Risk Factors Comparison 2024-03-15 to 2023-03-17 Form: 10-K

Legend: **New Text** ~~Removed Text~~ Unchanged Text Moved Text Section

Adverse economic conditions in market areas we serve could adversely impact our earnings and could increase the credit risk associated with our loan portfolio. A significant portion of our loans are to businesses and individuals in the state of Washington. An economic decline affecting our region could have a material adverse effect on our business, financial condition, results of operations, and prospects. Weakness in the global economy has adversely affected many businesses operating in our markets that are dependent on international trade. Deterioration in the national economy ~~as a result of continued inflation, the rising interest rate environment, and recurring supply chain issues~~ may also have an adverse effect on the region. Any future deterioration in economic conditions in the market areas we serve, in particular the North Olympic Peninsula and Puget Sound area of Washington State, could result in the following consequences, any of which could have a materially adverse impact on our business, financial condition **,** and results of operations: • ~~loan~~ **Loan** delinquencies, problem assets and foreclosures may increase; • ~~demand~~ **Demand** for our products and services may decline, possibly resulting in a decrease in our total loans or assets; • ~~loan~~ **Loan** collateral may decline in value, exposing us to increased risk of loss on existing loans and reducing customers' borrowing power; • ~~the~~ **The** net worth and liquidity of loan guarantors may decline, impairing their ability to honor commitments to us; and • ~~the~~ **The** amount of our deposits may decrease and the composition of our deposits may be adversely affected. A decline in local economic conditions may have a greater effect on our earnings and capital than on the earnings and capital of larger financial institutions whose real estate loan portfolios are geographically diverse. If we are required to liquidate a significant amount of collateral during a period of reduced real estate values, our financial condition and profitability could be adversely affected. Adverse changes in the regional and general economy could reduce our growth rate, impair our ability to collect loans, and generally have a negative effect on our financial condition and results of operations. Public health crises, geopolitical developments, acts of terrorism, natural disasters, climate change and other external factors could harm our business. Public health crises, domestic or geopolitical crises, such as the current ~~invasion of~~ **wars in** Ukraine ~~by Russia~~ **and the Middle East** , political instability or civil unrest, terrorism, human error or other events outside of our control, could cause disruptions to our business or the United States' economy, resulting in potentially adverse operating results. Natural disasters may disrupt our operations, result in damage to our properties, reduce or destroy the value of the collateral for our loans and negatively affect the economies in which we operate. Climate change may worsen the severity and impact of future natural disasters and other extreme weather- related events that could cause disruption to our business and operations. Chronic results of climate change such as shifting weather patterns could also cause disruption to the business and operations of our customers, with potentially negative effects on our loan portfolio and growth opportunities. A significant natural disaster, such as a tsunami, earthquake, **drought,** fire or flood, where we or our customers live and do business, could have a material adverse impact on our local market areas and our ability to conduct business, especially if our insurance coverage is insufficient to compensate for losses that may occur. The effects of any of the foregoing factors could have a material adverse effect on our business, operations **,** and financial condition. Conditions in the financial markets may limit our access to additional funding to meet our liquidity needs, which could adversely affect our earnings and capital levels. Liquidity is essential to our business. We rely on a variety of sources in order to meet our potential liquidity demands. We require enough liquidity to meet customer loan requests, customer deposit maturities and withdrawals, payments on our debt obligations as they come due and other cash commitments under both normal operating conditions and other unpredictable circumstances, including events causing industry or general financial market stress. A tightening of the credit markets and the inability to obtain adequate funding may negatively affect our liquidity, asset growth and, consequently, our earnings capability and capital levels. In addition to any deposit growth, and the sale of loans or investment securities, maturity of investment securities and loan payments, we rely from time to time on advances from the FHLB and certain other wholesale funding sources to meet liquidity demands. Our liquidity position could be significantly constrained if we were unable to access funds from the FHLB or other wholesale funding sources. Factors that could detrimentally impact our access to liquidity sources include actions by the FRB, a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated, negative operating results, or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as consumer and business behavior utilizing funds on deposit to pay down higher cost debt or to seek higher yielding investments, a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry or deterioration in credit markets. Any decline in available funding could adversely impact our ability to originate loans, invest in securities, meet our expenses, or fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could, in turn, have a material adverse effect on our business, financial condition and results of operations. Additionally, collateralized public funds are bank deposits of state and local municipalities. These deposits are required to be secured by certain investment grade securities or other collateral to ensure repayment, which on the one hand tends to reduce our contingent liquidity risk by making these funds somewhat less credit sensitive, but on the other hand reduces standby liquidity by restricting the potential liquidity of the pledged collateral. Although these funds historically have been a relatively stable source of funds for us, availability depends on the individual municipality' s fiscal policies and cash flow needs. **Competition for deposits may limit our ability to grow. Our loan growth is primarily dependent on retaining and attracting additional customer deposits. While we emphasize the generation of low- cost core deposits as a source of funding, there is strong competition for such deposits in our market area, including from internet- based banking institutions, which have grown rapidly in recent years. Deposit flows are influenced by various factors, including customer relationships, sales and**

marketing efforts, interest rates paid by competitors, alternative investments such as money market mutual funds, equities and bonds, government stimulus programs, and the overall levels of business and personal income and savings. The **current elevated interest rate environment has increased competition for deposits across** ~~continued economic effects of the COVID- 19 pandemic could adversely impact our financial results and those~~ -- **the** ~~of our~~ **banking industry, and deposit balances may decrease if** customers **perceive alternative investments as providing a better risk / return tradeoff** . **Our failure to grow or retain deposits may** ~~The COVID- 19 pandemic and related government actions caused significant economic turmoil in the U. S. and around the world, resulting~~ --- **result** in a **loss of** ~~slow- down in economic activity, increased unemployment levels and disruptions in global supply chains and financial markets~~ - **market** ~~. The long- term economic effects of the COVID- 19 pandemic are~~ **share** ~~difficult to predict due to the ongoing dynamic nature of COVID- 19 variants, the possibility of a similar health crisis~~ and ~~potential~~ **slower** ~~for~~ - **or negative** ~~additional government action. Management is confronted with a significant and unfamiliar degree of uncertainty in estimating the impact of the pandemic on credit quality, revenues and asset values. Although the Company estimates~~ loan **growth** ~~losses related to the pandemic as part of its evaluation of the allowance for loan losses~~ , **which likely would** ~~such estimates involve significant judgment and are made in the context of substantial uncertainty as to the long- term impact of the pandemic on the credit quality of our loan portfolio. Consistent with guidance provided by banking regulators, we modified loans by providing various loan payment deferral options to our borrowers affected by the COVID- 19 pandemic. Notwithstanding these modifications, not every borrower may be able to recover and make full payments on their loans. Any increases in the allowance for credit losses will result in a decrease in net income and may~~ have **an adverse** ~~a material negative~~ effect on our financial condition and results of operations ~~. Although the U. S. and global economies have started recovering as governments lift or reduce health- related restrictions and as demand for goods and services increases, some adverse consequences including labor shortages, disruptions of global supply chains, and increasing inflation, continue to negatively impact the international, national, and local economies. As a result, our business may be materially and adversely affected. To the extent the effects of the COVID- 19 pandemic adversely impact our business, financial condition, liquidity or results of operations, it may also have the effect of heightening many of the other risks described in this section~~ . Credit and Asset Quality Our increased emphasis on commercial real estate lending subjects us to various risks that could adversely impact our results of operations and financial condition. We have increased the amount of our commercial real estate and multi- family loans to $ ~~643~~ **721** . ~~8~~ **1** million, or ~~42~~ **43** . ~~0~~ **4** % **,** of our total loan portfolio, at December 31, ~~2022~~ **2023** , from $ ~~535~~ **641** . ~~7~~ **6** million, or ~~39~~ **41** . 5 %, of our total loan portfolio at December 31, ~~2021~~ **2022** . We intend to continue to increase, subject to market demand, our origination and purchase of commercial real estate loans. As an institution' s concentration in commercial real estate lending increases, it becomes subject to more scrutiny under the FDIC' s policies for management of its commercial real estate loan portfolio. Our increased focus on this type of lending has increased our risk profile. Commercial real estate loans are intended to enhance the average yield of our earning assets; however, they do involve a different level of risk compared to one- to **-** four ~~-~~ family loans. The repayment of commercial real estate loans typically depends on the successful operation and income stream of the borrowers' operating business, or their ability to lease the commercial property at sufficient rates. The value of the commercial real estate securing the loan as collateral is a secondary source of repayment in case of default, which can be significantly affected by economic conditions. ~~Recently~~ **The FDIC has issued pronouncements alerting banks of its concerns about banks with a heavy concentration of commercial real estate loans. Moreover** , federal ~~banking~~ **bank** regulators **have** highlighted the increased risk associated with commercial real estate loans ~~as a result of the stress COVID- 19 created for some industries~~ , ~~and~~ **including with respect to** the higher vulnerability of these credits to pressure **as** ~~from the current rising~~ interest ~~rate~~ **rates** ~~environment~~ **remain elevated** and **market conditions** ~~overall inflationary pressures~~ in ~~the economy~~ **many metropolitan areas continue to show signs of stress** . These loans also involve larger balances to a single borrower or groups of related borrowers. Some of our commercial borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development on a single one- to **-** four ~~-~~ family residential mortgage loan. Since commercial real estate loans generally have large balances, deterioration in the quality of commercial loans may result in the need to significantly increase our provision for ~~loan~~ **credit** losses **on loans** and charge- offs will likely be larger on a per loan basis compared to consumer loans. As a result, deterioration of this portfolio could have a materially adverse effect on our future earnings. Collateral evaluation and financial statement analysis for commercial loans also requires a more detailed review at origination and on an ongoing basis. Finally, if we foreclose on a commercial real estate loan, our holding period for the collateral is typically longer than for a one- to **-** four ~~-~~ family residence because the market for most types of commercial real estate is not readily liquid, resulting in less opportunity to mitigate credit risk by selling part or all of our interest in these assets. At December 31, ~~2022~~ **2023** , we had $ ~~51~~ **28** , 000 of nonperforming commercial real estate loans and $ 0 of nonperforming multi- family loans in our portfolio **. An increase in unsecured lending exposes us to an increase in loan losses. We have increased our commercial business loan portfolio by purchasing unsecured loans to small businesses and professionals and our consumer loan portfolio through purchases from Splash Financial. Our exposure on these purchased loan portfolios was $ 21. 1 million and $ 7. 3 million, respectively, at December 31, 2023. Unsecured loans present additional risks to us because if a borrower defaults on an unsecured loan, there is no collateral to repossess and liquidate in order to satisfy the outstanding loan balance. Also, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on an unsecured loan in default. Our efforts to mitigate this risk include carefully assessing a borrower' s creditworthiness, including their income, employment history, and debt- to- income ratio. In 2022, we began purchasing unsecured consumer loans through a partnership with Splash Financial, a private lender that underwrites and funds personal loans. First Fed has experienced losses of $ 3. 4 million on the Splash Financial loans to date. We made changes to the program participation criteria for these loans in 2023 with the goal of reducing additional losses. Additional losses in our unsecured lending**

portfolio would negatively affect our profitability and capital . The significant growth in our loan portfolio and expansion into new markets may increase our credit risk. Since the completion of our initial public offering in January 2015, we have grown substantially in terms of total assets, total loans, total deposits, employees, and locations, expanding our business activities throughout the Puget Sound region. Our commercial loan portfolio, which includes loans for commercial and multi-family real estate as well as other business loans, has increased to $ ~~720~~ **833** . ~~8~~ **4** million, or ~~47~~ **50** . ~~0~~ **2** % of total loans, at December 31, ~~2022~~ **2023** , from $ ~~615~~ **718** . 6 million, or ~~45~~ **46** . 4 % of total loans, at December 31, ~~2021~~ **2022** . One- to **-** four ~~-~~ family loans have increased to $ ~~343~~ **378. 4 million, or 22** . 8 ~~million, or 22. 4~~ % of total loans, at December 31, ~~2022~~ **2023** , from $ ~~295~~ **343** . ~~0~~ **6** million, or ~~21~~ **22** . ~~7~~ **2** % of total loans, at December 31, ~~2021~~ **2022** . Total consumer loans have increased to $ ~~275~~ **318** . ~~1~~ **5** million, or ~~17~~ **19** . ~~9~~ **2** % of total loans, at December 31, ~~2022~~ **2023** , from $ ~~221~~ **291** . ~~9~~ **8** million, or ~~16~~ **18** . ~~4~~ **8** % of total loans, at December 31, ~~2021~~ **2022** . Rapidly growing loan portfolios are, by their nature, less seasoned and our experience with these loans may not provide us with a ~~significant~~ **useful** payment history pattern. Rapid growth combined with the geographic expansion of our lending area may make estimating loan loss allowances more difficult and more susceptible to changes in estimates, and to losses exceeding estimates, than our more seasoned portfolio of loans in our traditional lending area. As a result, it is difficult to predict the future performance of these parts of our loan portfolio. These loans may develop delinquency or charge- off levels above our historical experience, which could adversely affect our future performance. We plan to continue both strategic and opportunistic growth, understanding that we may see a slowing of growth as we mature and manage capital down to more efficient levels. Continued growth can present substantial demands on management personnel, line employees, and other aspects of our operations, especially if our growth occurs rapidly. We may face difficulties in managing that growth effectively, which could damage our reputation, limit our growth, and negatively affect our operating results. Also see" Our expansion strategy will cause our expenses to increase and may negatively affect our earnings." We have a concentration of large loans outstanding to a limited number of borrowers that increases our risk of loss. First Fed has extended significant amounts of credit to certain borrowers, largely in connection with high- end residential real estate and commercial and multi- family real estate loans. At December 31, ~~2022~~ **2023** , the aggregate amount of loans, including unused commitments, to First Fed' s five largest borrowers (including related entities) amounted to approximately $ ~~79~~ **95** . ~~4~~ **8** million. Outstanding loan balances for the ten largest borrowing relationships at December 31, ~~2022~~ **2023** , totaled $ ~~151~~ **171** . ~~9~~ **2** million, or ~~9~~ **10** . ~~9~~ **3** % of total loans. Although **only** ~~none~~ - **one** of the loans to First Fed' s 20 largest borrowers ~~were~~ **was** nonperforming ~~loans~~ as of December 31, ~~2022~~ **2023** , concentration of credit to a limited number of borrowers increases the risk in First Fed' s loan portfolio. If one or more of these borrowers is not able to service the contractual repayment, the potential loss to First Fed is more likely to have a material adverse impact on our business, financial condition and results of operations. Our construction and land loans are based upon estimates of costs and the value of the completed project. During the year ended December 31, ~~2022~~ **2023** , our construction and land loans decreased $ ~~30~~ **64** . ~~1~~ **0** million, or ~~13~~ **33** . ~~4~~ **0** %, to $ ~~194~~ **129** . 7 million, or ~~12.~~ 7 **. 8** %, of the total loan portfolio at December 31, ~~2022~~ **2023** and consisted of properties secured by ~~one- to four- family residential of $ 58. 7 million,~~ multi- family of $ ~~77~~ **66** . ~~0~~ **7** million, **one** ~~commercial acquisition~~ - ~~renovation~~ **to- four family residential** of $ ~~19~~ **43** . ~~3~~ **7** million, commercial real estate of $ ~~27~~ **11** . **8 million, and land of $** 7 ~~million, and land of $ 11~~ . ~~8~~ **5** million. Land loans include raw land and land acquisition and development loans. Construction and land development lending generally involves additional risks when compared with permanent residential lending because funds are advanced upon estimates of costs in relation to values associated with the completed project that will produce a future value at completion. Because of the uncertainties inherent in estimating construction costs, the market value of the completed project, the effects of governmental regulation on real property, and changes in demand, it is relatively difficult to evaluate accurately the total funds required to complete a project and the completed project loan- to- value ratio, which may cause actual results to vary significantly from those estimated. For these reasons, this type of lending also typically involves higher loan principal amounts and is often concentrated with a small number of builders. A downturn in housing, or the real estate market, could increase loan delinquencies, defaults and foreclosures, and significantly impair the value of our collateral and our ability to sell the collateral upon foreclosure. Some of our builders have more than one loan outstanding with us, and an adverse development with respect to one loan or one credit relationship may expose us to a significantly greater risk of loss. In addition, during the term of most of our construction loans, no payment from the borrower is required since the accumulated interest is added to the principal of the loan through an interest reserve. As a result, these loans often involve the disbursement of funds with repayment substantially dependent on the successful outcome of the project and the ability of the borrower to sell or lease the property or obtain permanent take- out financing, rather than the ability of the borrower or guarantor to repay principal and interest. If our appraisal of the value of a completed project proves to be overstated, we may have inadequate security for the repayment of the loan upon completion of construction of the project and may incur a loss. Because construction loans require active monitoring of the building process, including cost comparisons and on- site inspections, these loans are more difficult and costly to monitor. Increases in market rates of interest may have a more pronounced effect on construction loans by rapidly increasing the end-purchasers' borrowing costs, thereby reducing the overall demand for the project. Properties under construction are often difficult to sell and typically must be completed in order to be successfully sold, which also complicates the process of working out problem construction loans. This may require us to advance additional funds and / or contract with another builder to complete construction and assume the market risk of selling the project at a future market price, which may or may not enable us to fully recover unpaid loan funds and associated construction and liquidation costs. Our business may be adversely affected by credit risk associated with residential real estate. At December 31, ~~2022~~ **2023** , $ ~~396~~ **447** . ~~2~~ **8** million, or ~~25~~ **27** . ~~8~~ **0** % of our total loan portfolio, consisted of one- to **-** four ~~-~~ family mortgage loans and home equity loans secured by residential properties. Lending on residential property is sensitive to regional and local economic conditions that significantly impact the ability of borrowers to meet their loan payment obligations, making loss levels difficult to predict. Declines in residential real estate values securing these types of loans may increase the level of borrower defaults and losses above the recent charge- off experience on these loans. Jumbo one- to **-** four ~~-~~family residential loans that do not conform to secondary market mortgage requirements for our market areas would not be immediately saleable to Freddie Mac or other investors and may expose us to increased risk because of their larger balances. Further, a significant amount of our home equity lines of credit consist of loans in a subordinate lien position to a first lienholder. For home equity lines secured by a second mortgage, it is unlikely that we will be successful in recovering all or a portion of our loan balances in the event of default unless we repay the first mortgage loan and such repayment and the costs associated with a foreclosure are justified by the value of the property. For these reasons we may experience higher rates of delinquencies, default and losses on loans secured by junior liens. Repayment of our commercial business loans is often dependent on the cash flows of the borrower, which may be unpredictable, and the collateral securing these loans may fluctuate in value. At December 31, ~~2022~~ **2023** , we had $ ~~77~~ **112** . ~~0~~ **3** million, or ~~5~~ **6** . ~~0~~ **8** % of total loans, in commercial business loans. Commercial business lending involves risks that are different from those associated with residential and commercial real estate lending. Real estate lending is generally considered to be collateral- based lending with loan amounts based on the value of the collateral and predetermined loan to collateral ratios; liquidation of the underlying real estate collateral is the primary source of repayment in the event of borrower default. Our commercial business loans are primarily supported by the cash flow of the borrower and secondarily by the underlying collateral provided by the borrower. The borrowers' cash flows may be unpredictable, and the collateral securing these loans may fluctuate in value. Although commercial business loans are often collateralized by equipment, inventory, accounts receivable, or other business assets, the liquidation of collateral in the event of default is often an insufficient source of repayment. Factors affecting the value of this type of collateral include uncollectable accounts receivable and obsolete or limited use inventory, among others. Our allowance for ~~loan~~ **credit** losses **on loans** may prove to be insufficient to absorb losses in our loan portfolio. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the allowance for ~~loan~~ **credit** losses **on loans** , we review our loan portfolios, loss and delinquency trends, and economic conditions. If our assumptions are incorrect, our allowance for ~~loan~~ **credit** losses **on loans** may not be sufficient to cover incurred losses, resulting in additions to our allowance for ~~loan~~ **credit** losses **on loans** through the provision for **credit** losses on loans which is charged against income. Additionally, pursuant to our growth strategy, management recognizes that significant new loan growth, new loan products, new market areas, and the refinancing of existing loans, resulting in portfolios composed of unseasoned loans that may not perform in a historical or projected manner, may increase the risk that our allowance may be insufficient to absorb losses without significant additional provisions. Significant provisions to our allowance could materially decrease our net income. In addition, bank regulatory agencies periodically review our allowance for ~~loan~~ **credit** losses **on loans** and may require an increase in the provision for possible loan losses or the recognition of further loan charge- offs, based on judgments different than those of management. In addition, if charge- offs in future periods exceed the allowance for ~~loan~~ **credit** losses **on loans** , we will need additional provisions to replenish the allowance for ~~loan~~ **credit** losses **on loans** . Any additional provisions will result in a decrease in net income, and possibly capital, and may have a material adverse effect on our financial condition and results of operations. ~~In addition, the Financial Accounting Standards Board (" FASB") adopted Accounting Standard Update (" ASU") 2016- 13 which became effective on January 1, 2023. This standard, referred to as Current Expected Credit Loss (" CECL"), will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances for credit losses. In March 2022, FASB amended ASU 2016- 13 related to CECL implementation and guidance on Troubled Debt Restructurings (" TDRs") and vintage disclosures. These updates will change the current method of providing allowances for credit losses that are probable, which may require us to increase our allowance for loan losses, and may greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for credit losses. For more information on this ASU, see Note 1 of the Notes to Consolidated Financial Statements- Recently Issued Accounting Pronouncements contained in Item 8 of this report.~~ If our nonperforming assets increase, our earnings will be adversely affected. At December 31, ~~2022~~ **2023** , our nonperforming assets, which consist of nonaccrual loans, real estate owned and repossessed assets, were $ ~~1~~ **18. 6 million, or 0** . 8 ~~million, or 0. 1~~ % of total assets. Our nonperforming assets adversely affect our net income in various ways. If additional borrowers become delinquent and do not pay their loans and we are unable to successfully manage our nonperforming assets, our losses and troubled assets could increase significantly, which could have a material adverse effect on our financial condition and results of operations. Our securities portfolio may be negatively impacted by fluctuations in market value and interest rates. Factors beyond our control can significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. These factors include, but are not limited to, ratings agency actions, defaults or other adverse events affecting the issuer or the underlying collateral, if any, of the security, changes in market interest rates, and continued instability in the capital markets. Additionally, financial markets may be adversely affected by the current or anticipated impact of military conflict, including the current **wars in** ~~invasion by Russia of~~ Ukraine **and the Middle East** , terrorism, or other geopolitical events. **A need for additional liquidity may also require us to sell investment securities at depressed prices.** These factors, among others, could **result in an allowance for credit losses on investment securities** ~~cause other- than- temporary- impairment (" OTTI")~~ , realized and / or unrealized losses in future periods, and declines in other comprehensive income, which could materially affect our business, financial condition, and results of operations. Determining ~~OTTI~~ **an allowance for credit losses on investment securities** requires complex, subjective judgments about the future financial performance and liquidity of the security' s issuer and underlying collateral, if any, to assess the probability of receiving all contractual principal and interest payments due, and these estimates may differ significantly from actual future performance of the security. If our real estate owned is not properly valued or declines further in value, our earnings could be reduced. We obtain updated valuations in the form of appraisals and tax assessed values when a loan has been foreclosed and the property taken in as real estate owned and at certain other times during the asset’ s holding period. Our net book value of the loan at the time of foreclosure and thereafter is compared to the updated market value of the foreclosed property less estimated selling costs (fair value). A charge- off is recorded for any excess in the asset' s net book value over its fair value. If our valuation process is incorrect, or if property values decline, the fair value of our real estate owned may not be sufficient to recover our carrying value in such assets, resulting in the need for additional charge- offs. In addition, bank regulators periodically review our real estate owned and may require us to recognize further charge- offs. Significant charge- offs to our real estate owned could have a material adverse effect on our financial condition and results of operations. We operate in a highly competitive industry. We face substantial competition in all areas of our operations from a variety of different competitors, many of which are larger and may have more financial resources. These competitors primarily include national, regional and digital banks within the various markets in which we operate. We also face competition from many other types of financial institutions, including savings and loans, credit unions, mortgage banking finance companies, brokerage firms, insurance companies and other financial intermediaries. The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. ~~Also~~ **Further, clients may choose to conduct business with other market participants who engage in business or offer products in areas we deem speculative or risky, such as cryptocurrencies, non- fungible tokens, and other digital assets. Additionally** , technology has lowered barriers to entry and made it possible for nonbanks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. Competitors in these nonbank sectors may have fewer regulatory constraints, as well as lower cost structures. Additionally, due to their size, many competitors may be able to achieve economies of scale and, as a result, may offer a broader range of products and services as well as better pricing for those products and services than we can. Failure to perform in any of these areas could significantly weaken our competitive position, which could adversely affect our growth and profitability and result in a material adverse effect on our financial condition and results of operations. We are subject to certain risks in connection with our use of networks and technology systems. Our security measures may not be sufficient to mitigate the risk of a cyber- attack. Communications and information systems are essential to the conduct of our business, as we use such systems to manage our customer relationships, our general ledger and virtually all other aspects of our business. Our operations rely on the secure processing, storage, and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, the security of our computer systems, software, and networks may be vulnerable to breaches, unauthorized access, misuse, computer viruses, or other malicious code and cyber- attacks that could have a security impact. If one or more of these events occur, this could jeopardize our or our customers' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our operations or the operations of our customers or counterparties. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us. We could also suffer significant reputational damage. We support the ability of our customers to transact business through multiple automated methods. As such, we may be susceptible to fraud performed through these technologies. Security breaches in our internet banking activities could further expose us to possible liability and damage our reputation. Any compromise of our security also could deter customers from using our internet banking services that involve the transmission of confidential information. We rely on standard internet security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our systems from compromises or breaches of our security measures, which could result in significant legal liability, heightened regulatory scrutiny or fines, violations of consumer protection and privacy laws, and significant damage to our reputation and our business. Our security measures may not protect us from systems failures or interruptions. While we have established policies and procedures to prevent or limit the impact of systems failures and interruptions, there can be no assurance that such events will not occur or that they will be adequately addressed if they do. In addition, we outsource certain aspects of our data processing and other operational functions to certain third- party providers. If our third- party providers encounter difficulties, or if we have difficulty in communicating with them, our ability to adequately process and account for transactions could be affected, and our business operations could be adversely impacted. Threats to information security also exist in the processing of customer and consumer information through various ~~other~~ **third- party** vendors and their personnel. The occurrence of any failures or interruptions may require us to identify alternative sources of such services, and we cannot assure that we would be able to negotiate terms that are as favorable to us or obtain services with similar functionality as found in our existing systems without the need to expend substantial resources, if at all. Further, the occurrence of any systems failure or interruption could damage our reputation and result in a loss of customers and business, could subject us to additional regulatory scrutiny, or could expose us to legal liability. Any of these occurrences could have a material adverse effect on our financial condition and results of operations. Interest Rates, Operations and Risk Management We are subject to interest rate risk. Our earnings and cash flows are largely dependent on our net interest income. Interest rates are highly sensitive to many factors beyond our control, including general economic conditions and policies of various governmental and regulatory agencies, particularly the Federal Reserve. ~~While~~ **The Federal Reserve slowed its increases to** the federal funds target rate **in** ~~remained at or near historical lows during 2020~~ **2023** ~~and 2021 as part of the fiscal response to the COVID- 19 pandemic~~ , **with** the **most recent** ~~Federal Reserve increased the federal funds target rate seven times in 2022 for a total annual~~ increase **occurring in July 2023** ~~of 425 basis points. Furthermore, the Federal Reserve has communicated that it anticipates ongoing increases until inflationary pressures subside~~ . When the Federal Reserve Board increases the Fed Funds rate, overall interest rates will likely rise, which may negatively impact housing markets by reducing refinancing activity and new home purchases. A rising **or elevated** interest rate environment may also adversely affect the U. S. economy and, as a result, our business as a whole **. The Federal Reserve has communicated that the economic outlook continues to be uncertain, and while it has stated that rates may decrease later in 2024, there can be no assurance of the timing or amount of any future rate adjustments. Further, there can be no assurance regarding any forecasts or predictions about**

the effect that any future rate adjustment may have on our results of operations . Further changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and investments and the amount of interest we pay on deposits and borrowings, but these changes could also affect (i) our ability to originate and / or sell mortgage and SBA loans **;** (ii) the fair value of our financial assets and liabilities, which could negatively impact shareholders' equity, and our ability to realize gains from sales of such assets; (iii) our ability to obtain and retain deposits in competition with other available investment alternatives; (iv) the ability of our borrowers to repay adjustable or variable rate loans; and (v) the average duration of our mortgage- backed securities portfolio and other interest- earning assets. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings. Additional changes in interest rates could also have a negative impact on our results of operations by reducing the ability of borrowers to repay their current loan obligations or by reducing our margins and profitability. Our net interest margin is the net interest income divided by average interest- earning assets. Further changes in interest rates ~~–~~**,** up or down ~~–~~**,** could adversely affect our net interest margin and, as a result, our net interest income. Although the yield we earn on our assets and our funding costs tend to move in the same direction in response to changes in interest rates, one can rise or fall faster than the other, causing our net interest margin to expand or contract. Our liabilities tend to be shorter in duration than our assets, so they may adjust faster in response to changes in interest rates. As a result, when interest rates rise, our funding costs may rise faster than the yield we earn on our assets, causing our net interest margin to contract until the yields on interest- earning assets catch up. Changes in the slope of the" yield curve", or the spread between short- term and long- term interest rates, could also reduce our net interest margin. Normally, the yield curve is upward sloping, meaning short- term rates are lower than long- term rates. Because our liabilities tend to be shorter in duration than our assets, when the yield curve flattens or even inverts, ~~as at the end of 2022,~~ we could experience pressure on our net interest margin as our cost of funds increases relative to the yield we can earn on our assets. A sustained increase in market interest rates could adversely affect our earnings. As a result of the exceptionally low interest rate environment ~~for~~ **in** the ~~past few~~ years **prior to 2022** , ~~an increasing~~ **a high** percentage of our deposits **were** ~~have been~~ composed of deposits bearing no or a relatively low rate of interest and having a shorter duration than our assets. We ~~would~~ **will likely** incur a higher cost of funds to retain these deposits in ~~this rising~~ **the current elevated** interest rate environment. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income, and therefore earnings, would be adversely affected. Changes in interest rates also affect the value of our interest- earning assets, including our securities portfolio. Generally, the fair value of fixed- rate securities fluctuates inversely with changes in interest rates. Unrealized gains and losses on securities available for sale are reported as a separate component of equity, net of tax. Decreases in the fair value of securities available for sale resulting from increases in interest rates could have an adverse effect on our shareholders' equity. Although management believes it has implemented effective asset and liability management strategies to reduce the potential effects of changes in interest rates on our results of operations, any substantial, unexpected or prolonged change in market interest rates could have a material adverse effect on our financial condition and results of operations. Also, our interest rate risk modeling techniques and assumptions likely will not fully predict or capture the impact of actual interest rate changes on our balance sheet. See Item 7." Management' s Discussion and Analysis of Financial Condition and Results of Operations – Asset and Liability Management and Market Risk," ~~of~~ **in** this Form 10- K for additional information. **Decreased volumes** ~~Changes in the method of determining the LIBOR or other reference rates may adversely impact the value of loans receivable~~ and **lower gains on sales of loans** ~~other financial instruments we hold that are linked to LIBOR or other reference rates in ways that are difficult to predict and~~ could adversely impact our ~~financial condition or results of operations. In July 2017, the United Kingdom Financial Conduct Authority announced the potential replacement of the London Interbank Offered Rate (" LIBOR") at the end of 2021. LIBOR is used extensively in the U. S. and globally as a" benchmark" or" reference rate" for various commercial and financial contracts. In response, the Alternative Reference Rates Committee (" ARRC "), made up of financial and capital market institutions, was convened to address the replacement of LIBOR in the U. S. The ARRC identified a potential successor to LIBOR in the Term Secured Overnight Financing Rate (" TSOFR ") and has crafted a plan to facilitate the transition. Our subordinated debt issued in March 2021 provides for application the TSOFR rate to determine the interest that will be payable on the Notes beginning in March 2026. In March 2022, the Adjustable Interest Rate (LIBOR) Act (the " LIBOR Act ") was enacted, providing that LIBOR- based contracts that lack practicable replacement benchmarks will automatically transition to the applicable reference rates recommended by the Federal Reserve. In December 2022, the Federal Reserve issued a Final Rule establishing benchmark replacements based on TSOFR. However, the ICE Benchmark Administration (" IBA "), the authorized and regulated administrator of LIBOR, expects to continue publishing some LIBOR tenors until June 2023 and may be compelled to continue publishing other tenors under a different methodology after the Financial Conduct Authority (" FCA ") completes a consultation and makes a final determination on the matter (expected in 2023). Despite the progress made through the LIBOR Act and the Federal Reserve' s Final Rule, it is impossible to predict the effect of any such alternatives on the value of LIBOR- based securities, variable rate loans, and other securities or financial arrangements. The transition to a new reference rate requires changes to contracts, risk and pricing models, valuation tools, systems, product design and hedging strategies. It is not currently possible to determine whether, or to what extent, the replacement of LIBOR will impact the value of any loans and other financial obligations or extensions of credit we hold or that are due to us, that are linked to LIBOR or other reference rates, or whether, or to what extent, such changes may impact our financial condition or results of operations. Decreased volumes and lower gains on sales of loans could adversely impact our~~ noninterest income. We originate and sell one- to **-** four ~~–~~family mortgage loans. Our mortgage banking income is a significant portion of our noninterest income. We generate gains on the sale of one- to **-** four ~~–~~family mortgage loans pursuant to programs currently offered by Freddie Mac and other secondary market investors. Any future changes in their purchase programs, our eligibility to participate in such programs, the criteria for loans to be accepted or laws that significantly affect the activity of such entities could, in turn, materially adversely affect our results of operations. Further, in a rising or higher interest rate environment, our originations of mortgage loans may decrease, resulting in fewer loans that are available to be sold to investors. This would result in a decrease in mortgage banking revenues and a corresponding decrease in noninterest income. In addition, our results of operations are affected by the amount of noninterest expense associated with mortgage banking activities, such as salaries and employee benefits, occupancy, equipment and data processing expense and other operating costs. During periods of reduced loan demand, our results of operations may be adversely affected to the extent that we are unable to reduce expenses commensurate with the decline in loan originations. In addition, although we sell loans into the secondary market without recourse, we are required to give customary representations and warranties about the loans to the buyers. If we breach those representations and warranties, the buyers may require us to repurchase the loans and we may incur a loss on the repurchase. A portion of our loan portfolio is serviced by third parties, which may limit our ability to foreclose on or repossess such loans. At December 31, ~~2022~~ **2023** , $ ~~83~~ **105** . 4 million of our consumer, $ **38** ~~25. 3 million of our one- to four- family, and $ 18~~ . 1 million of our commercial real estate **, and $ 19. 2 million of our one- to- four family** loan portfolios were serviced by third parties. When a loan goes into default, it is the responsibility of the third- party servicer to enforce the borrower' s obligation to repay the outstanding indebtedness. We are reliant on the servicer to bring the loan current, enter into a satisfactory loan modification or foreclose on the property on behalf of First Fed. We must comply with any loan modification entered into by the servicer even if we would not otherwise agree to the modified terms, which may result in a reduction in our interest income due to the loan modification. Delays in foreclosing on property, whether caused by restrictions under state or federal law or the failure of a third- party servicer to timely pursue foreclosure action, may increase our potential loss on such property, due to factors such as lack of maintenance, unpaid property taxes and adverse changes in market conditions. These delays may adversely affect our ability to limit our credit losses. Regulatory Matters Our lending limit may restrict our growth. Washington law provides that Washington chartered commercial banks are subject to loans- to- one- borrower restrictions, which generally restrict total loans and extensions of credit by a bank to 20 % of its unimpaired capital and surplus. As a result, under Washington law, First Fed would be limited to loans to one borrower of $ 46. ~~3~~ **0** million at December 31, ~~2022~~ **2023** . Under its current policy, First Fed has elected to restrict its loans to one borrower to no more than 60 % of the Bank' s lending limit, which is adjusted quarterly and was $ 34. ~~7~~ **5** million at December 31, ~~2022~~ **2023** , unless specifically approved by the Senior Loan Committee as an exception to policy. This amount is significantly less than that of many of our competitors and may discourage potential commercial borrowers who have credit needs in excess of our loans to one borrower lending limit from doing business with us. Our loans to one borrower restriction also impacts the efficiency of our commercial lending operation because it lowers our average loan size, which means we have to generate a higher number of transactions to achieve the same portfolio volume. We can accommodate larger loans by selling participations in those loans to other financial partners, but this strategy is not the most efficient or always available. We may not be able to attract or maintain clients seeking larger loans or may not be able to sell participations in these loans on terms we consider favorable. We operate in a highly regulated environment and may be adversely affected by changes in laws and regulations **and the impact of consent orders to which we are subject** . We are subject to extensive examination, supervision and comprehensive regulation by the Federal Reserve, the FDIC as insurer of our deposits, and by the DFI. First Northwest Bancorp is subject to regulation and supervision by the Federal Reserve (as a financial holding company) and regulation by the State of Washington (as a Washington corporation). The Bank is subject to regulation and supervision by the FDIC and the DFI. Such regulation and supervision govern the activities in which we may engage, primarily for the protection of depositors and the Deposit Insurance Fund. These regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the ability to impose restrictions on an institution' s operations, require additional capital, reclassify assets, determine the adequacy of an institution' s allowance for ~~loan~~ **credit** losses **on loans** and determine the level of deposit insurance premiums assessed. Any future changes to the laws, rules and regulations applicable to us could make compliance more difficult and expensive, or otherwise adversely affect our business, financial condition or prospects **. On November 21, 2023, the Bank entered into a consent order (" Order") with the FDIC, the Bank' s primary regulator. The Order, which will remain effective until modified, suspended or terminated by the FDIC, requires the Board and senior management to: • Review, revise, develop, and / or implement, as necessary, a sound risk- based compliance management system, including a written compliance program, policies, and training designed to effect compliance with all applicable consumer protection laws, a consumer complaint monitoring process, and a monitoring program designed to detect and correct compliance weaknesses; • Hold Bank management accountable for failing to adhere to consumer protection laws and the Bank' s policies and procedures; • Review and analyze the resources, management, and staffing necessary (i) for compliance with all consumer protection laws, (ii) to manage and supervise the Bank' s compliance program, (iii) to provide sufficient oversight over third- party relationships and products and services offered by or through third- party relationships, and (iv) to appropriately address certain prior violations and compliance issues; and • Review, revise, develop, and / or implement, as necessary, effective independent audit coverage of the Bank' s compliance program** . We are also subject to tax, accounting, securities, insurance, monetary laws and regulations, rules, standards, policies, and interpretations that control the methods by which financial institutions conduct business. These may change significantly over time, which could materially impact our business and have a significant adverse effect on our cost of regulatory compliance and results of operations. Further, changes in accounting standards and their interpretation may materially impact how we report, potentially retroactively, our financial condition and results of operations. Changes in federal policy and at regulatory agencies are expected to occur over time through policy and personnel changes, which could lead to changes involving the level of oversight and focus on the financial services industry. The nature, timing, and economic and political effects of potential changes to the current legal and regulatory framework affecting financial institutions remain highly uncertain. If changes to laws, rules and / or regulations applicable to us are made, such changes could offset the otherwise anticipated increase in operating and compliance costs (included in noninterest expense); however, no assurance can be given as to whether such changes will occur or what may result from such changes. The CFPB, which was created under the Dodd-Frank Act, has issued, and continues to issue, rules related to consumer protection, including The Truth in Lending Act and the Real Estate Settlement Procedures Act Integrated Disclosure (TRID), which combines certain disclosures that consumers receive in connection with applying for and closing a mortgage loan. These CFPB rules, including rules generally prohibiting creditors from extending mortgage loans without regard for the consumer' s ability to repay, may adversely affect the volume of mortgage loans that we underwrite and subject us to increased potential liabilities related to such residential loan origination activities. The CFPB has adopted a number of additional requirements and issued additional guidance, including with respect to indirect auto lending, appraisals, escrow accounts and servicing, each of which may entail increased compliance costs. General Risk Factors We are dependent on key personnel and the loss of one or more of those key persons may materially and adversely affect our prospects. We rely heavily on the efforts and abilities of our executive officers, and certain other key management personnel, which make up our management team. The loss of the services of any of our current management team could have a material adverse impact on our operations. The ability to attract, retain and season replacements to our management team presents risks to executing our business plan. Changes in our current management team and their responsibilities may be disruptive to our business and operations and could have a material adverse effect on our business, financial condition, and results of operations. While we believe that our relationship with our management team is good, we cannot guarantee that all members of our management team will remain with our organization. Our consideration of whole bank, branch acquisitions, or fintech partnerships in the future may expose us to financial, execution and operational risks that could adversely affect us. We may evaluate supplementing organic growth by acquiring other financial institutions or their businesses that we believe will help us fulfill our strategic objectives and enhance our earnings. There are risks associated with this strategy, however, including the following: • We may be exposed to potential asset quality issues or unknown or contingent liabilities of the financial institutions, businesses, assets and liabilities we acquire. If these issues or liabilities exceed our estimates, our results of operations and financial condition may be materially negatively affected; • The acquisition of other entities generally requires integration of systems, procedures and personnel of the acquired entity into our company to make the transaction economically successful. This integration process is complicated and time consuming and can also be disruptive to the customers of the acquired business. If the integration process is not conducted successfully, we may not realize the anticipated economic benefits of particular acquisitions within the expected time frame, and we may lose customers or employees of the acquired business. We may also experience greater than anticipated customer losses even if the integration process is successful; ~~and~~ • To finance a future acquisition, we may borrow funds, thereby increasing our leverage and diminishing our liquidity, or raise additional capital, which could dilute the interests of our existing shareholders **; and • If market or regulatory conditions change, we may be unable to successfully compete for, complete, or integrate potential future acquisitions as anticipated or at all. Downturns in the stock market and the market price of our stock, changes in our capital position, heightened regulatory scrutiny, and changes in our regulatory standing could each have a negative impact on our ability to complete future acquisitions** . Over the past seven years, we have opened four new full- service branches and two business centers. We also acquired a branch from another financial institution in 2021. We may continue to open or purchase new branches and lending centers, and the success of our expansion strategy into new markets is contingent upon numerous factors, such as our ability to select suitable locations, assess each market' s competitive environment, secure managerial resources, hire and retain qualified personnel and implement effective marketing strategies. The opening of new offices may not increase the volume of our loans and deposits as quickly or to the degree that we projected and opening new offices will increase our operating expenses. The cost of opening additional de novo branches and lending centers is uncertain, and projected timelines and estimated dollar amounts involved in opening new offices could differ significantly from actual results. In addition, we may not successfully manage the costs and implementation risks associated with our branching strategy. Accordingly, any new branch or lending center may negatively impact our earnings for some period of time until the office reaches certain economies of scale, and there is a risk that our new offices will not be successful even after they have been established. We may also expand our digital footprint through partnerships with and investments in fintech companies. The new technology and start- up companies we invest in may not be as successful as anticipated or may fail, resulting a total loss of our related investment.