,793	(1,142)
Life insurance gains	(585)	-
Equity securities losses	66	-
Net writedown of premises and equipment	3	60
Net gain on sale of foreclosed assets	(94)	(72)
Writedown of foreclosed assets	27	219
Net Cash Provided by Operating Activities	80,424	65,086
Investing Activities:		
Net repayments of loans	91,594	69,319
Net payments under FDIC[(1)] indemnification agreements	-	(63)
Proceeds from life insurance	1,183	-
Purchases of debt securities available for sale	(634,113)	(433,525)
Proceeds from sale/maturity/calls of debt securities available for sale	290,663	238,888
Proceeds from maturity/calls of debt securities held to maturity	127,578	135,208
Purchases of premises and equipment	(2,830)	(1,980)
Net change in FRB[(2)] stock	-	1
Proceeds from sale of foreclosed assets	873	1,521
Net Cash (Used in) Provided by Investing Activities	(125,052)	9,369
Financing Activities:		
Net change in deposits	8,224	29,839
Net change in short-term borrowings	3,285	7,259

Exercise of stock options	13,245	18,988
Retirement of common stock	(524)	(314)
Common stock dividends paid	(31,944)	(30,741)
Net Cash (Used in) Provided by Financing Activities	(7,714)	25,031
Net Change In Cash and Due from Banks	(52,342)	99,486
Cash and Due from Banks at Beginning of Period	575,002	462,271
Cash and Due from Banks at End of Period	$522,660	$561,757
Supplemental Cash Flow Disclosures:		
Supplemental disclosure of non cash activities:		
Loan collateral transferred to other real estate owned	$-	$-
Securities purchases pending settlement	-	811
Supplemental disclosure of cash flow activities:		
Interest paid for the period	1,440	1,437
Income tax payments for the period	7,028	14,657

See accompanying notes to unaudited consolidated financial statements.

(1) Federal Deposit Insurance Corporation ("FDIC")

(2) Federal Reserve Bank ("FRB")

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission and follow general practices within the banking industry. The results of operations reflect interim adjustments, all of which are of a normal recurring nature and which, in the opinion of Management, are necessary for a fair presentation of the results for the interim periods presented. The interim results for the three and nine months ended September 30, 2018 are not necessarily indicative of the results expected for the full year. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes as well as other information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Note 2: Accounting Policies

The most significant accounting policies followed by the Company are presented in Note 1 to the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017. These policies, along with the disclosures presented in the other financial statement notes and in this discussion, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, it is reasonably possible conditions could change materially affecting results of operations and financial conditions.

Application of these principles requires the Company to make certain estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions, and judgments. Certain accounting policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment writedown or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available.

Certain amounts in prior periods have been reclassified to conform to the current presentation.

Recently Adopted Accounting Standards

In the nine months ended September 30, 2018, the Company adopted the following new accounting guidance:

FASB Accounting Standard Update (ASU) 2014-09, *Revenue (Topic 606): Revenue from Contracts with Customers,* was issued May 2014. The ASU specifies a standardized approach for revenue recognition across industries and transactions. The ASU also requires additional disclosures. The scope of the ASU does not include revenue streams covered by other ASU topics; thus, Topic 606 does not apply to revenue related to financial instruments, guarantees and leases, which are the primary sources of the Company's net interest income.

Approximately 73% of the Company's revenue, including all of its net interest income and a portion of its noninterest income, is out of scope of the guidance. The contracts that are in scope of the guidance are primarily related to service charges and fees on deposit accounts, merchant processing fees, debit card fees, ATM processing fees, trust fees and other service charges, commissions and fees. The Company's revenue recognition practices within the scope of the ASU as described below did not change in any material regard upon adoption of the ASU.

Service Charges on Deposit Accounts: The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Merchant Processing Services and Debit Card Fees: The Company earns interchange fees from cardholder transactions conducted through the payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Trust Fees: The Company earns trust fees from its contracts with customers to manage assets for investment or custody services. These fees are primarily earned over time as the Company provides the contracted monthly services and are generally assessed based on a tiered scale of the market value of assets under management (AUM) at month-end. Other related services provided, which are based on a fixed fee schedule, are recognized when the services are rendered.

Gains/Losses on Sales of OREO: The Company records a gain or loss from the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. The Company does not finance the sale of OREO.

The Company adopted the ASU on January 1, 2018 and no cumulative adjustment was required.

FASB ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,* was issued January 2016. The ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Most notably, the ASU changes the income statement impact of equity investments held by the Company and the requirement for the Company to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes (Note 9).

The Company was required to adopt the ASU provisions on January 1, 2018, and for those equity securities with readily determinable fair values, the Company elected the retrospective transition approach with a cumulative effect adjustment to the balance sheet and for those equity securities that do not have readily determinable fair values, the Company elected the prospective transition approach. The impact of the adoption of this accounting standard on the Company's consolidated financial statements will be subject to the price volatility of the equity investments. As a result of implementing the ASU provisions, effective January 1, 2018, the Company recorded a cumulative effect adjustment to retained earnings of $142 thousand.

FASB ASU 2018-02, *Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,* was issued February 2018. The ASU eliminates the stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 by allowing a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017. The Company early adopted the provisions of the ASU effective January 1, 2018, by reclassifying the

Company's $3,625 thousand stranded tax effect.

Recently Issued Accounting Standards

FASB ASU 2016-02, *Leases (Topic 842),* was issued February 25, 2016. The provisions of the new standard require lessees to recognize most leases on-balance sheet, increasing reported assets and liabilities. Lessor accounting remains substantially similar to current U.S. GAAP.

The Company will be required to adopt the ASU provisions effective January 1, 2019, and plans to elect the modified retrospective transition approach. Management is evaluating the impact that the ASU will have on the Company's financial statements. As of December 31, 2017, the Company leased 58 of its operating facilities; the remaining minimum lease payments were $17.5 million. The Company does not expect a material change in noninterest expenses upon adoption of the new standard.

FASB ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,* was issued on June 16, 2016. The ASU significantly changes estimates for credit losses related to financial assets measured at amortized cost and certain other contracts. For estimating credit losses, the FASB is replacing the incurred loss model with the current expected credit loss (CECL) model, which will accelerate recognition of credit losses. Additionally, credit losses relating to debt securities available-for-sale will be recorded through an allowance for credit losses under the new standard. The Company will also be required to provide additional disclosures related to the financial assets within the scope of the new standard.

The Company will be required to adopt the ASU provisions on January 1, 2020. Management has commenced an implementation project to include evaluating available data, defining portfolio segments of loans with similar attributes, and selecting loss estimate models for each identified loan portfolio segment. The ultimate adjustment to the allowance for loan losses will be accomplished through an offsetting after-tax adjustment to shareholders' equity. Management has also segmented debt securities held to maturity and selected methods to estimate losses for each segment. Economic conditions and the composition of the Company's loan portfolio at the time of adoption will influence the extent of the adopting accounting adjustment.

FASB ASU 2017-08, *Receivables – Non-Refundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*, was issued March 2017. The ASU will shorten the amortization period for certain callable debt securities held at a premium. Specifically, the ASU requires the premium to be amortized to the earliest call date. The ASU does not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity.

The Company will be required to adopt the ASU provisions on January 1, 2019. Management has evaluated the impact the ASU will have on the Company's financial statements relative to shareholder's equity and the change in monthly earnings and the impact is not expected to be material.

FASB ASU 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, was issued August 2017. The ASU will expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. The ASU also provides for a one-time reclassification of prepayable assets from held-to-maturity (HTM) to available for sale (AFS) regardless of derivative use.

The Company will be required to adopt the ASU provisions on January 1, 2019. The Company does not currently engage in trading activities or use derivative instruments to control interest rate risk, even though such activities may be permitted with the approval of the Company's Board of Directors. The Company has evaluated the prepayable assets in the HTM portfolio and will not effect a one-time reclassification of prepayable assets from HTM to the AFS upon implementation.

FASB ASU 2018-13, *Fair Value Measurements (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*, was issued August 2018. The ASU is part of the disclosure framework project, where the primary focus is to improve the effectiveness of disclosures in the financial statements. The ASU removes, modifies and adds disclosure requirements related to Fair Value Measurements.

The provisions of the ASU are effective January 1, 2020 with the option to early adopt any removed or modified disclosures upon issuance of the ASU. The Company early adopted the provisions to remove and/or modify relevant disclosures in Note 9 to the unaudited consolidated financial statements. The requirement to include additional disclosures will be adopted by the Company January 1, 2020. The additional disclosures will not affect the financial results upon adoption.

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Note 3: Investment Securities

Effective January 1, 2018, upon adoption of ASU 2016-01, equity securities included in the Company's available for sale portfolio of $1,800 thousand were reclassified to equity securities. The reclassification of equity securities resulted in recording a cumulative effect adjustment to retained earnings of $142 thousand, net of tax.

At September 30, 2018, the market value of equity securities was $1,734 thousand. During the nine months ended September 30, 2018, the Company recognized gross unrealized holding losses of $66 thousand in earnings.

An analysis of the amortized cost and fair value by major categories of debt securities available for sale, which are carried at fair value with net unrealized gains (losses) reported on an after-tax basis as a component of cumulative other comprehensive income, and debt securities held to maturity, which are carried at amortized cost, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
At September 30, 2018	(In thousands)			
Debt securities available for sale				
Securities of U.S. Government sponsored entities	$167,222	$ -	$(5,478)	$161,744
Agency residential mortgage-backed securities (MBS)	919,381	243	(41,595)	878,029
Non-agency residential MBS	122	2	-	124
Agency commercial MBS	1,877	-	(30)	1,847
Securities of U.S. Government entities	1,223	-	(13)	1,210
Obligations of states and political subdivisions	182,851	1,841	(4,349)	180,343
Corporate securities	1,282,991	411	(27,791)	1,255,611
Total debt securities available for sale	2,555,667	2,497	(79,256)	2,478,908
Debt securities held to maturity				
Agency residential MBS	468,354	200	(21,100)	447,454
Non-agency residential MBS	3,524	72	-	3,596
Obligations of states and political subdivisions	553,821	2,526	(4,749)	551,598
Total debt securities held to maturity	1,025,699	2,798	(25,849)	1,002,648
Total	$3,581,366	$ 5,295	$(105,105)	$3,481,556

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
At December 31, 2017	(In thousands)			

Debt securities available for sale				
Securities of U.S. Government sponsored entities	$122,285	$ 1	$ (2,967)	$119,319
Agency residential MBS	787,679	522	(20,495)	767,706
Non-agency residential MBS	153	1	-	154
Agency commercial MBS	2,244	-	(25)	2,219
Securities of U.S. Government entities	1,612	-	(22)	1,590
Obligations of states and political subdivisions	182,907	3,796	(1,482)	185,221
Corporate securities	1,123,671	1,104	(9,277)	1,115,498
Total debt securities available for sale	2,220,551	5,424	(34,268)	2,191,707
Debt securities held to maturity				
Agency residential MBS	545,883	606	(9,850)	536,639
Non-agency residential MBS	4,462	70	-	4,532
Agency commercial MBS	9,041	-	(66)	8,975
Obligations of states and political subdivisions	599,478	7,736	(2,018)	605,196
Total debt securities held to maturity	1,158,864	8,412	(11,934)	1,155,342
Total	$3,379,415	$ 13,836	$ (46,202)	$3,347,049

The amortized cost and fair value of debt securities by contractual maturity are shown in the following tables at the dates indicated:

	At September 30, 2018			
	Debt Securities Available for Sale		Debt Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Maturity in years:				
1 year or less	$128,356	$128,080	$90,266	$90,491
Over 1 to 5 years	1,355,592	1,323,725	220,377	219,016
Over 5 to 10 years	111,553	110,850	242,137	241,023
Over 10 years	38,786	36,253	1,041	1,068
Subtotal	1,634,287	1,598,908	553,821	551,598
MBS	921,380	880,000	471,878	451,050
Total	$2,555,667	$2,478,908	$1,025,699	$1,002,648

	At December 31, 2017			
	Debt Securities Available for Sale		Debt Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Maturity in years:				
1 year or less	$193,337	$193,385	$50,295	$51,105
Over 1 to 5 years	1,031,807	1,023,047	269,050	269,471
Over 5 to 10 years	159,266	160,042	277,170	281,546
Over 10 years	46,065	45,154	2,963	3,074
Subtotal	1,430,475	1,421,628	599,478	605,196
MBS	790,076	770,079	559,386	550,146
Total	$2,220,551	$2,191,707	$1,158,864	$1,155,342

Expected maturities of mortgage-related securities can differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties. In addition, such factors as prepayments and interest rates may affect the yield on the carrying value of mortgage-related securities. At September

30, 2018 and December 31, 2017, the Company had no high-risk collateralized mortgage obligations as defined by regulatory guidelines.

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An analysis of the gross unrealized losses of the debt securities available for sale portfolio follows:

Debt Securities Available for Sale
At September 30, 2018

	No. of Investment Positions	Less than 12 months Fair Value	Unrealized Losses	No. of Investment Positions	12 months or longer Fair Value	Unrealized Losses	No. of Investment Positions	Total Fair Value	Unrealized Losses
	($ in thousands)								
Securities of U.S. Government sponsored entities	5	$46,531	$(461)	8	$115,213	$(5,017)	13	$161,744	$(5,478)
Agency residential MBS	23	421,962	(9,816)	50	447,104	(31,779)	73	869,066	(41,595)
Agency commercial MBS	-	-	-	1	1,847	(30)	1	1,847	(30)
Securities of U.S. Government entities	-	-	-	2	1,210	(13)	2	1,210	(13)
Obligations of states and political subdivisions	43	32,193	(392)	74	67,715	(3,957)	117	99,908	(4,349)
Corporate securities	86	826,287	(16,386)	37	333,319	(11,405)	123	1,159,606	(27,791)
Total	157	$1,326,973	$(27,055)	172	$966,408	$(52,201)	329	$2,293,381	$(79,256)

An analysis of gross unrecognized losses of the debt securities held to maturity portfolio follows:

Debt Securities Held to Maturity
At September 30, 2018

	No. of Investment Positions	Less than 12 months Fair Value	Unrecognized Losses	No. of Investment Positions	12 months or longer Fair Value	Unrecognized Losses	No. of Investment Positions	Total Fair Value	Unrecognized Losses
	($ in thousands)								
Agency residential MBS	26	$34,278	$(952)	70	$404,842	$(20,148)	96	$439,120	$(21,100)
Obligations of states and political subdivisions	224	191,579	(1,540)	162	164,011	(3,209)	386	355,590	(4,749)
Total	250	$225,857	$(2,492)	232	$568,853	$(23,357)	482	$794,710	$(25,849)

The unrealized losses on the Company's debt securities were caused by market conditions for these types of investments, particularly changes in risk-free interest rates. The Company evaluates debt securities on a quarterly basis including changes in security ratings issued by rating agencies, changes in the financial condition of the issuer, and, for mortgage-backed and asset-backed securities, delinquency and loss information with respect to the underlying collateral, changes in the levels of subordination for the Company's particular position within the repayment structure and remaining credit enhancement as compared to expected credit losses of the security. Substantially all of these securities continue to be investment grade rated by a major rating agency. One corporate bond with a carrying value of $15.0 million and a market value of $14.1 million at September 30, 2018, is rated below investment grade. In addition to monitoring credit rating agency evaluations, Management performs its own evaluations regarding the credit worthiness of the issuer or the securitized assets underlying asset backed securities.

The Company does not intend to sell any debt securities and has concluded that it is more likely than not that it will not be required to sell the debt securities prior to recovery of the amortized cost basis. Therefore, the Company does not consider these debt securities to be other-than-temporarily impaired as of September 30, 2018.

The fair values of the debt securities could decline in the future if the general economy deteriorates, inflation increases, credit ratings decline, the issuer's financial condition deteriorates, or the liquidity for debt securities declines. As a result, other than temporary impairments may occur in the future.

As of September 30, 2018 and December 31, 2017, the Company had debt securities pledged to secure public deposits and short-term borrowed funds of $740,177 thousand and $715,774 thousand, respectively.

An analysis of gross unrealized losses of debt securities available for sale follows:

Debt Securities Available for Sale
At December 31, 2017

	Less than 12 months			12 months or longer			Total		
	No. of Investment Positions	Fair Value	Unrealized Losses	No. of Investment Positions	Fair Value	Unrealized Losses	No. of Investment Positions	Fair Value	Unrealized Losses
	($ in thousands)								
Securities of U.S. Government sponsored entities	1	$996	$(2)	8	$117,252	$(2,965)	9	$118,248	$(2,967)
Agency residential MBS	7	238,554	(1,501)	51	516,711	(18,994)	58	755,265	(20,495)
Non-agency residential MBS	1	1	-	-	-	-	1	1	-
Agency commercial; MBS	2	2,219	(25)	-	-	-	2	2,219	(25)
Securities of U.S. Government entities	-	-	-	3	1,590	(22)	3	1,590	(22)
Obligations of states and political subdivisions	50	21,453	(228)	35	52,071	(1,254)	85	73,524	(1,482)
Corporate securities	64	571,112	(4,047)	38	282,924	(5,230)	102	854,036	(9,277)
Total	125	$834,335	$(5,803)	135	$970,548	$(28,465)	260	$1,804,883	$(34,268)

An analysis of gross unrecognized losses of the debt securities held to maturity portfolio follows:

Debt Securities Held to Maturity
At December 31, 2017

Less than 12 months			12 months or longer			Total		
No. of Investment Positions	Fair Value	Unrecognized Losses	No. of Investment Positions	Fair Value	Unrecognized Losses	No. of Investment Positions	Fair Value	Unrecognized Losses
($ in thousands)								
15	$30,218	$ (201)	65	$479,775	$(9,649)	80	$509,993	$(9,850)

Agency residential MBS									
Agency commercial MBS	1	1,913	(4)	1	7,062	(62)	2	8,975	(66)
Obligations of states and political subdivisions	146	131,032	(553)	59	58,979	(1,465)	205	190,011	(2,018)
Total	162	$163,163	$ (758)	125	$545,816	$ (11,176)	287	$708,979	$ (11,934)

The following table provides information about the amount of interest income earned on investment securities which is fully taxable and which is exempt from regular federal income tax:

	For the Three Months		For the Nine Months	
	Ended September 30,			
	2018	2017	2018	2017
	(In thousands)			
Taxable	$16,780	$12,957	$47,327	$37,584
Tax-exempt from regular federal income tax	4,880	5,106	14,768	15,718
Total interest income from investment securities	$21,660	$18,063	$62,095	$53,302

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Note 4: Loans, Allowance for Loan Losses and Other Real Estate Owned

A summary of the major categories of loans outstanding is shown in the following table at the dates indicated.

	At September 30, 2018	At December 31, 2017
	(In thousands)	
Commercial	$276,031	$335,996
Commercial Real Estate	567,213	568,584
Construction	3,939	5,649
Residential Real Estate	48,150	65,183
Consumer Installment & Other	301,622	312,570
Total	$1,196,955	$1,287,982

Total loans outstanding reported above include loans purchased from the FDIC of $65,868 thousand and $83,478 thousand at September 30, 2018 and December 31, 2017, respectively. Loans purchased from the FDIC were separately reported in prior periods and have been reclassified into their respective categories in the current presentation.

Changes in the accretable yield for purchased loans were as follows:

	For the Nine Months Ended September 30, 2018	For the Year Ended December 31, 2017
Accretable yield:	(In thousands)	
Balance at the beginning of the period	$738	$ 1,237
Reclassification from nonaccretable difference	896	1,852
Accretion	(1,380)	(2,351)
Balance at the end of the period	$254	$ 738
Accretion	$(1,380)	$ (2,351)
Change in FDIC indemnification	2	192
(Increase) in interest income	$(1,378)	$ (2,159)

The following summarizes activity in the allowance for loan losses:

	Allowance for Loan Losses For the Three Months Ended September 30, 2018						
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Balance at beginning of period	$8,275	$ 3,789	$ 210	$ 1,064	$ 5,943	$ 3,759	$23,040
(Reversal) provision	(184)	372	44	(120)	(137)	25	-
Chargeoffs	(384)	(240)	-	-	(845)	-	(1,469)
Recoveries	103	-	-	-	353	-	456
Total allowance for loan losses	$7,810	$ 3,921	$ 254	$ 944	$ 5,314	$ 3,784	$22,027

	Allowance for Loan Losses For the Nine Months Ended September 30, 2018						
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Balance at beginning of period	$7,746	$ 3,849	$ 335	$ 995	$ 6,418	$ 3,666	$23,009
(Reversal) provision	(863)	312	(81)	(51)	565	118	-
Chargeoffs	(425)	(240)	-	-	(3,015)	-	(3,680)
Recoveries	1,352	-	-	-	1,346	-	2,698
Total allowance for loan losses	$7,810	$ 3,921	$ 254	$ 944	$ 5,314	$ 3,784	$22,027

Allowance for Loan Losses
For the Three Months Ended September 30, 2017

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Balance at beginning of period	$8,167	$ 3,545	$ 160	$ 1,105	$ 7,215	$ 3,911	$24,103
(Reversal) provision	(391)	288	136	(50)	167	(150)	-
Chargeoffs	(132)	-	-	-	(886)	-	(1,018)
Recoveries	128	-	-	-	415	-	543
Total allowance for loan losses	$7,772	$ 3,833	$ 296	$ 1,055	$ 6,911	$ 3,761	$23,628

Allowance for Loan Losses
For the Nine Months Ended September 30, 2017

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Balance at beginning of period	$8,327	$ 3,330	$ 152	$ 1,330	$ 7,980	$ 4,835	$25,954
(Reversal) provision	(220)	415	(1,755)	(275)	1,009	(1,074)	(1,900)
Chargeoffs	(961)	-	-	-	(3,783)	-	(4,744)
Recoveries	626	88	1,899	-	1,705	-	4,318
Total allowance for loan losses	$7,772	$ 3,833	$ 296	$ 1,055	$ 6,911	$ 3,761	$23,628

The allowance for loan losses and recorded investment in loans evaluated for impairment were as follows:

Allowance for Loan Losses and Recorded Investment in Loans Evaluated for Impairment
At September 30, 2018

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Individually evaluated for impairment	$4,668	$ 172	$ -	$ -	$ -	$ -	$4,840
Collectively evaluated for impairment	3,142	3,749	254	944	5,314	3,784	17,187
Purchased loans with evidence of credit deterioration	-	-	-	-	-	-	-
Total	$7,810	$ 3,921	$ 254	$ 944	$ 5,314	$ 3,784	$22,027
Carrying value of loans:							

Individually evaluated for impairment	$10,254	$10,816	$ -	$202	$-	$ -	$21,272
Collectively evaluated for impairment	265,740	556,173	3,939	47,948	301,473	-	1,175,273
Purchased loans with evidence of credit deterioration	37	224	-	-	149	-	410
Total	$276,031	$567,213	$ 3,939	$48,150	$301,622	$ -	$1,196,955

	Allowance for Loan Losses and Recorded Investment in Loans Evaluated for Impairment At December 31, 2017						
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Unallocated	Total
	(In thousands)						
Allowance for loan losses:							
Individually evaluated for impairment	$4,814	$171	$ -	$-	$-	$ -	$4,985
Collectively evaluated for impairment	2,932	3,678	335	995	6,418	3,666	18,024
Purchased loans with evidence of credit deterioration	-	-	-	-	-	-	-
Total	$7,746	$3,849	$ 335	$995	$6,418	$ 3,666	$23,009
Carrying value of loans:							
Individually evaluated for impairment	$10,675	$14,234	$ -	$208	$-	$ -	$25,117
Collectively evaluated for impairment	325,291	553,769	5,649	64,975	312,406	-	1,262,090
Purchased loans with evidence of credit deterioration	30	581	-	-	164	-	775
Total	$335,996	$568,584	$ 5,649	$65,183	$312,570	$ -	$1,287,982

The Company’s customers are small businesses, professionals and consumers. Given the scale of these borrowers, corporate credit rating agencies do not evaluate the borrowers’ financial condition. The Company’s subsidiary, Westamerica Bank (the “Bank”) maintains a Loan Review Department which reports directly to the Audit Committee of the Board of Directors. The Loan Review Department performs independent evaluations of loans and validates management assigned credit risk grades on evaluated loans using grading standards employed by bank regulatory agencies. Loans judged to carry lower-risk attributes are assigned a “pass” grade, with a minimal likelihood of loss. Loans judged to carry higher-risk attributes are referred to as “classified loans,” and are further disaggregated, with increasing expectations for loss recognition, as “substandard,” “doubtful,” and “loss.” Loan Review Department performs continuous evaluations throughout the year. If the Bank becomes aware of deterioration in a borrower’s performance or financial condition between Loan Review Department examinations, assigned risk grades are re-evaluated promptly. Credit risk grades assigned by management and validated by the Loan Review Department are subject to review by the Bank’s regulatory authorities during regulatory examinations.

The following summarizes the loan credit risk profile by internally assigned grade:

Loan Credit Risk Profile by Internally Assigned Grade
At September 30, 2018

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Total
	(In thousands)					
Grade:						
Pass	$264,908	$551,956	$ 3,939	$46,901	$299,590	$1,167,294
Substandard	11,123	15,257	-	1,249	1,618	29,247
Doubtful	-	-	-	-	56	56
Loss	-	-	-	-	358	358
Total	$276,031	$567,213	$ 3,939	$48,150	$301,622	$1,196,955

Credit risk profile reflects internally assigned grades of purchased covered loans without regard to FDIC indemnification on $6,086 thousand residential real estate and consumer loans.

Loan Credit Risk Profile by Internally Assigned Grade
At December 31, 2017

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Total
	(In thousands)					
Grade:						
Pass	$324,185	$548,853	$ 5,649	$62,253	$310,429	$1,251,369
Substandard	11,811	19,731	-	2,930	1,370	35,842
Doubtful	-	-	-	-	1	1
Loss	-	-	-	-	770	770
Total	$335,996	$568,584	$ 5,649	$65,183	$312,570	$1,287,982

Credit risk profile reflects internally assigned grades of purchased covered loans without regard to FDIC indemnification on $7,766 thousand residential real estate and consumer loans.

The following tables summarize loans by delinquency and nonaccrual status:

Summary of Loans by Delinquency and Nonaccrual Status
At September 30, 2018

	Current and Accruing	30-59 Days Past Due and Accruing	60-89 Days Past Due and Accruing	Past Due 90 Days or More and Accruing	Nonaccrual	Total Loans
	(In thousands)					
Commercial	$275,259	$ 425	$ 347	$ -	$ -	$276,031
Commercial real estate	559,441	2,334	-	-	5,438	567,213
Construction	3,939	-	-	-	-	3,939
Residential real estate	47,634	516	-	-	-	48,150
Consumer installment and other	297,416	3,001	801	361	43	301,622
Total	$1,183,689	$ 6,276	$ 1,148	$ 361	$ 5,481	$1,196,955

Summary of Loans by Delinquency and Nonaccrual Status
At December 31, 2017

	Current and Accruing	30-59 Days Past Due and Accruing	60-89 Days Past Due and Accruing	Past Due 90 Days or More and Accruing	Nonaccrual	Total Loans
	(In thousands)					
Commercial	$334,908	$ 627	$ 164	$ -	$ 297	$335,996
Commercial real estate	561,883	1,143	125	-	5,433	568,584
Construction	5,649	-	-	-	-	5,649
Residential real estate	65,183	-	-	-	-	65,183
Consumer installment and other	307,445	3,321	1,077	531	196	312,570
Total	$1,275,068	$ 5,091	$ 1,366	$ 531	$ 5,926	$1,287,982

There were no commitments to lend additional funds to borrowers whose loans were on nonaccrual status at September 30, 2018 and December 31, 2017.

The following summarizes impaired loans:

	Impaired Loans At September 30, 2018			At December 31, 2017		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(In thousands)					
With no related allowance recorded:						
Commercial	$809	$845	$ -	$1,212	$1,271	$ -
Commercial real estate	9,690	11,632	-	13,169	14,985	-
Residential real estate	202	232	-	208	239	-
Consumer installment and other	192	298	-	360	466	-
Total with no related allowance recorded	10,893	13,007	-	14,949	16,961	-
With an allowance recorded:						
Commercial	9,482	9,482	4,668	9,764	9,764	4,814
Commercial real estate	1,750	1,752	172	1,790	1,792	171
Total with an allowance recorded	11,232	11,234	4,840	11,554	11,556	4,985
Total	$22,125	$24,241	$ 4,840	$26,503	$28,517	$ 4,985

Impaired loans include troubled debt restructured loans. Impaired loans at September 30, 2018, included $8,747 thousand of restructured loans, $4,270 thousand of which were on nonaccrual status. Impaired loans at December 31, 2017, included $12,081 thousand of restructured loans, $4,285 thousand of which were on nonaccrual status.

	Impaired Loans For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2018		2017		2018		2017	
	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income
	(In thousands)							
Commercial	$10,426	$ 175	$11,125	$ 130	$10,671	$ 495	$11,203	$ 366
Commercial real estate	11,282	189	14,681	208	12,291	615	14,826	669
Residential real estate	203	4	365	4	205	12	494	13

Consumer installment and other	173	4	340	3	261	10	466	17
Total	$22,084	$ 372	$26,511	$ 345	$23,428	$ 1,132	$26,989	$ 1,065

The following tables provide information on troubled debt restructurings:

	Troubled Debt Restructurings At September 30, 2018			
	Number of Contracts	Pre-Modification Carrying Value	Period-End Carrying Value	Period-End Individual Impairment Allowance
	($ in thousands)			
Commercial	5	$ 2,324	$ 904	$ 34
Commercial real estate	8	9,237	7,642	-
Residential real estate	1	241	201	-
Total	14	$ 11,802	$ 8,747	$ 34

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Troubled Debt Restructurings
At December 31, 2017

	Number of Contracts	Pre-Modification Carrying Value	Period-End Carrying Value	Period-End Individual Impairment Allowance
	($ in thousands)			
Commercial	7	$ 2,393	$ 1,085	$ 43
Commercial real estate	10	11,528	10,788	-
Residential real estate	1	241	208	-
Total	18	$ 14,162	$ 12,081	$ 43

During the three and nine months ended September 30, 2018, the Company did not modify any loans that were considered troubled debt restructurings. During the three and nine months ended September 30, 2017, the Company modified one loan with a carrying value of $50 thousand and four loans with a carrying value of $699 thousand, respectively, that were considered troubled debt restructurings. The four concessions granted in the first nine months of 2017 consisted of modifications of payment terms to extend the maturity date to allow for deferred principal repayment and under-market terms. There were no chargeoffs related to troubled debt restructurings made during the three and nine months ended September 30, 2018. During the three and nine months ended September 30, 2017, one troubled debt restructured loan with a carrying value of $58 thousand was charged off. During the three and nine months ended September 30, 2018 and 2017, no troubled debt restructured loans defaulted within 12 months of the modification date. A troubled debt restructuring is considered to be in default when payments are ninety days or more past due.

There were no loans restricted due to collateral requirements at September 30, 2018 and December 31, 2017.

There were no loans held for sale at September 30, 2018 and December 31, 2017.

At September 30, 2018 and December 31, 2017, the Company held total other real estate owned (OREO) of $620 thousand net of reserve of $-0- thousand and $1,426 thousand net of reserve of $1,905 thousand, respectively, of which there were no foreclosed residential real estate properties or covered OREO at both dates, respectively. The amount of consumer mortgage loans outstanding secured by residential real estate properties for which formal foreclosure proceedings were in process was $19 thousand at September 30, 2018 and $196 thousand at December 31, 2017.

Note 5: Concentration of Credit Risk

Under the California Financial Code, credit extended to any one person owing to a commercial bank at any one time shall not exceed the following limitations: (a) unsecured loans shall not exceed 15 percent of the sum of the shareholders' equity, allowance for loan losses, capital notes, and debentures of the bank, or (b) secured and unsecured loans in all shall not exceed 25 percent of the sum of the shareholders' equity, allowance for loan losses, capital notes, and debentures of the bank. At September 30, 2018, the Bank did not have credit extended to any one entity exceeding these limits. At September 30, 2018, the Bank had 35 lending relationships each with aggregate amounts of $5 million or more. The Company has significant credit arrangements that are secured by real estate collateral. In addition to real estate loans outstanding as disclosed in Note 4, the Company had loan commitments related to real estate loans of $52,842 thousand and $53,874 thousand at September 30, 2018 and December 31, 2017, respectively. The Company requires collateral on all real estate loans with loan-to-value ratios at origination generally no greater than 75% on commercial real estate loans and no greater than 80% on residential real estate loans. At September 30, 2018, the Bank held corporate bonds in 80 issuing entities that exceeded $5 million for each issuer.

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Note 6: Other Assets

Other assets consisted of the following:

	At September 30, 2018	At December 31, 2017
	(In thousands)	
Equity securities without readily determinable fair values:		
Federal Reserve Bank stock [(1)]	$14,069	$14,069
Other investments	158	158
Total equity securities without readily determinable fair values	14,227	14,227
Life insurance cash surrender value	55,442	54,101
Net deferred tax asset	48,622	33,112
Limited partnership investments	10,919	10,119
Interest receivable	23,734	23,557
Prepaid assets	4,119	4,906
Other assets	8,411	18,428
Total other assets	$165,474	$158,450

(1) A bank applying for membership in the Federal Reserve System is required to subscribe to stock in the Federal Reserve Bank (FRB) in its district in a sum equal to six percent of the bank's paid-up capital stock and surplus. One-half of the amount of the bank's subscription shall be paid to the FRB and the remaining half will be subject to call when deemed necessary by the Board of Governors of the Federal Reserve System.

The Company owns 211 thousand shares of Visa Inc. class B common stock which have transfer restrictions; the carrying value is $-0- thousand. On July 5, 2018, Visa Inc. announced a new conversion rate applicable to its class B common stock resulting from its June 28, 2018 deposit of funds into its litigation escrow account. This funding reduced the conversion rate of class B common stock into class A common stock, which is unrestricted and trades actively on the New York Stock Exchange, from 1.6483 to 1.6298. Visa Inc. class A common stock had a closing price of $150.09 per share on September 28, 2018, the last day of stock market trading for the third quarter 2018. The ultimate value of the Company's Visa Inc. class B shares is subject to the extent of Visa Inc.'s future litigation escrow fundings; the resulting conversion rate to class A common stock, and current and future trading restrictions on the class B common stock.

The Company invests in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for low-income housing tax credits. At September 30, 2018, this investment totaled $10,919 thousand and $5,088 thousand of this amount represents outstanding equity capital commitments that are included in other liabilities. At December 31, 2017, this investment totaled $10,119 thousand and $2,299 thousand of this amount represented outstanding equity capital commitments. At September 30, 2018, the $5,088 thousand of outstanding equity capital commitments are expected to be paid as follows, $552 thousand in 2018, $364 thousand in 2019, $2,026 thousand in 2020, $138 thousand in 2021, $261 thousand in 2022, $134 thousand in 2023, $1,041 thousand in 2024 and $572 thousand in 2025 or thereafter.

The amounts recognized in net income for these investments include:

	For the Three Months Ended		For the Nine Months Ended	
	September 30,			
	2018	2017	2018	2017
	(In thousands)			
Investment loss included in pre-tax income	$900	$450	$2,200	$1,350
Tax credits recognized in provision for income taxes	336	463	1,008	1,388

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Note 7: Goodwill and Identifiable Intangible Assets

The Company has recorded goodwill and other identifiable intangibles associated with purchase business combinations. Goodwill is not amortized, but is evaluated for impairment at least annually. The Company did not recognize impairment during the three and nine months ended September 30, 2018 and year ended December 31, 2017. Identifiable intangibles are amortized to their estimated residual values over their expected useful lives. Such lives and residual values are also periodically reassessed to determine if any amortization period adjustments are indicated. During the three and nine months ended September 30, 2018 and year ended December 31, 2017 no such adjustments were recorded.

The carrying values of goodwill were:

	At September 30, 2018	At December 31, 2017
	(In thousands)	
Goodwill	$121,673	$121,673

The gross carrying amount of identifiable intangible assets and accumulated amortization was:

	At September 30, 2018		At December 31, 2017	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Core Deposit Intangibles	$56,808	$ (54,432)	$56,808	$ (52,987)
Merchant Draft Processing Intangible	10,300	(10,300)	10,300	(10,271)
Total Identifiable Intangible Assets	$67,108	$ (64,732)	$67,108	$ (63,258)

As of September 30, 2018, the current period and estimated future amortization expense for identifiable intangible assets was:

Total

	Core Deposit Intangibles	Merchant Draft Processing Intangible	
	(In thousands)		
For the Nine Months ended September 30, 2018 (actual)	$1,445	$ 29	$1,474
Estimate for the remainder of year ending December 31, 2018	447	-	447
Estimate for year ending December 31, 2019	538	-	538
2020	287	-	287
2021	269	-	269
2022	252	-	252
2023	236	-	236

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Note 8: Deposits and Borrowed Funds

The following table provides additional detail regarding deposits.

	Deposits	
	At September 30, 2018	At December 31, 2017
	(In thousands)	
Noninterest-bearing	$2,211,028	$2,197,526
Interest-bearing:		
Transaction	909,954	904,245
Savings	1,510,015	1,494,024
Time deposits less than $100 thousand	107,755	117,848
Time deposits $100 thousand through $250 thousand	68,677	76,578
Time deposits more than $250 thousand	28,408	37,392
Total deposits	$4,835,837	$4,827,613

Demand deposit overdrafts of $950 thousand and $2,786 thousand were included as loan balances at September 30, 2018 and December 31, 2017, respectively. Interest expense for aggregate time deposits with individual account balances in excess of $100 thousand was $91 thousand and $283 thousand for the three and nine months ended September 30, 2018, respectively and $103 thousand and $314 thousand for the three and nine months ended September 30, 2017, respectively.

The following table provides additional detail regarding short-term borrowed funds.

	Repurchase Agreements (Sweep) Accounted for as Secured Borrowings	
	Remaining Contractual Maturity of the Agreements	
	Overnight and Continuous	
	At September	At December

	30, 2018	31, 2017
Repurchase agreements:	(In thousands)	
Collateral securing borrowings:		
Securities of U.S. Government sponsored entities	$72,675	$74,173
Agency residential MBS	59,367	58,251
Corporate securities	91,818	105,113
Total collateral carrying value	$223,860	$237,537
Total short-term borrowed funds	$61,756	$58,471

Note 9: Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Equity securities and debt securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as other real estate owned, impaired loans, certain loans held for investment, debt securities held to maturity, and other assets. These nonrecurring fair value adjustments typically involve the lower-of-cost or fair-value accounting of individual assets.

In accordance with the Fair Value Measurement and Disclosure topic of the FASB Accounting Standards Codification, the Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in the principal market or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date under current market conditions. A fair value measurement reflects all of the assumptions that market participants would use in pricing the asset or liability, including assumptions about the risk inherent in a particular valuation technique, the effect of a restriction on the sale or use of an asset, and the risk of nonperformance.

The Company groups its assets and liabilities measured at fair value into a three-level hierarchy, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. When the valuation assumptions used to measure the fair value of the asset or liability are categorized within different levels of the fair value hierarchy, the asset or liability is categorized in its entirety within the lowest level of the hierarchy. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Level 1 includes U.S. Treasury and equity securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Level 2 includes mutual funds, federal agency securities, mortgage-backed securities, corporate securities, asset-backed securities, and municipal bonds.

Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

The Company relies on independent vendor pricing services to measure fair value for equity securities, debt securities available for sale and debt securities held to maturity. The Company employs three pricing services. To validate the pricing of these vendors, the Company compares vendors' pricing for each of the securities for consistency; significant pricing differences, if any, are evaluated using all available independent quotes with the quote most closely reflecting the market generally used as the fair value estimate. In addition, the Company conducts "other than temporary impairment (OTTI)" analysis on a quarterly basis; debt securities selected for OTTI analysis include all debt securities at a market price below 95 percent of par value. As with any valuation technique used to estimate fair value, changes in underlying assumptions used could significantly affect the results of current and future values. Accordingly, these fair value estimates may not be realized in an actual sale of the securities.

The Company regularly reviews the valuation techniques and assumptions used by its vendors and determines which valuation techniques are utilized based on observable market inputs for the type of securities being measured. The Company uses the information to determine the placement in the fair value hierarchy as level 1, 2 or 3.

Assets Recorded at Fair Value on a Recurring Basis

The tables below present assets measured at fair value on a recurring basis on the dates indicated.

At September 30, 2018

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3) [1]
	(In thousands)			
Equity securities				
Mutual funds	$1,734	$ -	$1,734	$ -
Total equity securities	1,734	-	1,734	-
Debt securities available for sale				
Securities of U.S. Government sponsored entities	161,744	-	161,744	-
Agency residential MBS	878,029	-	878,029	-
Non-agency residential MBS	124	-	124	-
Agency commercial MBS	1,847	-	1,847	-
Securities of U.S. Government entities	1,210	-	1,210	-
Obligations of states and political subdivisions	180,343	-	180,343	-
Corporate securities	1,255,611	-	1,255,611	-
Total debt securities available for sale	2,478,908	-	2,478,908	-
Total	$2,480,642	$ -	$2,480,642	$ -

[1] There were no transfers in to or out of level 3 during the nine months ended September 30, 2018.

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	At December 31, 2017			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3) [(1)]
	(In thousands)			
Equity securities				
Mutual funds	$1,800	$ -	$1,800	$ -
Total equity securities	1,800	-	1,800	-
Debt securities available for sale				
Securities of U.S. Government sponsored entities	119,319	-	119,319	-
Agency residential MBS	767,706	-	767,706	-
Non-agency residential MBS	154	-	154	-
Agency commercial MBS	2,219	-	2,219	-
Securities of U.S. Government entities	1,590	-	1,590	-
Obligations of states and political subdivisions	185,221	-	185,221	-
Corporate securities	1,115,498	-	1,115,498	-
Total debt securities available for sale	2,191,707	-	2,191,707	-
Total	$2,193,507	$ -	$2,193,507	$ -

[(1)] There were no transfers in to or out of level 3 during the year ended December 31, 2017.

Assets Recorded at Fair Value on a Nonrecurring Basis

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower of cost or fair value accounting of individual assets. For assets measured at fair value on a nonrecurring basis that were recorded in the balance sheet at September 30, 2018 and December 31, 2017, the following tables provide the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at period end.

		For the Nine Months Ended
	At September 30, 2018	

	Carrying Value	Level 1	Level 2	Level 3	September 30, 2018 Total Losses
	(In thousands)				
Other real estate owned	$620	$ -	$ -	$620	$ -
Impaired loans:					
Commercial	4,815	-	-	4,815	-
Commercial real estate	5,448	-	-	5,448	(240)
Total assets measured at fair value on a nonrecurring basis	$10,883	$ -	$ -	$10,883	$ (240)

	At December 31, 2017				For the Year Ended December 31, 2017
	Carrying Value	Level 1	Level 2	Level 3	Total Losses
	(In thousands)				
Other real estate owned	$1,426	$ -	$ -	$1,426	$ (219)
Impaired loans:					
Commercial	4,950	-	-	4,950	-
Commercial real estate	5,904	-	-	5,904	-
Total assets measured at fair value on a nonrecurring basis	$12,280	$ -	$ -	$12,280	$ (219)

Level 3 – Valuation is based upon present value of expected future cash flows, independent market prices, estimated liquidation values of loan collateral or appraised value of the collateral as determined by third-party independent appraisers, less 10% for selling costs, generally. Level 3 includes other real estate owned that has been measured at fair value upon transfer to foreclosed assets and impaired loans collateralized by real property and other business asset collateral where a specific reserve has been established or a chargeoff has been recorded. Losses on other real estate owned represent losses recognized in earnings during the period subsequent to its initial classification as foreclosed assets. The unobservable inputs and qualitative information about the unobservable inputs are not presented as the inputs were not developed by the Company.

Disclosures about Fair Value of Financial Instruments

The following section describes the valuation methodologies used by the Company for estimating fair value of financial instruments not recorded at fair value in the balance sheet. The Company implemented the provisions of ASU 2016-01, *Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*, effective January 1, 2018. The provisions require the Company to use the “exit price notion” when measuring the fair value of financial instruments for disclosure purposes.

Cash and Due from Banks Cash and due from banks represent U.S. dollar denominated coin and currency, deposits at the Federal Reserve Bank and correspondent banks, and amounts being settled with other banks to complete the processing of customers’ daily transactions. Collectively, the Federal Reserve Bank and financial institutions operate in a market in which cash and due from banks transactions are processed continuously in significant daily volumes honoring the face value of the U.S. dollar.

Debt Securities Held to Maturity The fair values of debt securities were estimated using quoted prices as described above for Level 2 valuation.

Loans Loans are valued using the exit price notion. The Company uses a net present value of cash flows methodology that seeks to incorporate interest rate, credit, liquidity and prepayment risks in the fair market value estimation. Inputs to calculation include market rates for similarly offered products, market interest rate projections, credit spreads, estimated credit losses and prepayment assumptions.

Prior to adoption of ASU 2016-01, loans were separated into two groups for valuation. Variable rate loans, except for those described below, that reprice frequently with changes in market rates were valued using historical cost. Fixed rate loans and variable rate loans that have reached their minimum contractual interest rates were valued by discounting the future cash flows expected to be received from the loans using current interest rates charged on loans with similar characteristics. Additionally, the allowance for loan losses of $23,009 thousand at December 31, 2017 was applied against the estimated fair values to recognize estimated future defaults of contractual cash flows.

Deposit Liabilities Deposits with no stated maturity such as checking accounts, savings accounts and money market accounts can be readily converted to cash or used to settle transactions at face value through the broad financial system operated by the Federal Reserve Banks and financial institutions. The fair value of deposits with no stated maturity is equal to the amount payable on demand. The fair value of time deposits was estimated using a net present value of cash flows methodology, incorporating market interest rate projections and rates on alternative funding sources.

Prior to adoption of ASU 2016-01, the fair value of time deposits were estimated by discounting estimated future contractual cash flows using current market rates for financial instruments with similar characteristics.

Short-Term Borrowed Funds The carrying amount of securities sold under agreement to repurchase and other short-term borrowed funds approximate fair value due to the relatively short period of time between their origination and their expected realization.

The tables below are a summary of fair value estimates for financial instruments and the level of the fair value hierarchy within which the fair value measurements are categorized, excluding financial instruments recorded at fair value on a recurring basis. The values assigned do not necessarily represent amounts which ultimately may be realized for assets or paid to settle liabilities. In addition, these values do not give effect to adjustments to fair value which may occur when financial instruments are sold or settled in larger quantities. The carrying amounts in the following tables are recorded in the balance sheet under the indicated captions.

The Company has not included assets and liabilities that are not financial instruments, such as goodwill, long-term relationships with deposit, merchant processing and trust customers, other purchased intangibles, premises and equipment, deferred taxes and other assets and liabilities. The total estimated fair values do not represent, and should not be construed to represent, the underlying value of the Company.

	At September 30, 2018				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:	(In thousands)				
Cash and due from banks	$522,660	$522,660	$522,660	$-	$ -
Debt securities held to maturity	1,025,699	1,002,648	-	1,002,648	-
Loans	1,174,928	1,176,889	-	-	1,176,889
Financial Liabilities:					
Deposits	$4,835,837	$4,832,135	$-	$4,630,997	$ 201,138
Short-term borrowed funds	61,756	61,756	-	61,756	-

	At December 31, 2017				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:	(In thousands)				
Cash and due from banks	$575,002	$575,002	$575,002	$-	$ -
Debt securities held to maturity	1,158,864	1,155,342	-	1,155,342	-
Loans	1,264,973	1,257,811	-	-	1,257,811
Financial Liabilities:					
Deposits	$4,827,613	$4,824,586	$-	$4,595,795	$ 228,791
Short-term borrowed funds	58,471	58,471	-	58,471	-

The majority of the Company’s standby letters of credit and other commitments to extend credit carry current market interest rates if converted to loans. No premium or discount was ascribed to these commitments because virtually all funding would be at current market rates.

Note 10: Commitments and Contingent Liabilities

Loan commitments are agreements to lend to a customer provided there is no violation of any condition established in the agreement. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future funding requirements. Loan commitments are subject to the Company’s normal credit policies and collateral requirements. Unfunded loan commitments were $292,704 thousand and $272,646 thousand at September 30, 2018 and December 31, 2017, respectively. Standby letters of credit commit the Company to make payments on behalf of customers when certain specified future events occur. Standby letters of credit are primarily issued to support customers’ short-term financing requirements and must meet the Company’s normal credit policies and collateral requirements. Financial and performance standby letters of credit outstanding totaled $2,904 thousand and $19,263 thousand at September 30, 2018 and December 31, 2017, respectively. The Company had no commitments outstanding for commercial and similar letters of credit at September 30, 2018 and December 31, 2017. The Company had a reserve for unfunded commitments of $2,308 thousand at September 30, 2018 and $2,308 thousand at December 31, 2017, included in other liabilities.

Due to the nature of its business, the Company is subject to various threatened or filed legal cases. Based on the advice of legal counsel, the Company does not expect such cases will have a material, adverse effect on its financial position or results of operations. Legal liabilities are accrued when obligations become probable and the amount can be reasonably estimated. In the third quarter 2018, the Company achieved a mediated settlement to dismiss a lawsuit, subject to court approval, and has accrued a liability for $3,500 thousand.

The Company has determined that it will be obligated to provide refunds of revenue recognized in years prior to 2017 to some customers. The Company estimates the probable amount of these obligations will be $5,542 thousand and has accrued a liability for such amount; the estimated liability is subject to revision.

Note 11: Earnings Per Common Share

The table below shows earnings per common share and diluted earnings per common share. Basic earnings per common share are computed by dividing net income by the average number of common shares outstanding during the period. Diluted earnings per common share are computed by dividing net income by the average number of common shares outstanding during the period plus the impact of common stock equivalents.

	For the Three Months		For the Nine Months	
	Ended September 30,			
	2018	2017	2018	2017
	(In thousands, except per share data)			
Net income applicable to common equity (numerator)	$16,993	$15,017	$52,509	$45,865
Basic earnings per common share				
Weighted average number of common shares outstanding - basic (denominator)	26,701	26,309	26,622	26,260
Basic earnings per common share	$0.64	$0.57	$1.97	$1.75
Diluted earnings per common share				
Weighted average number of common shares outstanding - basic	26,701	26,309	26,622	26,260
Add common stock equivalents for options	114	95	114	119
Weighted average number of common shares outstanding - diluted (denominator)	26,815	26,404	26,736	26,379
Diluted earnings per common share	$0.63	$0.57	$1.96	$1.74

For the three and nine months ended September 30, 2018, options to purchase 326 thousand and 432 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted earnings per common share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

For the three and nine months ended September 30, 2017, options to purchase 376 thousand and 343 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted earnings per common share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

WESTAMERICA BANCORPORATION

FINANCIAL SUMMARY

	For the Three Months Ended September 30,		For the Nine Months	
	2018	2017	2018	2017
	(In thousands, except per share data)			
Net Interest and Loan Fee Income (FTE)(1)	$37,137	$35,680	$109,189	$107,474
Reversal of Provision for Loan Losses	-	-	-	(1,900)
Noninterest Income:				
Life Insurance Gains	585	-	585	-
Securities Losses	(16)	-	(66)	-
Other Noninterest income	11,959	12,548	35,733	36,328
Total Noninterest Income	12,528	12,548	36,252	36,328
Noninterest Expense:				
Loss Contingency	3,500	-	3,500	-
Other Noninterest Expense	23,505	24,114	71,696	73,125
Total Noninterest Expense	27,005	24,114	75,196	73,125
Income Before Income Taxes (FTE)(1)	22,660	24,114	70,245	72,577
Income Tax Provision (FTE)(1)	5,667	9,097	17,736	26,712
Net Income	$16,993	$15,017	$52,509	$45,865
Average Common Shares Outstanding	26,701	26,309	26,622	26,260
Average Diluted Common Shares Outstanding	26,815	26,404	26,736	26,379
Common Shares Outstanding at Period End	26,727	26,319		
Per Common Share:				
Basic Earnings	$0.64	$0.57	$1.97	$1.75
Diluted Earnings	0.63	0.57	1.96	1.74
Book Value	$22.17	$22.95		
Financial Ratios:				
Return on Assets	1.19%	1.09%	1.25%	1.13%
Return on Common Equity	10.58%	9.94%	11.22%	10.36%
Net Interest Margin (FTE) (1)	3.10%	3.10%	3.07%	3.12%
Net Loan Losses to Average Loans	0.34%	0.15%	0.11%	0.04%
Efficiency Ratio (2)	54.4%	50.0%	51.7%	50.9%
Average Balances:				
Assets	$5,648,004	$5,441,612	$5,600,499	$5,407,661
Earning Assets	4,786,511	4,587,848	4,754,436	4,601,931

Loans	1,194,874	1,287,740	1,215,712	1,325,128
Deposits	4,893,859	4,714,579	4,856,639	4,692,330
Shareholders' Equity	636,965	599,473	625,496	591,691
Period End Balances:				
Assets	$5,529,463	$5,445,808		
Earning Assets	4,703,296	4,579,499		
Loans	1,196,955	1,284,782		
Deposits	4,835,837	4,734,580		
Shareholders' Equity	592,591	603,957		
Capital Ratios at Period End:				
Total Risk Based Capital	16.99 %	16.71 %		
Tangible Equity to Tangible Assets	8.67 %	8.98 %		
Dividends Paid Per Common Share	$0.40	$0.39	$1.20	$1.17
Common Dividend Payout Ratio	63 %	68 %	61 %	67 %

The above financial summary has been derived from the Company's unaudited consolidated financial statements. This information should be read in conjunction with those statements, notes and the other information included elsewhere herein. Percentages under the heading "Financial Ratios" are annualized with the exception of the efficiency ratio.

(1) Yields on securities and certain loans have been adjusted upward to a "fully taxable equivalent" ("FTE") basis in order to reflect the effect of income which is exempt from federal income taxation at the current statutory tax rate.

(2) The efficiency ratio is defined as noninterest expense divided by total revenue (net interest income on an FTE basis and noninterest income).

Financial Overview

Westamerica Bancorporation and subsidiaries' (collectively, the "Company") reported net income of $17.0 million or $0.63 diluted earnings per common share ("EPS") for the third quarter 2018 and net income of $52.5 million or $1.96 EPS for the nine months ended September 30, 2018. The third quarter 2018 results include a $585 thousand tax-exempt life insurance policy gain and a $3.5 million settlement, which on an aggregate basis reduced EPS $0.07. In the third quarter 2018, the Company achieved a mediated settlement to dismiss a lawsuit, subject to court approval, and has accrued a liability for such amount. The results for the third quarter 2018 and the nine months ended September 30, 2018 compare to net income of $15.0 million or $0.57 EPS for the third quarter 2017 and net income of $45.9 million or $1.74 EPS for the nine months ended September 30, 2017. Results for the nine months ended September 30, 2017 include a $1.9 million reversal of provision for loan losses which accounted for $0.04 of the EPS.

The Company's principal source of revenue is net interest and loan fee income, which represents interest and fees earned on loans and investment securities ("earning assets") reduced by interest paid on deposits and other borrowings ("interest-bearing liabilities"). Market interest rates declined considerably following the recession of 2008 and 2009. Interest rates remained historically low through 2016 as the monetary policy of the Federal Open Market Committee (the "FOMC") was highly accommodative. During this period, Management avoided originating long-dated, low-yielding loans given the potential impact of such assets on forward earning potential; as a result, loans declined and investment securities increased. The changed composition of the earning assets and low market interest rates pressured the net interest margin to lower levels. The FOMC began removing monetary stimulus in December 2016 and has increased the federal funds rate by 1.75 percent to 2.25 percent through September 2018, although longer-term rates have not increased by a similar magnitude. This recent increase in market interest rates has begun benefiting the Company's earning asset yields. However, the rising market rates have not resulted in higher rates paid on deposits. The funding source of the Company's earning assets is primarily customer deposits. The Company's long-term strategy includes maximizing checking and savings deposits as these types of deposits are lower-cost and less sensitive to changes in interest rates compared to time deposits. During the nine months ended September 30, 2018 the average volume of checking and savings deposits was 95 .5 percent of average total deposits. Net interest income was $35.7 million and $104.9 million for the three and nine months ended September 30, 2018, respectively, compared with $32.7 million and $98.2 million for the three and nine months ended September 30, 2017, respectively. The increase in net interest income is due to higher asset yields and higher levels of average earning assets.

Credit quality remained solid with nonperforming assets totaling $6.5 million at September 30, 2018 and net loan losses of $1.0 million for the nine months ended September 30, 2018. The Company did not recognize a provision for loan losses in the nine months ended September 30, 2018.

The Company presents its net interest margin and net interest income on an FTE basis using the current statutory federal tax rate. Management believes the FTE basis is valuable to the reader because the Company's loan and investment securities portfolios contain a relatively large portion of municipal loans and securities that are federally tax exempt. The Company's tax exempt loans and securities composition may not be similar to that of other banks, therefore in order to reflect the impact of the federally tax exempt loans and securities on the net interest margin and net interest income for comparability with other banks, the Company presents its net interest margin and net interest income on an FTE basis. Yields on tax-exempt securities and loans have been adjusted upward to reflect the effect of income exempt from federal income taxation at the federal statutory tax rate of 35% for 2017. Due to the Tax Cuts and Jobs Act of 2017 (“Act”), the federal tax rate became 21% for 2018; as such, the upward adjustment to reflect the effect of income exempt from federal taxation is lower in 2018.

The Company’s significant accounting policies (see Note 1, “Summary of Significant Accounting Policies,” to Financial Statements in the Company’s 2017 Form 10-K) are fundamental to understanding the Company’s results of operations and financial condition.

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Net Income

Following is a summary of the components of net income for the periods indicated:

	For the Three Months Ended September 30,		For the Nine Months	
	2018	2017	2018	2017
	(In thousands, except per share data)			
Net interest and loan fee income	$35,726	$32,672	$104,897	$98,203
FTE adjustment	1,411	3,008	4,292	9,271
Net interest and loan fee income (FTE)	37,137	35,680	109,189	107,474
Reversal of provision for loan losses	-	-	-	(1,900)
Noninterest income	12,528	12,548	36,252	36,328
Noninterest expense	27,005	24,114	75,196	73,125
Income before taxes (FTE)	22,660	24,114	70,245	72,577
Income tax provision (FTE)	5,667	9,097	17,736	26,712
Net income	$16,993	$15,017	$52,509	$45,865
Average diluted common shares	26,815	26,404	26,736	26,379
Diluted earnings per common share	$0.63	$0.57	$1.96	$1.74
Average total assets	$5,648,004	$5,441,612	$5,600,499	$5,407,661
Net income to average total assets (annualized)	1.19 %	1.09 %	1.25 %	1.13 %
Net income to average common shareholders' equity (annualized)	10.58 %	9.94 %	11.22 %	10.36 %

Net income for the third quarter of 2018 was $2.0 million more than the same quarter of 2017. Net interest and loan fee income increased $3.1 million in the third quarter 2018 compared with third quarter 2017 mostly attributable to higher average balances of investments and higher yield on earning assets as market interest rates rose. The increase was offset by lower average balances of loans. Net interest and loan fee income (FTE) in the third quarter 2018 included a lower FTE adjustment than in the third quarter 2017 due to the reduced federal corporate tax as a result of enactment of the Act. The provision for loan losses remained zero, reflecting Management's evaluation of losses inherent in the loan portfolio. Noninterest expense increased $2.9 million in the third quarter 2018 compared with the same period in 2017 due to a $3.5 million settlement. In the third quarter 2018, the Company achieved a mediated settlement to dismiss a lawsuit, subject to court approval, and has accrued a liability for such amount. The non-FTE book tax provision for the third quarter 2018, which reflected the tax-exempt nature of a $585 thousand life insurance policy gain, was $4.3 million compared with $6.1 million for the third quarter 2017, representing effective tax rates of 20.0% and 28.8%, respectively. The non-FTE book tax provisions for the three months ended September 30, 2018 and September 30, 2017 include tax benefits of $152 thousand and $22 thousand, respectively, for tax deductions from the exercise of employee stock options which exceed related compensation expenses recognized in the financial statements.

Comparing the first nine months of 2018 with the first nine months of 2017, net income increased $6.6 million. Net interest and loan fee income increased $6.7 million in the first nine months of 2018 compared with the first nine months of 2017 mostly attributable to higher average balances of investments and higher yields on earning assets as market interest rates rose. The increase was offset by lower average balances of loans. Net interest and loan fee income (FTE) in the first nine months of 2018 included a lower FTE adjustment than in the first nine months of 2017 due to the reduced federal corporate tax as a result of enactment of the Act. The provision for loan losses remained zero, reflecting Management's evaluation of losses inherent in the loan portfolio. In the first nine months of 2018, noninterest expense increased $2.1 million compared with the first nine months of 2017 due to a $3.5 million settlement. In the third quarter 2018, the Company achieved a mediated settlement to dismiss a lawsuit, subject to court approval, and has accrued a liability for such amount. The non-FTE book tax provision for the first nine months of 2018, which reflected the tax-exempt nature of a $585 thousand life insurance policy gain, was $13.4 million compared with $17.4 million for the first nine months of 2017, representing effective tax rates of 20.4% and 27.6%, respectively. The non-FTE book tax provisions for the nine months ended September 30, 2018 and September 30, 2017 include tax benefits of $731 thousand and $688 thousand, respectively, for tax deductions from the exercise of employee stock options which exceed related compensation expenses recognized in the financial statements.

Net Interest and Loan Fee Income (FTE)

Following is a summary of the components of net interest and loan fee income (FTE) for the periods indicated:

	For the Three Months Ended September 30,		For the Nine Months	
	2018	2017	2018	2017
	($ in thousands)			
Interest and loan fee income	$36,253	$33,145	$106,342	$99,632
Interest expense	527	473	1,445	1,429
Net interest and loan fee income	35,726	32,672	104,897	98,203
FTE adjustment	1,411	3,008	4,292	9,271
Net interest and loan fee income (FTE)	$37,137	$35,680	$109,189	$107,474
Average earning assets	$4,786,511	$4,587,848	$4,754,436	$4,601,931
Net interest margin (FTE) (annualized)	3.10 %	3.10 %	3.07 %	3.12 %

Net interest and loan fee income increased $3.1 million in the third quarter 2018 compared with the third quarter 2017, mainly due to higher average balances of investments (up $292 million) and higher yield on earning assets (up 0.14%), partially offset by lower average balances of loans (down $93 million). The FTE adjustment was lower in the third quarter 2018 compared with the third quarter 2017 mainly due to the reduced federal corporate tax rate as a result of enactment of the Act.

Comparing the first nine months of 2018 with the first nine months of 2017, net interest and loan fee income increased $6.7 million due to higher average balances of investments (up $262 million) and higher yield on interest earning assets (up 0.10%), offset by lower average balances of loans (down $109 million). The FTE adjustment was lower in the first nine months of 2018 compared with the first nine months of 2017 mainly due to the reduced federal corporate tax rate as a result of enactment of the Act.

The annualized net interest margin (FTE) was 3.10% in the third quarter 2018 and 3.07% in the nine months ended September 30, 2018 compared with 3.10% in the third quarter 2017 and 3.12% in the nine months ended September 30, 2017. The net interest margin (FTE) reflected higher market interest rates which offset the impact of the reduced federal corporate tax rate as a result of enactment of the Act. The net interest margin (FTE) was lower in the nine months ended September 30, 2018 than in the same period of 2017 primarily due to the reduced federal corporate tax rate as a result of enactment of the Act.

The Company's funding cost was 0.04% in the nine months ended September 30, 2018, unchanged from the nine months ended September 30, 2017. Average balances of time deposits declined $35 million from the third quarter 2017 to the third quarter 2018 while lower-cost checking and savings deposits grew 5% in the same period. Average balances of checking and saving deposits accounted for 95.5% of average total deposits in the nine months ended September 30, 2018 compared with 94.7% in the nine months ended September 30, 2017.

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Net Interest Margin (FTE)

The following summarizes the components of the Company's net interest margin for the periods indicated (percentages are annualized.):

	For the Three Months		For the Nine Months	
	Ended September 30,			
	2018	2017	2018	2017
Yield on earning assets	3.02 %	2.88 %	2.99 %	2.89 %
Impact of FTE adjustment	0.12 %	0.26 %	0.12 %	0.27 %
Yield on earning assets (FTE)	3.14 %	3.14 %	3.11 %	3.16 %
Rate paid on interest-bearing liabilities	0.08 %	0.07 %	0.07 %	0.07 %
Net interest spread (FTE)	3.06 %	3.07 %	3.04 %	3.09 %
Impact of noninterest-bearing demand deposits	0.04 %	0.03 %	0.03 %	0.03 %
Net interest margin (FTE)	3.10 %	3.10 %	3.07 %	3.12 %

The FOMC increased the federal funds rate between December 2016 and September 2018. In the nine months ended September 30, 2018, the yield on earning assets increased with rising market interest rates. The net interest spread and net interest margin stated on an FTE basis are lower in 2018 compared with 2017 because the FTE adjustment to reflect the effect of income exempt from federal taxation is lower in 2018 compared with 2017. Rates on interest-bearing liabilities were kept low by reducing the volume of higher-cost time deposits and increasing balances of checking and savings deposits, which earn relatively low interest rates and are less volatile than time deposits during periods of rising market interest rates.

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Summary of Average Balances, Yields/Rates and Interest Differential

The following tables present information regarding the consolidated average assets, liabilities and shareholders' equity, the amounts of interest income earned from average interest earning assets and the resulting yields, and the amounts of interest expense incurred on average interest-bearing liabilities and the resulting rates. Average loan balances include nonperforming loans. Interest income includes reversal of previously accrued interest on loans placed on non-accrual status during the period and proceeds from loans on nonaccrual status only to the extent cash payments have been received and applied as interest income and accretion of purchased loan discounts. Yields, rates and interest margins are annualized. Yields on tax-exempt securities and loans have been adjusted upward to reflect the effect of income exempt from federal income taxation at the federal statutory tax rate of 35 percent for 2017. Due to the Act, the federal tax rate became 21 percent for 2018; as such, the upward adjustment to reflect the effect of income exempt from federal taxation is lower in 2018.

Distribution of Assets, Liabilities & Shareholders' Equity and Yields, Rates & Interest Margin

	For the Three Months Ended September 30, 2018		
	Average Balance	Interest Income/ Expense	Yields/ Rates
	($ in thousands)		
Assets			
Investment securities:			
Taxable	$2,849,187	$16,780	2.36%
Tax-exempt (1)	742,450	6,177	3.33%
Total investments (1)	3,591,637	22,957	2.56%
Loans:			
Taxable	1,140,448	14,161	4.93%
Tax-exempt (1)	54,426	546	3.98%
Total loans (1)	1,194,874	14,707	4.88%
Total Interest-earning assets (1)	4,786,511	37,664	3.14%
Other assets	861,493		
Total assets	$5,648,004		
Liabilities and shareholders' equity			
Noninterest-bearing demand	$2,223,678	$-	- %
Savings and interest-bearing transaction	2,461,357	358	0.06%
Time less than $100,000	118,156	69	0.23%
Time $100,000 or more	90,668	91	0.40%
Total interest-bearing deposits	2,670,181	518	0.08%
Short-term borrowed funds	63,489	9	0.06%
Total interest-bearing liabilities	2,733,670	527	0.08%

Other liabilities	53,691		
Shareholders' equity	636,965		
Total liabilities and shareholders' equity	$5,648,004		
Net interest spread (1) (2)			3.06%
Net interest and fee income and interest margin (1) (3)		$37,137	3.10%

(1) Amounts calculated on an FTE basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate incurred on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense, divided by the average balance of interest-earning assets. The net interest margin is greater than the net interest spread due to the benefit of noninterest-bearing demand deposits.

Distribution of Assets, Liabilities & Shareholders' Equity and Yields, Rates & Interest Margin

	For the Three Months Ended September 30, 2017		
	Average Balance	Interest Income/ Expense	Yields/ Rates
	($ in thousands)		
Assets			
Investment securities:			
Taxable	$2,496,470	$12,957	2.08%
Tax-exempt [1]	803,638	7,847	3.91%
Total investments [1]	3,300,108	20,804	2.52%
Loans:			
Taxable	1,225,937	14,586	4.72%
Tax-exempt [1]	61,803	763	4.90%
Total loans [1]	1,287,740	15,349	4.73%
Total Interest-earning assets [1]	4,587,848	36,153	3.14%
Other assets	853,764		
Total assets	$5,441,612		
Liabilities and shareholders' equity			
Noninterest-bearing demand	$2,103,042	$-	- %
Savings and interest-bearing transaction	2,367,501	280	0.05%
Time less than $100,000	135,363	78	0.23%
Time $100,000 or more	108,673	103	0.38%
Total interest-bearing deposits	2,611,537	461	0.07%
Short-term borrowed funds	76,083	12	0.06%
Total interest-bearing liabilities	2,687,620	473	0.07%
Other liabilities	51,477		
Shareholders' equity	599,473		
Total liabilities and shareholders' equity	$5,441,612		
Net interest spread [1] [2]			3.07%
Net interest and fee income and interest margin [1] [3]		$35,680	3.10%

[1] Amounts calculated on an FTE basis using the current statutory federal tax rate.

[2] Net interest spread represents the average yield earned on interest-earning assets less the average rate incurred on interest-bearing liabilities.

[3] Net interest margin is computed by calculating the difference between interest income and expense, divided by the average balance of interest-earning assets. The net interest margin is greater than the net interest spread due to the benefit of noninterest-bearing demand deposits.

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Distribution of Assets, Liabilities & Shareholders’ Equity and Yields, Rates & Interest Margin

	For the Nine Months Ended September 30, 2018		
	Average Balance	Interest Income/ Expense	Yields/ Rates
	($ in thousands)		
Assets			
Investment securities:			
Taxable	$2,781,814	$47,327	2.27%
Tax-exempt [1]	756,910	18,697	3.29%
Total investments [1]	3,538,724	66,024	2.49%
Loans:			
Taxable	1,159,049	42,876	4.95%
Tax-exempt [1]	56,663	1,734	4.09%
Total loans [1]	1,215,712	44,610	4.91%
Total Interest-earning assets [1]	4,754,436	110,634	3.11%
Other assets	846,063		
Total assets	$5,600,499		
Liabilities and shareholders' equity			
Noninterest-bearing demand	$2,186,250	$-	- %
Savings and interest-bearing transaction	2,450,893	924	0.05%
Time less than $100,000	121,619	210	0.23%
Time $100,000 or more	97,877	283	0.39%
Total interest-bearing deposits	2,670,389	1,417	0.07%
Short-term borrowed funds	62,131	28	0.06%
Total interest-bearing liabilities	2,732,520	1,445	0.07%
Other liabilities	56,233		
Shareholders' equity	625,496		
Total liabilities and shareholders' equity	$5,600,499		
Net interest spread [1] [2]			3.04%
Net interest and fee income and interest margin [1] [3]		$109,189	3.07%

(1) Amounts calculated on an FTE basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate incurred on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense, divided by the average balance of interest-earning assets. The net interest margin is greater than the net interest spread due to the benefit of noninterest-bearing demand deposits.

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Distribution of Assets, Liabilities & Shareholders' Equity and Yields, Rates & Interest Margin

	For the Nine Months Ended September 30, 2017		
	Average Balance	Interest Income/ Expense	Yields/ Rates
	($ in thousands)		
Assets			
Investment securities:			
Taxable	$2,459,360	$37,584	2.04%
Tax-exempt (1)	817,443	24,154	3.94%
Total investments (1)	3,276,803	61,738	2.51%
Loans:			
Taxable	1,261,726	44,777	4.74%
Tax-exempt (1)	63,402	2,388	5.04%
Total loans (1)	1,325,128	47,165	4.76%
Total Interest-earning assets (1)	4,601,931	108,903	3.16%
Other assets	805,730		
Total assets	$5,407,661		
Liabilities and shareholders' equity			
Noninterest-bearing demand	$2,069,521	$-	- %
Savings and interest-bearing transaction	2,373,814	839	0.05%
Time less than $100,000	138,483	242	0.23%
Time $100,000 or more	110,512	314	0.38%
Total interest-bearing deposits	2,622,809	1,395	0.07%
Short-term borrowed funds	71,976	34	0.06%
Total interest-bearing liabilities	2,694,785	1,429	0.07%
Other liabilities	51,664		
Shareholders' equity	591,691		
Total liabilities and shareholders' equity	$5,407,661		
Net interest spread (1) (2)			3.09%
Net interest and fee income and interest margin (1) (3)		$107,474	3.12%

(1) Amounts calculated on an FTE basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate incurred on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense, divided by the average balance of interest-earning assets. The net interest margin is greater than the net interest spread due to the benefit of noninterest-bearing demand deposits.

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Summary of Changes in Interest Income and Expense due to Changes in Average Asset & Liability Balances and Yields Earned & Rates Paid

The following tables set forth a summary of the changes in interest income and interest expense due to changes in average assets and liability balances (volume) and changes in average interest yields/rates for the periods indicated. Changes not solely attributable to volume or yields/rates have been allocated in proportion to the respective volume and yield/rate components.

Summary of Changes in Interest Income and Expense

	For the Three Months Ended September 30, 2018 Compared with For the Three Months Ended September 30, 2017		
	Volume	Yield/Rate	Total
	(In thousands)		
Increase (decrease) in interest and loan fee income:			
Investment securities:			
Taxable	$1,831	$ 1,992	$3,823
Tax-exempt [(1)]	(597)	(1,073)	(1,670)
Total investments [(1)]	1,234	919	2,153
Loans:			
Taxable	(1,017)	592	(425)
Tax-exempt [(1)]	(91)	(126)	(217)
Total loans [(1)]	(1,108)	466	(642)
Total increase in interest and loan fee income [(1)]	126	1,385	1,511
Increase (decrease) in interest expense:			
Deposits:			