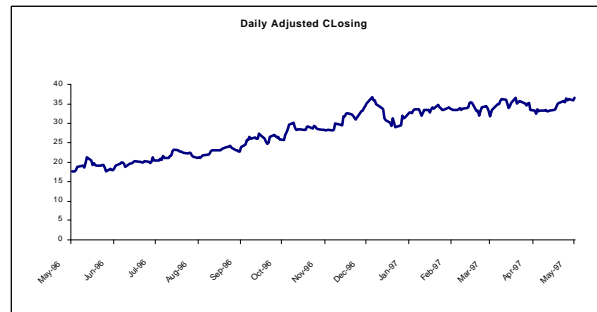




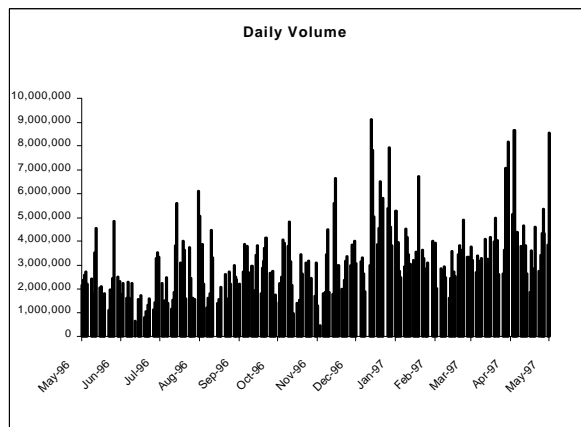
Stock Data

| | |
|----------------------|-------------------|
| Price (52 weeks) | \$17.58 - \$37.29 |
| Symbol/Exchange | WM NYSE |
| Beta | .66 |
| Dividend yield | 2.46% |
| Fully diluted shares | 877.6 Million |
| Average daily volume | 3.56 Million |
| Current market cap | \$31.4 Billion |
| Book Value/Share | \$14.06 |
| LTD Ratio | 25.34% |



Valuation (per share)

| | |
|---------------------|---------|
| FCF Analysis | \$14.50 |
| Comparable Analysis | \$24.62 |
| Target Price | \$15.00 |



Summary Financials (in millions)

| | 2000A |
|----------------|----------|
| Revenue | \$15,767 |
| Earnings | \$1,899 |
| Free Cash Flow | \$1,639 |

Business Overview

Established after the Great Seattle Fire of 1889 (the fire destroyed over 120 acres of the city), Washington Mutual (WM) was incorporated to “help” the misfortunate souls rebuild their homes after the fire. WM is a financial services company (known as a thrift) that is focused on serving consumers and small to mid-sized businesses. WM is broken into various segments that deal in consumer banking, mortgage banking, commercial banking, financial services and consumer finance.

Consumer Banking (52% of revenue)

The consumer-banking group deals in a myriad of financial products and services to individuals and small businesses in Arizona, California, Florida, Idaho, Nevada, Oregon, Texas, Utah and Washington. The banking subsidiaries accept deposits from the general public, makes, buys and sells residential loans, consumer loans, and commercial loans, and engage in certain commercial banking activities. To serve their 5 million households, they have

over 1,100 traditional “financial centers” and over 1,600 automated teller machines in eight states. They also offer 24 hour telephone and internet banking services.

Mortgage Banking (21% of revenue)

The mortgage-banking group serves over 1.2 million households throughout the United States and is the nation's fifth-largest mortgage originator. They originate, purchase, sell and service specialty mortgage finance loans through its subsidiaries, Washington Mutual Finance Corporation and Long Beach Mortgage Company. They have 176 retail home loan centers, 22 wholesale home loan centers, and internet services.

Commercial Banking (2% of revenue)

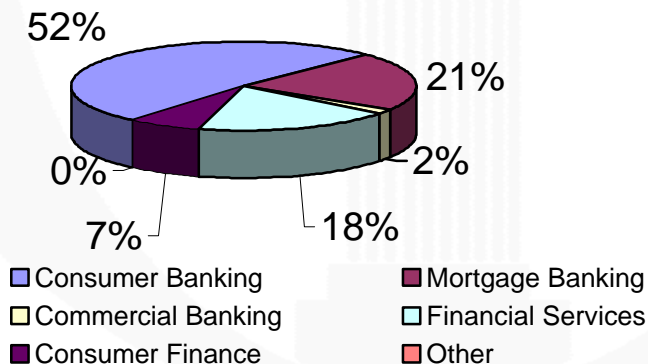
The commercial banking group is comprised of two primary business lines: commercial banking and commercial real estate lending. The commercial banking segment operating under the names of WM Business Bank (in California) and Western Bank (in Idaho, Oregon, Utah and Washington), while the commercial real estate segment operates under the Washington Mutual brand.

Financial Services (18% of revenue)

The financial services group is composed of three lines of business: WM Financial Services, Inc., WM Group of Funds, and Washington Mutual Insurance Services, Inc. Through licensed subsidiaries, WM markets annuities and other insurance products, offers full service securities brokerage operations, and acts as the investment advisor to and the distributor of mutual funds. WM’s investment services are offered through: Washington Mutual Financial Services, a licensed broker-dealer; WM Fund Advisors, Inc. providing investment advisory and distribution services for the WM Group of Funds; and the Annuity Program. At December 31, 2000, WMFS was licensed in 49 states

and Puerto Rico and operated in the eight states where its financial centers are located. Over 500 financial consultants and 800 licensed bank employees provide investment

Revenue Breakdown



services to retail customers. WM Advisors, the Company's registered investment advisor subsidiary, had \$8.21 billion of assets under management in 17 mutual funds, five asset management portfolios, and one variable annuity at December 31, 2000.

Washington Mutual Insurance Services is an insurance agency that offers fire, homeowners, flood, earthquake and other property and casualty insurance products, as well as, offering mortgage life insurance, accidental death and dismemberment, property and casualty, and life insurance products.

Consumer Finance (7% of revenue)

The consumer finance group consists of Washington Mutual Finance Corporation and Long Beach Mortgage. Washington Mutual Finance makes direct consumer installment loans and real estate secured loans, and purchases secured retail installment contracts from local retail establishments. Long Beach Mortgage is engaged in the business of originating, purchasing and selling specialty finance mortgage loans secured by one-to-four family residences.

Recent Acquisition

On January 31, 2001, WM acquired the mortgage operations of The PNC Financial Services Group, Inc. The company was then renamed Washington Mutual Home Loans, Inc. and Washington Mutual Mortgage Securities Corp. On February 9, 2001, WM acquired Texas-based Bank United Corp., which was merged into Washington Mutual, Inc. As a result, all of the subsidiaries of Bank United Corp., including Bank United, a federally chartered savings bank, became its subsidiaries. Bank United was subsequently merged into WMBFA. As a result of the acquisitions described above, the Company has been transformed into a national financial services company. Although it operates principally in California, Washington, Oregon, Florida, Texas and Utah, WM has physical operations in 42 states.

Industry Analysis

Washington Mutual, Inc. is part of a subset of the financial institution market known as thrifts. Thrifts are the nation's fourth-largest group of financial institutions in terms of assets, after commercial banks, mutual funds, and insurance companies. As of December 31, 2001, there were 1,091 savings and loans (S&Ls) and 533 savings banks in the United States, according to the Federal Deposit Insurance Corporation (FDIC). These institutions held total assets of about \$1,222.6 billion and had total net income of 10.75 billion for the year 2000.

Types of Thrifts

The primary business of thrifts is to provide credit for residential housing with retail deposits supplying these funds. There are four basic types of thrifts; savings and loans (S&Ls), savings banks, cooperatives, and credit unions. Thrifts can either be federally or state chartered, allowing them to only do business within the charter's boundaries.

Savings and loans (S&Ls)- also called federal savings banks, S & Ls are federally chartered. S & Ls are required to keep 65% of their assets in housing-related investments. In the Midwest, certain federal S&Ls are called "building and loans." Of all the thrifts, the S&Ls are the most liberal. S & Ls can create subsidiaries through which they can engage in real estate, insurance, discount brokerage, and other non-thrift activities. Federal S&Ls may also be owned by non-bank entities.

Savings banks- Savings banks are state-chartered depository institutions that are more like banks than other thrifts in that they tend to hold higher balances of commercial and consumer loans. They are mainly located in the Northeast.

Cooperatives- Cooperatives are state-chartered thrifts located in New England. They are the same as savings and loans in all but name.

Credit unions- Credit unions are nonprofit organizations that offer various banking services to people who share a common bond, usually those that work for the same employer.

Since most institutions are small in size and focused on local in reach, the U.S. thrift industry is highly fragmented. However, there are some very large thrifts. The 10 largest thrifts accounted for more than half of the over 1222.6 billion in assets.

LEADING THRIFT INSTITUTIONS

(Ranked by total assets, as of December 31, 1999)

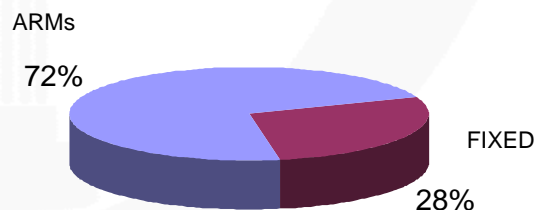
| COMPANY | ASSETS (MIL \$) | |
|-------------------------------|-----------------|----------|
| | 12/31/98 | 12/31/99 |
| 1. Washington Mutual Inc | 165,493 | 186,514 |
| 2. Golden State Bancorp | 54,869 | 57,019 |
| 3. Golden West Financial | 38,469 | 42,142 |
| 4. Sovereign Bancorp | 21,914 | 26,587 |
| 5. Dime Bancorp Inc. | 22,321 | 23,921 |
| 6. Astoria Financial Corp. | 20,588 | 22,697 |
| 7. Bank United Corp. | 14,940 | 17,352 |
| 8. GreenPoint Financial Corp. | 15,016 | 15,395 |
| 9. Peoples Heritage Financial | 12,050 | 13,919 |
| 10. Commercial Federal Corp. | 12,076 | 13,349 |

Source: American Banker.

INTEREST RATE SENSITIVITY

Thrifts are extremely interest rate sensitive, their profits vary inversely with the direction of interest rates. This occurs because thrift's liabilities (principally deposits) are short-term

Mortgage Rates



in nature, while its assets (mainly mortgages) are long-term. So when interest rates rise, deposit costs rise quicker than mortgage yields, putting pressure on their spread. When interest rates fall they tend to lower deposit costs, while loan yields adjust more slowly, causing a wider spread.

Ever since the S & L crash of the 80's, many thrifts have tried to minimize the impact of changes in the interest rates on their bottom line. Currently, the most popular method to do this is with adjustable rate mortgages (ARMs), as opposed to fixed rate mortgages. Presently, there are two main types of; one year ARMs that are tied to the T-Bill rates and adjust once a year, and monthly ARMs that are tied to a cost of funds index (a ratio of the dollar amount paid in interest during the month to the average dollar amount of the principle for that month). However both of these are imperfect hedges. ARMs are extremely popular with consumers when interest rates are high; however, fixed rates become more popular in low-rate environments.

The Bad News

Over the past fifteen years, S&Ls have experienced a decline in their share of the new and refinanced mortgage origination market. In 1985, thrifts originated 41% of the total mortgages in the United States, compared with 35% for mortgage bankers. By 1991, thrifts' percentage of new and refinanced residential mortgages fell to 25%, versus 45% for mortgage bankers. In 1997 (latest available), S&Ls originated 18% of the total \$907.1 billion in new and refinanced residential mortgage loans, compared with commercial banks' 26% share and mortgage bankers' 56% share.

One of the major reasons for this is that competition among the various mortgage originators has intensified. Commercial banks have entered the mortgage business, this is because their risk-based capital requirements give them a credit for low-risk mortgage assets, and also because commercial lending is also undergoing a profit squeeze. Mortgage bankers have also evolved as major players, garnering a growing share of the mortgage origination market. This is largely because of their relatively newfound staying power. During the 1991-93 refinancing boom, many mortgage bankers built up their capital coffers, giving them the staying power to survive the inevitable next downturn. Previously, mortgage bankers would simply vanish during down cycles.

A thrift's basic business involves acquiring retail deposits and using these deposits to provide loans for residential housing. One of the largest problems that is affecting the industry is the declining deposit-to-asset ratios (57.3% 2000, 58.1% 1999, and 70.7% in 1995). With the decline in the ratio, thrifts have been forced to look elsewhere to higher cost funding sources. This is done mainly through Federal Home Loan Banks. Because borrowings is a more expensive funding source than deposits, a continued decrease in the deposits-

to-assets ratio can be expected to put pressure on a thrifts' net interest margin.

The reason for the decrease in deposits is due, mainly from mutual funds. Mutual funds have gained a lot of popularity because of the advent of the individual retirement account (IRA) and the money market. Another reason was the past decade's stock market rally, as well as greater "investor sophistication," this caused many investors to seek higher-yielding investment. The decline can also be partially attributed to the problems that S&L's faced in the mid to late 1980's. Depositors are weary about future problems with these types of financial institutions. Further, many consumers

Survival of the Fittest

Due to the increase in competition in the thrift's main business, as well as the capitalistic search for greater profits, many thrifts have started to pursue a more commercial banking model of business. Companies pursuing this strategy include Washington Mutual and Charter One Financial, Inc. At the end of 2000, Charter One formally converted to a bank holding company.

By shifting their mix of assets and liabilities, many thrifts hope to boost their profitability to the level of commercial banks. On the liability (or funding) side, many thrifts are trying to increase checking accounts in an effort to lower their cost of funds. On the asset side, thrifts are expanding consumer and business lending in an effort to boost yields. In addition to all this, thrifts are also trying to increase investment products in order to increase fee income.

Consolidation is a trend that has been reshaping the thrift industry since the early 1980s. In 1980, there were approximately 4,000 thrift institutions. By 1990, that number had dwindled to 2,616. From 1990 to year-end 1998, the number of thrifts declined by more than 50%. At June 30, 2000, the total number of OTS-regulated thrift institutions was 1,091. This trend makes the thrift industry one of the most rapidly consolidating industries in the United States. One of the main reasons for this is that because thrifts have large caches of low-risk deposit, which look very inviting to banks looking for more ways to access cheap funding.

A Changing but Heavily Regulated Industry

Ever since the near failure of the thrift industry in the late 1980's, federal regulations have become stricter and stricter as time has passed. For instance, the Financial Institutions Reform Recovery, and Enforcement Act of 1989, created a stricter capital (the amount the company must hold for each loan) environment. This had led to the decrease in loans available per deposit. However, ever since 1996 and the later repeal of the Glass-Steigal act, the regulators have slowly been easing up their restrictions on both banks and the thrift industry.

The Bread & Butta Analysis

When analyzing a thrift, there are three major things to look at, they are:

One of the most important factors to a thrift's success is its net worth, or capitalization. Capitalization means many things to thrifts, such as how much they can loan out, a means of expansion, a measure of the ability to pay dividends, and a cushion against losses. It has been shown that capitalization and profitability are related. The more funds an institution has free, the more they can lend out, and the more profits they can earn on the spread. The way the industry measures the capitalization of a firm is the ratio of tangible shareholders' equity divided by assets (since I could not find an abbreviation for this ratio, I will call it cap ratio). For thrifts that focus on low risk, single family lending, a cap ratio of 5 to 6% is adequate. A cap ratio of 9% shows a thrift with a strong financial footing. However, too high a cap ratio (11 - 12%) signifies that an institution is carrying too much excess capital and is not earning its potential.

A thrift's interest rate spread is the same as a operating firm's profit margin. This is the bread and the butter that allows these firms to survive. The spread is the difference between the rates a thrift earns on its interest earning assets (mortgages, loans) and the rate it pays for its interest bearing liabilities (deposits). During 2000, the S & L spread range was from 1.9% to 3.5%, the average being at 2.7%

The last of the main three things to look at when analyzing a thrift is its coverage ratio (net interest divided by general and administrative costs.) This ratio generally ranges between 95% to 250% states how much of a thrift's overhead is covered by their income spread.

| | WM | CF | DME | GDW | Industry |
|-----------------------|-----------|-----------|------------|------------|-----------------|
| ROA | 1.06% | 1.34% | 0.71% | 1.15% | 1.13% |
| ROE | 21.19% | 18.00% | 10.98% | 16.99% | 14.13% |
| Capital Ratio | 19.15% | 13.42% | 14.89% | 15.10% | 11.00% |
| Coverage Ratio | 108.46% | 78.44% | 34.70% | 127.22% | 172.50% |

From the table above, we can see that WM leads both its closest competitors in both the capital ratio and ROE. However, they are lower than average for both coverage ratio and ROA.

Discounted Cash Flow Analysis

I used the percentage of sales for calculating expenses, changes in net working capital, capital expenditures, and depreciation. Revenues were separated into two parts, consisting of interest income and noninterest income. This was done because revenues incurred from the company arise from these two main segments that differ in growth. Expenses were also separated into interest expense and noninterest expenses, and were assumed to be constant. I

assumed that in the end the interest rate all even out over the long-run and because interest rates change often and I would be unable to forecast them for three, four, or five years into the future.

We assumed that depreciation, capital expenditures, and changes in net working capital will all continue to reflect, close to, the same percentage of sales growth as they averaged over the last couple years. Finally, we used a terminal rate of 3% after

The analysis assumes that the thrift market will continue to grow for the next couple of years, then in 2003, growth declines due to the fact that the thrift market is starting to decline in general, I then assumed that by 2005 WM would have changed its core business enough into a bank that growth would resume. I came up with an implied share price of \$14.50, which is \$24.09 less, then the price on Monday May 21st.

Comparables Valuation

When I ran my comparables valuation, I took the three largest (excluding WM) thrift institutions and compared them on three attributes. The first two are pretty standard; price to sales, and price to earnings, however, the third one is brand new. As I mentioned above, capitalization is how a thrift grows, so I figured a good way to value a thrift is through a price to capital ratio. These numbers are not published but I was able to calculate them by using the capital ratio of shareholder's equity (tangible) over total assets. The following are the companies I chose:

Golden West Financial Corporation (GDW)- GDW is a savings and loan holding company. Their main operation is a savings bank business through World Savings Bank, FSB. The Company operates 120 savings branch offices in California, 37 in Florida, 36 in Colorado, 22 in Texas, 15 in Arizona, 11 in New Jersey, eight in Kansas, and four in Illinois. In addition, the Company operates 278 loan origination offices.

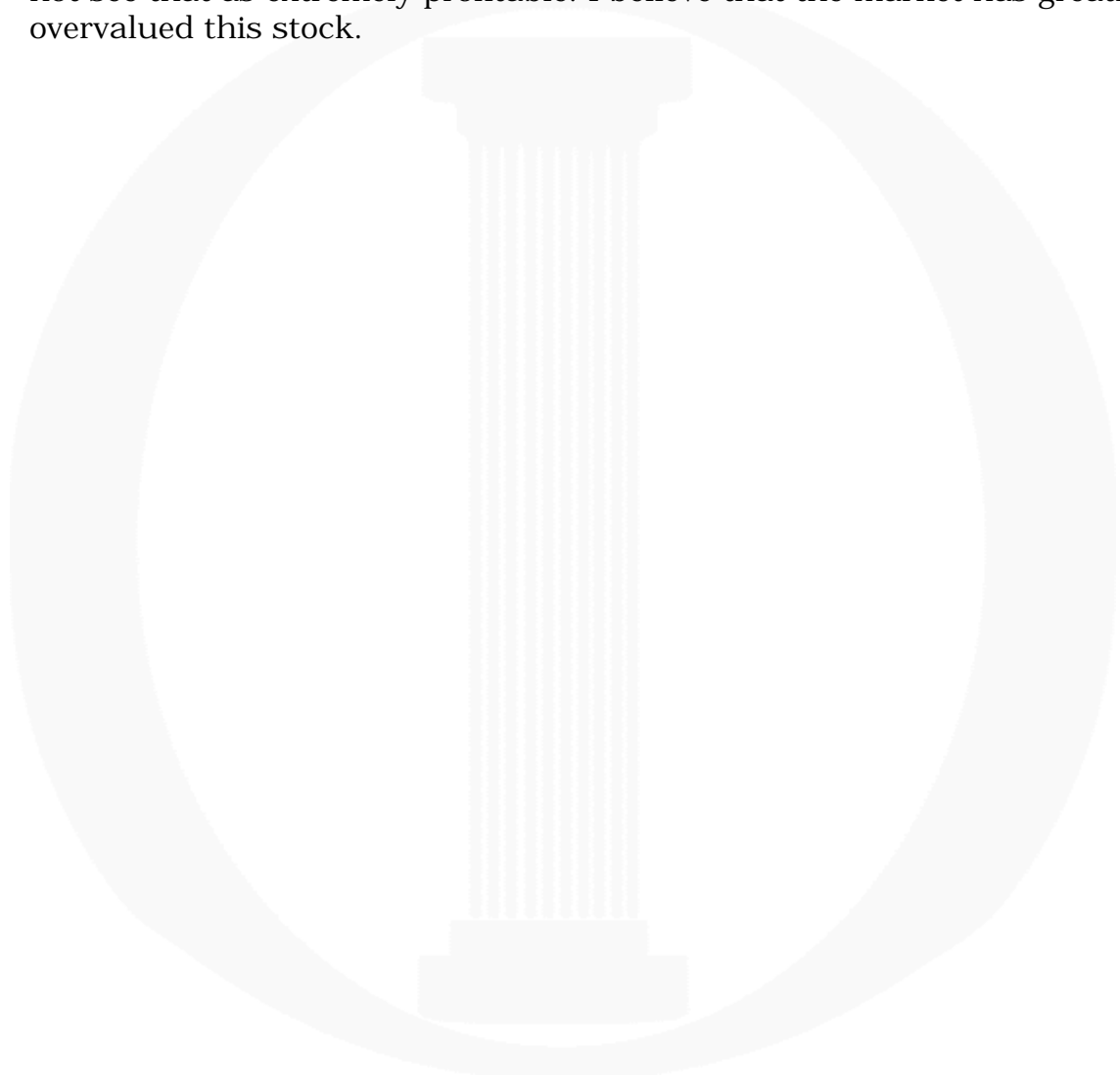
Charter One Financials, Inc (CF)- Charter One Financial, Inc. is another financial holding company. CF's principal line of business is running consumer banks and thrifts. This is primarily conducted through the operations of Charter One Bank, F.S.B. and its subsidiaries. CF manages \$33 billion in total assets and operates 419 banking centers in six Midwest and Northeast states. In addition to retail and business banking services in those areas, its diverse product set also positions the Company to serve other areas of the United States, with commercial leasing services, indirect auto lending and mortgage banking.

Dime Bancorp Inc. (DME)- is a savings and loan holding company. DME's main business is ran through The Dime Savings Bank of New York, FSB. The principal subsidiary of the Bank is North American Mortgage Company, a mortgage banking company. DME currently operates 123 banking branches located throughout the greater New York City metropolitan area and conducts its mortgage banking activities nationwide.

I then weighted the different ratios based on importance. I weighted the price to sales ratio less then the other two because in all businesses, it does not matter how much money you bring in, it only matters how much you make. With my weighting I got an implied per share price of \$24.62.

Recommendation

Looking back at all the information I have found and considering both of my valuations. I recommend a **HOLD** on this stock. From what I found, the thrift market is slowly declining and merging into the banking sector. WM is the powerhouse in the thrift sector, and I see them making the change into the banking successfully, but that is only after some time has passed and I still do not see that as extremely profitable. I believe that the market has greatly overvalued this stock.





UNIVERSITY OF OREGON
INVESTMENT GROUP

May 21, 2001
Financials (Thrift)

| | 1996A | 1997A | 1998A | 1999A | 2000A | 2001E | 2002E | 2003E | 2004E | 2005E | 2006E |
|--------------------------|--------------------------|---------------|-------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Interest Income | 9,892 | 10,203 | 11,222 | 12,062 | 13,783 | 15,816 | 18,267 | 21,008 | 24,054 | 27,722 | 32,157 |
| % | | 3.14% | 9.99% | 7.49% | 14.27% | 14.75% | 15.50% | 15.00% | 14.50% | 15.25% | 16.00% |
| Non Interest Income | 934 | 981 | 1,507 | 1,509 | 1,984 | 2,480 | 3,143 | 3,953 | 4,941 | 6,226 | 7,891 |
| % | | 5.01% | 53.72% | 0.12% | 31.48% | 25.00% | 26.75% | 25.75% | 25.00% | 26.00% | 26.75% |
| Interest Expense | 6,027 | 6,287 | 6,930 | 7,610 | 9,472 | 10,978 | 12,847 | 14,976 | 17,397 | 20,369 | 24,029 |
| % | 55.67% | 56.22% | 54.44% | 56.08% | 60.07% | 60.00% | 60.00% | 60.00% | 60.00% | 60.00% | 60.00% |
| Non Interest Expense | 3,610 | 3,111 | 3,268 | 2,910 | 3,126 | 3,659 | 4,282 | 4,992 | 5,799 | 6,790 | 8,010 |
| % | 33.34% | 27.82% | 25.67% | 21.44% | 19.83% | 20.00% | 20.00% | 20.00% | 20.00% | 20.00% | 20.00% |
| Income Before LP | 1,189 | 1,785 | 2,532 | 3,051 | 3,169 | 3,659 | 4,282 | 4,992 | 5,799 | 6,790 | 8,010 |
| | 10.98% | 15.96% | 19.89% | 22.48% | 20.10% | | | | | | |
| Loan Loss Provision (LP) | 499 | 247 | 162 | 167 | 185 | 220 | 257 | 300 | 348 | 407 | 481 |
| % | 4.61% | 2.21% | 1.27% | 1.23% | 1.17% | 1.20% | 1.20% | 1.20% | 1.20% | 1.20% | 1.20% |
| Net Income | 691 | 1,538 | 2,370 | 2,884 | 2,984 | 3,440 | 4,025 | 4,693 | 5,451 | 6,382 | 7,529 |
| | 6.38% | 13.76% | 18.62% | 21.25% | 18.93% | | | | | | |
| Dep & Amort | 319 | 308 | 314 | 400 | 539 | 549 | 642 | 749 | 870 | 1,018 | 1,201 |
| % | 2.95% | 2.76% | 2.46% | 2.95% | 3.42% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% |
| Tax Rate | 29% | 37% | 37% | 37% | 36% | 37% | 37% | 37% | 37% | 37% | 37% |
| After Tax Income | 618 | 924 | 1,389 | 1,670 | 1,674 # | 1,960 | 2,293 | 2,673 | 3,105 | 3,636 | 4,289 |
| | 5.70% | 8.26% | 10.91% | 12.31% | 10.62% | | | | | | |
| Capital Exp | 130 | 346 | 846 | 1,335 | 1,420 | 1,647 | 1,927 | 2,246 | 2,610 | 3,055 | 3,604 |
| | 1.20% | 3.09% | 6.65% | 9.83% | 9.00% | 9.00% | 9.00% | 9.00% | 9.00% | 9.00% | 9.00% |
| Change in NWC | (148) | 51 | 233 | 19 | 217 | 183 | 214 | 250 | 290 | 339 | 400 |
| | -1.37% | 0.45% | 1.83% | 0.14% | 1.38% | 1.00% | 1.00% | 1.00% | 1.00% | 1.00% | 1.00% |
| Add Dep & Amort | 319 | 308 | 314 | 400 | 539 | 549 | 642 | 749 | 870 | 1,018 | 1,201 |
| Free Cash Flow | 955 | 836 | 624 | 716 | 576 # | 679 | 794 | 926 | 1,076 | 1,259 | 1,486 |
| Terminal Value | | | | | | | | | | | 51364 |
| PV of Future CF | | | | | | 641 | 709 | 780 | 856 | 946 | 1055 |
| PV of Terminal Value | | | | | | | | | | | 36456 |
| Number of Shares | 877.5 Million | | CAPM | | 9.80% | | | | | | |
| Return on Debt | 7.00% | | WACC | | 5.88% | | | | | | |
| Beta | 0.66 | | Terminal Value | | 3% | | | | | | |
| Risk Free Rate | 4.85% (5 year note rate) | | PV of Future Cash Flows | | \$ 42,676 | | | | | | |
| Market Premium | 7.50% | | Total LTD | | \$ 29,951 | | | | | | |
| Weight of Equity | 25.34% | | Implied Price | | \$ 14.50 | | | | | | |
| Weight of Debt | 74.66% | | | | | | | | | | |

Comparables (Appendix B)

| | | | | DME | | Average | Implied Price |
|-----------------------------|-----------|--------|--------|--------|--------|-------------|---------------|
| | Weighting | WM | GDF | | CF | | |
| Price to Earnings | 40% | 13.91 | 16.52 | 23.97 | 14.68 | 13.91 | \$ 30.10 |
| Price to Sales | 20% | 2.01 | 2.38 | 2.39 | 2.79 | 2.52 | \$ 45.27 |
| Market Cap to Capital Ratio | 40% | 1.64 | 0.65 | 0.27 | 0.46 | 0.459871157 | \$ 8.81 |
| Beta | | 0.72 | 0.42 | 0.93 | 0.93 | | |
| Market Cap | | 31.4 B | 9.75 B | 4.09 B | 6.17 B | | |
| ROA | | 1.06% | 1.15% | 0.71% | 1.34% | | |
| Implied Price | | | | | | | \$ 24.62 |

