CENTRAL VALLEY COMMUNITY BANCORP
Form 10-K
March 21, 2012
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011
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: 000-31977
CENTRAL VALLEY COMMUNITY BANCORP
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| CALIFORNIA | 77-0539125 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 7100 N. Financial Dr., Suite 101, Fresno, CA | 93720 |
| (Address of principal executive offices) | (Zip Code) |

559-298-1775
(Registrant's telephone number, including area code)
[None]
(Former name, former address and former fiscal year, if changed since last report)
Securities registered pursuant to Section 12(b) of the Act:

| | |
|---|---|
| None | NASDAQ Capital Market |
| [Common Stock, $ par value per share] | [EXCHANGE] |

Securities registered pursuant to Section 12(g) of the Act: Common Stock, No Par Value
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No x
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of June 30, 2011, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $49,577,000 based on the price at which the stock was last sold on June 30, 2011.

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

| Common Stock, No Par Value | Outstanding at March 14, 2012 | |
|---|---|---|
| [Common Stock, No par value per share] | 9,591,316 | shares |

DOCUMENTS INCORPORATED BY REFERENCE

| Document | Parts into Which Incorporated |
|---|---|
| Proxy Statement for the Annual Meeting of Shareholders to be held May 16, 2012 (Proxy Statement) | Part III |

Table of Contents

TABLE OF CONTENTS


| | | |
|---|---|---|
| ITEM 1 - | DESCRIPTION OF BUSINESS | 1 |
| ITEM 1A - | RISK FACTORS | 24 |
| ITEM 2 - | DESCRIPTION OF PROPERTY | 31 |
| ITEM 3 - | LEGAL PROCEEDINGS | 31 |
| ITEM 4 - | MINE SAFETY DISCLOSURES | 32 |
| ITEM 5 - | MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES | 32 |
| ITEM 6 - | SELECTED FINANCIAL DATA | 33 |
| ITEM 7- | MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION | 34 |
| ITEM 7A- | QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK | 59 |
| ITEM 8 - | FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA | 62 |
| ITEM 9 - | CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE | 113 |
| ITEM 9A - | CONTROLS AND PROCEDURES | 113 |
| ITEM 9B- | OTHER INFORMATION | 114 |
| ITEM 10 - | DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT | 114 |
| ITEM 11 - | EXECUTIVE COMPENSATION | 114 |
| ITEM 12 - | SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS | 114 |
| ITEM 13 - | CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS | 114 |
| ITEM 14 - | PRINCIPAL ACCOUNTING FEES AND SERVICES | 114 |
| ITEM 15 - | EXHIBITS, FINANCIAL STATEMENT SCHEDULES | 114 |
| SIGNATURES | | 115 |

ADDITIONAL INFORMATION; INQUIRIES

Under the Securities Exchange Act of 1934, Sections 13 and 15(d), periodic and current reports must be filed with the SEC. We electronically file the following reports with the SEC:

•Form 10-K — Annual Report;

•Form 10-Q — Quarterly Report;

•Form 8-K — Report of Unscheduled Material Events; and

•Form DEF 14A — Proxy Statement.

We may file additional forms. The SEC maintains an Internet site, www.sec.gov, in which all forms filed electronically may be accessed. Additional shareholder information regarding the Company and our Directors is available on our website: www.cvcb.com. None of the information on or hyperlinked from our website is incorporated into this Report.

Copies of the annual report on Form 10-K for the year ended December 31, 2011 may be obtained without charge upon written request to Dave Kinross, Chief Financial Officer, at the Company's administrative offices, 7100 N. Financial Dr., Suite 101, Fresno, CA 93720.

Inquiries regarding Central Valley Community Bancorp's accounting, internal controls or auditing concerns should be directed to Steven D. McDonald, chairman of the Board of Directors' Audit Committee, at steve.mcdonald@cvcb.com or anonymously at www.ethicspoint.com or EthicsPoint, Inc. at 1-866-294-9588.

General inquiries about Central Valley Community Bancorp or Central Valley Community Bank should be directed to Cathy Ponte, Assistant Corporate Secretary at 1-800-298-1775.

PART I

ITEM 1 - DESCRIPTION OF BUSINESS

General

Central Valley Community Bancorp (the Company) was incorporated on February 7, 2000 as a California corporation, for the purpose of becoming the holding company for Central Valley Community Bank (the Bank), formerly known as Clovis Community Bank, a California state chartered bank, through a corporate reorganization. In the reorganization, the Bank became the wholly-owned subsidiary of the Company, and the shareholders of the Bank became the shareholders of the Company. The Company is registered as a bank holding company under the Bank Holding Company Act of 1956, as amended (the BHC Act), and is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the Board of Governors).

At December 31, 2011, we had one banking subsidiary, the Bank. Our principal business is to provide, through our banking subsidiary, financial services in our primary market area in California. We serve Fresno County, Madera County, Sacramento County, San Joaquin County, Merced County, and Stanislaus County and their surrounding areas through the Bank. We do not currently conduct any operations other than through the Bank. Unless the context otherwise requires, references to us refer to the Company and the Bank on a consolidated basis. At December 31, 2011, we had consolidated total assets of approximately $849,023,000. See Items 7 and 8, Management's Discussion

and Analysis or Plan of Operation and Financial Statements.

After the close of business on November 12, 2008, Service 1st Bancorp (Service 1st) was merged with and into the Company, and Service 1st Bank (S1 Bank) was merged with and into the Bank. S1 Bank had three branches in Stockton, Tracy, and Lodi which continue to be operated by the Bank.

On August 18, 2011, the Company entered into a Securities Purchase Agreement with the Small Business Lending Fund of the United States Department of the Treasury (the Treasury), under which the Company issued 7,000 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series C (the Preferred Shares) to the Treasury for an aggregate purchase price of $7,000,000. Simultaneously, the Company agreed with Treasury under a Letter Agreement to redeem, for an aggregate price of

Table of Contents

$7,000,000, the 7,000 shares of the Company's Series A Fixed Rate Cumulative Preferred Stock (Series A Stock)originally issued pursuant to the Treasury's Capital Purchase Program (CPP) in 2009. The redemption of the Series A Stock resulted in an acceleration of the remaining discount booked at the time of the CPP transaction.

In connection with the repurchase of the Series A Stock, the Company also notified the Treasury of the Company's intent to repurchase the warrant (the Warrant) to purchase 79,037 shares of the Company's common stock that was originally issued to Treasury in connection with the CPP transaction. On September 28, 2011, the Company completed the repurchase of the Warrant for total consideration of $185,000.

The Preferred Shares will qualify as Tier 1 capital and will pay non-cumulative dividends at an initial rate of 5% per annum. The dividend rate may vary, but not exceed 5%, with any reductions in interest rate to be calculated by reference to increases over a baseline amount in the Company's small business lending activities. The Preferred Stock may be redeemed by the Company, or by Treasury in the event that it is statutorily prevented from continuing to hold the Preferred Stock.

The Preferred Stock was issued in a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended.

The Series C Preferred Stock is non-voting, other than class voting rights on (i) any authorization or issuance of shares ranking senior to the Series C Preferred Stock, (ii) any amendment to the rights of the Series C Preferred Stock, or (iii) any merger, exchange or similar transaction which would adversely affect the rights of the Series C Preferred Stock.

If dividends on the Series C Preferred Stock are not paid in full for six dividend periods, whether or not consecutive, the holders of the Series C Preferred Stock will have the right to elect 2 directors. The right to elect directors will end when full dividends have been paid for four consecutive dividend periods. The Company has paid all scheduled dividend payments as of December 31, 2011.

On December 23, 2009, the Company entered into Stock Purchase Agreements (Agreements) with a limited number of accredited investors (collectively, the Purchasers) to sell to the Purchasers a total of 1,264,952 shares of common stock, (Common Stock) at $5.25 per share and 1,359 shares of non-voting Series B Convertible Adjustable Rate Non-Cumulative Perpetual Preferred Stock (Series B Preferred Stock) at $1,000 per share, for an aggregate gross purchase price of $8,000,000 (the Offering) offset by issuance costs totaling $242,000.

The Series B Preferred Stock was eligible to receive a semi-annual non-cumulative preferred dividend with an initial annualized coupon of 10%, payable at the end of the first six months the shares are outstanding. The annual dividend rate would have increased to 15% for the second six month period and 20% for each six month period thereafter. Dividends could not be paid on any other class or series of the Company's stock unless dividends are currently paid on the Preferred Stock in any period.

In May 2010, the shareholders of the Company approved an amendment to the Company's governing instruments to create a series of non-voting common stock. In June 2010, the Company exercised its option to require the Purchasers to exchange 1,359 shares of Series B Preferred Stock for 258,862 shares of non-voting common stock. In August, 2011, the Company agreed to exchange 258,862 shares of the Company's non-voting common stock for 258,862 shares of the Company's voting common stock. The issuance of voting common stock was conducted in a privately negotiated transaction exempt from registration pursuant to Sections 3(a)(9) and 4(2) of the Securities Act of 1933, as amended.

The Company had no stock repurchase plans in place during 2011, 2010 or 2009.

As of March 9, 2012, we had a total of 231 employees and 219 full time equivalent employees, including the employees of the Bank.

The Bank

The Bank was organized in 1979 and commenced business as a California state chartered bank in 1980. The deposits of the Bank are insured by the Federal Deposit Insurance Corporation (the FDIC) up to applicable limits. The Bank is not a member of the Federal Reserve System

The Bank operates 17 full-service banking offices in Clovis, Fresno, Kerman, Lodi, Madera, Merced, Modesto, Oakhurst, Prather, Sacramento, Stockton, and Tracy. The Oakhurst and Madera branches were added through the Bank of Madera County merger in 2005. The Tracy, Stockton and Lodi offices were added through the merger with Service 1st Bank in

November of 2008. The Bank has a Real Estate Division, an Agribusiness Center and an SBA Lending Division in Fresno. All real estate related transactions are conducted and processed through the Real Estate Division, including interim construction loans for single family residences and commercial buildings. We offer permanent single family residential loans through our mortgage broker services. Our total market share of deposits in Fresno and Madera counties increased to 4.55% in 2011 compared to 4.49% in 2010 based on FDIC deposit market share information published as of June 30, 2011.

The Bank of Madera County (BMC) was merged with and into the Bank on January 1, 2005. The transaction was a combination of cash and stock and was accounted for under the purchase method of accounting. BMC had two branches in Madera County which continue to be operated by the Bank.

In November of 2008, The Company acquired Service 1st and its banking subsidiary, S1 Bank, adding three branches located in Tracy, Stockton and Lodi, California.

In 2009, we opened a new full service office in Merced, California and relocated our Oakhurst office to a new smaller facility in a more desirable location.

In 2010, the Company expanded the existing Modesto loan production office opened in 2007, to a larger full-service branch.

Branch expansions provide the Company with opportunities to expand its loan and deposit base; however, based on past experience, management expects these new offices will initially have a negative impact on earnings until the volume of business grows to cover fixed overhead expenses. The Bank anticipates additional future branch openings to meet the growing service needs of its customers, although none are planned during 2012.

The Bank established an interest in Central Valley Community Insurance Services, LLC at the end of 2006. The purpose of this entity is to market health, commercial property and casualty insurance products and services primarily to business customers.

The Bank conducts a commercial banking business, which includes accepting demand, savings and time deposits and making commercial, real estate and consumer loans. It also provides domestic and international wire transfer services and provides safe deposit boxes and other customary banking services. The Bank also has offered Internet Banking since 2000. Internet Banking consists of inquiry, account status, bill paying, account transfers, and cash management. The Bank does not offer trust services or international banking services and does not currently plan to do so in the near future.

Since August of 1995 the Bank has been a party to an agreement with Investment Centers of America, pursuant to which Investment Centers of America provides Bank customers with access to investment services. In connection with entering into this agreement, the Bank adopted a policy intended to comply with FDIC Regulation Section 337.4, which outlines the guidelines under which an insured non-member bank may be affiliated with a company that directly engages in the sale, distribution, or underwriting of stocks, bonds, debentures, notes, or other securities.

The Bank’s operating policy since its inception has emphasized serving the banking needs of individuals and the business and professional communities in the central valley area of California. At December 31, 2011, we had total loans of $427,395,000. Total commercial and industrial loans outstanding were $78,089,000; total agricultural land and production loans outstanding were $29,958,000, total real estate construction and other land loans outstanding were $33,047,000; total other real estate loans outstanding were $226,194,000, total equity loans and lines of credit were $51,106,000 and total consumer installment loans outstanding were $9,765,000. We accept real estate, listed securities, savings and time deposits, automobiles, inventory, machinery and equipment as collateral for loans.

No individual or single group of related accounts is considered material in relation to the Bank's assets or deposits, or in relation to the overall business of the Company. However, at December 31, 2011 approximately 72.4% of our loan portfolio held for investment consisted of real estate-related loans, including construction loans, equity loans and lines of credit and commercial loans secured by real estate and 25.3% consisted of commercial loans. See Item 7 — Management's Discussion and Analysis of Financial Condition and Results of Operations. We believe that these concentrations are mitigated by the diversification of our loan portfolio among commercial, real estate and consumer loans. In addition, our business activities currently are mainly concentrated in Fresno, Madera and San Joaquin County, California. Consequently, our results of operations and financial condition are dependent upon the general trends in this part of the California economy and, in particular, the residential and commercial real estate markets. In addition, our concentration of operations in this area of California exposes us to greater risk than other banking companies with a wider geographic base in the event of catastrophes, such as earthquakes, fires and floods in this region or as a result of energy shortages in California.

Table of Contents

Our deposits are attracted from individual and commercial customers.  A material portion of our deposits have not been obtained from a single person or a few persons, the loss of any one or more of which would have a material adverse effect on our business.

In order to attract loan and deposit business from individuals and small businesses, we maintain the following lobby hours at our branches:

| Branch | Monday — Thursday | Friday | Saturday |
|---|---|---|---|
| | 9:00 a.m. to 4:00 p.m. | 9:00 a.m. to 6:00 p.m. | |
| Clovis Main | Drive Up 8:00 a.m. to 5:30 p.m. | Drive Up 8:00 a.m. to 6:00 p.m. | None |
| | 9:00 a.m. to 4:00 p.m. | 9:00 a.m. to 5:00 p.m. | |
| Fresno Downtown | Walk-up window 8:00 a.m. to 9:00 a.m. | Walk-up window 8:00 a.m. to 9:00 a.m. | None |
| Fig Garden Village | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | 10:00 a.m. to 2:00 p.m. |
| | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | 9:00 a.m. to 2:00 p.m. |
| Herndon & Fowler | Drive Up 8:30 a.m. to 5:30 p.m. | Drive Up 8:30 a.m. to 6:00 p.m. | Drive Up 9:00 a.m. to 2:00 p.m. |
| | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | 10:00 a.m. to 2:00 p.m. |
| River Park | Drive Up 9:00 a.m. to 5:30 p.m. | Drive Up 9:00 a.m. to 6:00 p.m. | Drive Up 10:00 a.m. to 2:00 p.m. |
| | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | |
| Sunnyside | Drive Up 8:00 a.m. to 5:00 p.m. | Drive Up 8:00 a.m. to 6:00 p.m. | None |
| | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | |
| Kerman | Drive Up 8:30 a.m. to 5:00 p.m. | Drive Up 8:30 a.m. to 6:00 p.m. | None |
| Lodi | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | None |
| Madera | 8:30 a.m. to 5:00 p.m. | 8:30 a.m. to 6:00 p.m. | None |
| Merced | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | None |
| | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | |
| Modesto | Drive Up 8:30 a.m. to 5:00 p.m. | Drive Up 8:30 a.m. to 6:00 p.m. | None |
| Oakhurst | 8:30 a.m. to 5:00 p.m. | 8:30 a.m. to 6:00 p.m. | None |
| Prather (Foothill office) | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | 9:00 a.m. to 1:00 p.m. |
| Sacramento Private Banking | 9:00 a.m. to 4:00 p.m. | 9:00 a.m. to 4:00 p.m. | None |
| Stockton | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | None |
| Tracy | 9:00 a.m. to 5:00 p.m. | 9:00 a.m. to 6:00 p.m. | None |
| Financial Drive | 8:00 a.m. to 5:00 p.m. | 8:00 a.m. to 5:00 p.m. | None |

Automated teller machines operate at 16 branch locations. All operate 24 hours per day, seven days per week. No automated teller machines are currently located at the Sacramento office. Our Real Estate, Small Business Administration (SBA) Departments and Agribusiness office maintain business hours of 8:00 A.M. to 5:00 P.M., Monday through Friday, and extended hours are available upon customer request.

To compete effectively, we rely substantially on local promotional activity, personal contacts by our officers, directors and employees, referrals by our shareholders, extended hours, personalized service and our reputation in the communities we serve.

In Fresno and Madera Counties, in addition to our 12 full-service branch locations, serving the Bank's primary service

Table of Contents

areas, as of December 31, 2011 there were 163 operating banking and credit union offices in our primary service area, which consists of the cities of Clovis, Fresno, Kerman, Oakhurst, Madera, and Prather, California. Prather does not contain any banking offices other than our office. The June 2011 FDIC Summary of Deposits report indicated the Company had 4.29% of the total deposits held by all depositories in Fresno County and 7.27% in Madera County. In San Joaquin County, in addition to our three full service branch locations acquired from Service 1st, as of December 31, 2011 there were 118 operating banking and credit union offices. The FDIC Summary of Deposits as of June 2011 report indicated the Company had 1.63% of total deposits held by all depositories in San Joaquin County. In Sacramento County, in addition to our one branch, as of December 31, 2011 there were 229 operating banking and credit union offices in our primary service area. In Stanislaus County, in addition to our one branch, there were 99 operating banking and credit union offices in our primary service area. Business activity in our primary service area is oriented toward light industry, small business and agriculture.

The banking business in California generally, and our primary service area specifically, is highly competitive with respect to both loans and deposits, and is dominated by a relatively small number of major banks with many offices operating over a wide geographic area. Among the advantages such major banks have over us is their ability to finance wide-ranging advertising campaigns and to allocate their investment assets, including loans, to regions of higher yield and demand. Major banks offer certain services such as international banking and trust services which we do not offer directly but which we usually can offer indirectly through correspondent institutions. In addition, by virtue of their greater total capitalization, such banks have substantially higher lending limits than we do. Legal lending limits to an individual customer are limited to a percentage of our total capital accounts. As of December 31, 2011, the Bank’s legal lending limits to individual customers were $13,203,000 for unsecured loans and $22,005,000 for unsecured and secured loans combined. For borrowers desiring loans in excess of the Bank’s lending limits, the Bank makes, and may in the future make, such loans on a participation basis with other community banks taking the amount of loans in excess of the Bank’s lending limits. In other cases, the Bank may refer such borrowers to larger banks or other lending institutions.

Other entities, both governmental and in private industry, seeking to raise capital through the issuance and sale of debt or equity securities also provide competition for us in the acquisition of deposits. Banks also compete with money market funds and other money market instruments, which are not subject to interest rate ceilings. In recent years, increased competition has also developed from specialized finance and non-finance companies that offer wholesale finance, credit card, and other consumer finance services, including on-line banking services and personal finance software. Competition for deposit and loan products remains strong, from both banking and non-banking firms, and affects the rates of those products as well as the terms on which they are offered to customers.

Technological innovation continues to contribute to greater competition in domestic and international financial services markets. Technological innovation has, for example, made it possible for non-depository institutions to offer customers automated transfer payment services that previously have been traditional banking products. In addition, customers now expect a choice of several delivery systems and channels, including telephone, mail, home computer, ATMs, remote deposit, self-service branches, and in-store branches.

Mergers between financial institutions have placed additional pressure on banks to streamline their operations, reduce expenses, and increase revenues to remain competitive. In addition, competition has intensified due to federal and state interstate banking laws, which permit banking organizations to expand geographically with fewer restrictions than in the past. Such laws allow banks to merge with other banks across state lines, thereby enabling banks to establish or expand banking operations in our market. The competitive environment also is significantly impacted by federal and state legislation, which may make it easier for non-bank financial institutions to compete with us.

Statistical Disclosure

The information in the tables set out below should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations, which are included in Items 7 and 8 of this annual report.

Distribution of Average Assets, Liabilities and Shareholders' Equity; Interest Rates and Interest Differential

Table A sets forth our average consolidated balance sheets for the years ended December 31, 2011, 2010, and 2009 and an analysis of interest rates and the interest rate differential for the years then ended.  Table B sets forth the changes in interest income and interest expense in 2011 and 2010 resulting from changes in volume and changes in rates.

Investment Portfolio

Table of Contents

The book value (amortized cost) of investment securities at December 31, 2011, 2010, and 2009 and the book value, maturities and weighted average yield of investment securities at December 31, 2011 are set forth in Table C.

Loan Portfolio

The composition of the loan portfolio at December 31, 2011, 2010, 2009, 2008, and 2007, is summarized in Table D.

Maturities and sensitivity to changes in interest rates in the loan portfolio at December 31, 2011 are summarized in Table E.

Table F shows the composition of nonaccrual, past due and restructured loans at December 31, 2011, 2010, 2009, 2008, and 2007. Set forth in the text accompanying Table F is a discussion of the Company's policy for placing loans on nonaccrual status.

Summary of Loan Loss Experience

Table G sets forth an analysis of loan loss experience as of and for the years ended December 31, 2011, 2010, 2009, 2008, and 2007.

Set forth in the text accompanying Table G is a description of the factors which influenced management's judgment in determining the amount of the additions to the allowance charged to operating expense in each fiscal year, a table showing the allocation of the allowance for credit losses to the various types of loans in the portfolio, as well as a discussion of management's policy for establishing and maintaining the allowance for credit losses.

Deposits

Table H sets forth the average amount of and the average rate paid on major deposit categories for the years ended December 31, 2011, 2010, and 2009.

Table I sets forth the maturity of time certificates of deposit of $100,000 or more at December 31, 2011.

Return on Equity and Assets

Table J sets forth certain financial ratios for the years ended December 31, 2011, 2010, and 2009.

Table of Contents

Table A

DISTRIBUTION OF AVERAGE ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL

The following table sets forth consolidated average assets, liabilities and shareholders' equity; interest income earned and interest expense paid; and the average yields earned or rates paid thereon for the years ended December 31, 2011, 2010, and 2009. The average balances reflect daily averages except nonaccrual loans, which were computed using quarterly averages.

| | 2011 | | | 2010 | | | 2009 | | |
|---|---|---|---|---|---|---|---|---|---|
| (Dollars in thousands) | Average Balance | Interest Income/ Expense | Average Interest Rate | Average Balance | Interest Income/ Expense | Average Interest Rate | Average Balance | Interest Income/ Expense | Average Interest Rate |
| ASSETS: | | | | | | | | | |
| Interest-earning deposits in other banks | $73,016 | $187 | 0.26 % | $42,047 | $110 | 0.26 % | $3,008 | $8 | 0.27 % |
| Securities: | | | | | | | | | |
| Taxable securities | 150,559 | 4,548 | 3.02 % | 124,163 | 5,472 | 4.41 % | 114,465 | 7,701 | 6.73 % |
| Non-taxable securities (1) | 75,665 | 5,248 | 6.94 % | 64,838 | 4,605 | 7.10 % | 64,325 | 4,632 | 7.20 % |
| Total investment securities | 226,224 | 9,796 | 4.33 % | 189,001 | 10,077 | 5.33 % | 178,790 | 12,333 | 6.90 % |
| Federal funds sold | 695 | 2 | 0.29 % | 713 | 2 | 0.28 % | 17,627 | 48 | 0.27 % |
| Total | 299,935 | 9,985 | 3.33 % | 231,761 | 10,189 | 4.40 % | 199,425 | 12,389 | 6.21 % |
| Loans (2)(3) | 412,969 | 26,098 | 6.32 % | 437,959 | 27,390 | 6.25 % | 469,341 | 29,920 | 6.37 % |
| Federal Home Loan Bank stock | 2,958 | 9 | 0.30 % | 3,084 | 11 | 0.36 % | 3,140 | 7 | 0.22 % |
| Total interest-earning assets (1) | 715,862 | $36,092 | 5.04 % | 672,804 | $37,590 | 5.59 % | 671,906 | $42,316 | 6.30 % |
| Allowance for credit losses | (11,018 ) | | | (10,922 ) | | | (8,608 ) | | |
| Nonaccrual loans | 15,322 | | | 17,381 | | | 13,117 | | |
| Other real estate owned | 217 | | | 2,972 | | | 2,553 | | |
| Cash and due from banks | 17,977 | | | 16,479 | | | 17,401 | | |
| Bank premises and equipment | 5,788 | | | 6,089 | | | 6,629 | | |
| Other non-earning assets | 56,030 | | | 54,049 | | | 49,511 | | |
| Total average assets | $800,178 | | | $758,852 | | | $752,509 | | |

Table of Contents

| (Dollars in thousands) | 2011 Average Balance | Interest Income/ Expense | Average Interest Rate | 2010 Average Balance | Interest Income/ Expense | Average Interest Rate | 2009 Average Balance | Interest Income/ Expense | Average Interest Rate |
|---|---|---|---|---|---|---|---|---|---|
| LIABILITIES AND SHAREHOLDERS' EQUITY: | | | | | | | | | |
| Interest-bearing liabilities | | | | | | | | | |
| Interest-bearing deposits: | | | | | | | | | |
| Savings and NOW accounts | $154,765 | $368 | 0.24 % | $142,350 | $498 | 0.35 % | $131,818 | $771 | 0.58 % |
| Money market accounts (MMA) | 174,049 | 692 | 0.40 % | 157,761 | 1,036 | 0.66 % | 136,104 | 1,262 | 0.93 % |
| Time certificates of deposit, under $100,000 | 70,111 | 688 | 0.98 % | 69,066 | 866 | 1.25 % | 90,614 | 1,922 | 2.12 % |
| Time certificates of deposit, $100,000 and over | 96,620 | 914 | 0.95 % | 114,043 | 1,313 | 1.15 % | 120,579 | 1,912 | 1.59 % |
| Total interest-bearing deposits | 495,545 | 2,662 | 0.54 % | 483,220 | 3,713 | 0.77 % | 479,115 | 5,867 | 1.22 % |
| Other borrowed funds | 10,265 | 280 | 2.73 % | 19,634 | 570 | 2.90 % | 29,987 | 760 | 2.53 % |
| Total interest-bearing liabilities | 505,810 | $2,942 | 0.58 % | 502,854 | $4,283 | 0.85 % | 509,102 | $6,627 | 1.30 % |
| Non-interest bearing demand deposits | 182,244 | | | 152,946 | | | 153,148 | | |
| Other liabilities | 8,738 | | | 6,878 | | | 6,859 | | |
| Shareholders' equity | 103,386 | | | 96,174 | | | 83,400 | | |
| Total average liabilities and shareholders' equity | $800,178 | | | $758,852 | | | $752,509 | | |
| Interest income and rate earned on average earning assets (1) | | $36,092 | 5.04 % | | $37,590 | 5.59 % | | $42,316 | 6.30 % |
| Interest expense and interest cost related to average interest-bearing liabilities | | 2,942 | 0.58 % | | 4,283 | 0.85 % | | 6,627 | 1.30 % |
| Net interest income and net interest margin (4) | | $33,150 | 4.63 % | | $33,307 | 4.95 % | | $35,689 | 5.31 % |

(1) Calculated on a fully tax equivalent basis, which includes Federal tax benefits relating to income earned on municipal bonds totaling $1,784, $1,566 and $1,575 in 2011, 2010 and 2009, respectively.
(2) Loan interest income includes loan fees of $399 in 2011, $460 in 2010, and $544 in 2009.
(3) Average loans do not include nonaccrual loans.
(4) Net interest margin is computed by dividing net interest income by total average interest-earning assets.

Table of Contents

Table B

VOLUME AND RATE ANALYSIS

The following table sets forth, for the years indicated, a summary of the changes in interest earned and interest paid resulting from changes in asset and liability volumes and changes in rates. The change in interest due to both volume and rate has been allocated to change due to volume and rate in proportion to the relationship of absolute dollar amounts of change in each.

| | Years Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2011 Compared to 2010 | | | 2010 Compared to 2009 | | |
| (In thousands) | Volume | Rate | Net | Volume | Rate | Net |
| Increase (decrease) due to changes in: | | | | | | |
| Interest income: | | | | | | |
| Interest-earning deposits in other banks | $80 | $(3) | $77 | $102 | $— | $102 |
| Investment securities: | | | | | | |
| Taxable | 1,926 | (2,850) | (924) | 726 | (2,955) | (2,229) |
| Non-taxable (1) | 746 | (103) | 643 | 39 | (66) | (27) |
| Total investment securities | 2,672 | (2,953) | (281) | 765 | (3,021) | (2,256) |
| Federal funds sold | — | — | — | (48) | 2 | (46) |
| Loans | (1,654) | 362 | (1,292) | (1,649) | (881) | (2,530) |
| FHLB Stock | — | (2) | (2) | — | 4 | 4 |
| Total earning assets (1) | 1,098 | (2,596) | (1,498) | (830) | (3,896) | (4,726) |
| Interest expense: | | | | | | |
| Deposits: | | | | | | |
| Savings, NOW and MMA | 167 | (641) | (474) | 291 | (790) | (499) |
| Certificates of deposit under $100,000 | 13 | (191) | (178) | (388) | (668) | (1,056) |
| Certificates of deposit $100,000 and over | (184) | (215) | (399) | (99) | (500) | (599) |
| Total interest-bearing deposits | (4) | (1,047) | (1,051) | (196) | (1,958) | (2,154) |
| Other borrowed funds | (336) | 46 | (290) | (327) | 137 | (190) |
| Total interest bearing liabilities | (340) | (1,001) | (1,341) | (523) | (1,821) | (2,344) |
| Net interest income (1) | $1,438 | $(1,595) | $(157) | $(307) | $(2,075) | $(2,382) |

(1) Computed on a tax equivalent basis for securities exempt from federal income taxes.

Table of Contents

Table C

INVESTMENT PORTFOLIO

The book value of investment securities at December 31, 2011, 2010, and 2009 is set forth in the following table. At December 31, 2011, we held no investment securities from any issuer which totaled over 10% of our shareholders' equity.

| Available-for-Sale | Book Value at December 31, | | |
|---|---|---|---|
| (In thousands) | 2011 | 2010 | 2009 |
| U.S. Government sponsored entities and agencies | $149 | $190 | $353 |
| Obligations of states and political subdivisions | 101,030 | 74,598 | 68,708 |
| U.S. Government agencies collateralized by mortgage obligations | 204,222 | 88,105 | 85,530 |
| Other collateralized mortgage obligations | 8,408 | 18,661 | 36,280 |
| Corporate debt securities | — | 500 | 1,228 |
| Other equity securities | 7,596 | 7,628 | 7,645 |
| Total Available-for-Sale Securities | $321,405 | $189,682 | $199,744 |

The book value, maturities and weighted average yield of investment securities at December 31, 2011 are summarized in the following table.

| (Dollars in thousands) | In one year or less | | After one through five years | | After five through ten years | | After ten years | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| Available-for-Sale Securities | Amount | Yield(1) | Amount | Yield(1) | Amount | Yield(1) | Amount | Yield(1) | Amount | Yield(1) |
| Debt securities(2) | | | | | | | | | | |
| U.S. Government sponsored entities and agencies | $149 | 4.84 % | $— | — | $— | — | $— | — | $149 | 4.84 % |
| Obligations of states and political subdivisions | 420 | 4.09 % | 8,705 | 4.34 % | 20,553 | 4.12 % | 71,352 | 4.38 % | 101,030 | 4.32 % |
| U.S. Government agencies collateralized by mortgage obligations | 72 | 5.00 % | 176 | 5.92 % | 7,183 | 4.03 % | 196,791 | 4.99 % | 204,222 | 4.96 % |
| Other collateralized mortgage obligations | — | — | — | — | 1,420 | 4.75 % | 6,988 | 5.64 % | 8,408 | 5.49 % |
| Other equity securities | 7,596 | 3.72 % | — | — | — | — | — | — | 7,596 | 3.72 % |
| | $8,237 | 3.77 % | $8,881 | 4.38 % | $29,156 | 4.13 % | $275,131 | 4.85 % | $321,405 | 4.74 % |

(1) Not computed on a tax equivalent basis.

(2) Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties. Expected maturities will also differ from contractual maturities due to unscheduled principal pay downs.

Table of Contents

Table D

LOAN PORTFOLIO

The composition of the loan portfolio at December 31, 2011, 2010, 2009, 2008, and 2007 is summarized in the table below.

| (In thousands) | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Commercial: | | | | | |
| Commercial and industrial | $78,089 | $81,318 | $93,282 | $109,664 | $71,416 |
| Agricultural land and production | 29,958 | 20,604 | 13,903 | 20,406 | 17,584 |
| Total commercial | 108,047 | 101,922 | 107,185 | 130,070 | 89,000 |
| Real estate: | | | | | |
| Owner occupied | 113,183 | 111,888 | 106,606 | 113,414 | 76,808 |
| Real estate-construction and other land loans | 33,047 | 32,038 | 51,633 | 57,923 | 48,593 |
| Commercial real estate | 62,523 | 63,627 | 71,420 | 64,358 | 43,334 |
| Agricultural real estate | 42,596 | 44,397 | 38,759 | 32,136 | 26,796 |
| Other real estate | 7,892 | 8,103 | 4,610 | 2,926 | 1,772 |
| Total real estate | 259,241 | 260,053 | 273,028 | 270,757 | 197,303 |
| Consumer: | | | | | |
| Equity loans and lines of credit | 51,106 | 58,860 | 65,353 | 63,828 | 46,575 |
| Consumer and installment | 9,765 | 11,261 | 14,033 | 19,801 | 8,838 |
| Total consumer | 60,871 | 70,121 | 79,386 | 83,629 | 55,413 |
| Deferred loan fees, net | (764 ) | (499 ) | (392 ) | (218 ) | (588 ) |
| Total gross loans | 427,395 | 431,597 | 459,207 | 484,238 | 341,128 |
| Allowance for credit losses | (11,396 ) | (11,014 ) | (10,200 ) | (7,223 ) | (3,887 ) |
| Total (1) | $415,999 | $420,583 | $449,007 | $477,015 | $337,241 |

| | 2011 | 2010 | | 2009 | | 2008 | | 2007 |
|---|---|---|---|---|---|---|---|---|
| (1) Includes nonaccrual loans of: | $14,434 | $18,561 | 18,959 | $18,959 | 179 | $15,750 | 18,561 | $179 |

Table E

LOAN MATURITIES AND SENSITIVITY TO CHANGES IN INTEREST RATES

The following table presents information concerning loan maturities and sensitivity to changes in interest rates of the indicated categories of our loan portfolio, as well as loans in those categories maturing after one year that have fixed or floating interest rates at December 31, 2011

Table of Contents

| (In thousands) | One Year or Less | After One Through Five Years | After Five Years | Total |
|---|---|---|---|---|
| Loan Maturities: | | | | |
| Commercial and agricultural | $56,389 | $36,727 | $14,931 | $108,047 |
| Real estate construction and other land loans | 14,247 | 12,525 | 6,275 | 33,047 |
| Other real estate | 21,305 | 31,222 | 173,667 | 226,194 |
| Consumer and installment | 8,343 | 15,732 | 36,796 | 60,871 |
| | $100,284 | $96,206 | $231,669 | $428,159 |
| Sensitivity to Changes in Interest Rates: | | | | |
| Loans with fixed interest rates | $27,160 | $42,205 | $37,620 | $106,985 |
| Loans with floating interest rates | 73,124 | 54,001 | 194,049 | 321,174 |
| | $100,284 | $96,206 | $231,669 | $428,159 |

Table F

COMPOSITION OF NONACCRUAL, PAST DUE AND RESTRUCTURED LOANS

A summary of nonaccrual, restructured and past due loans at December 31, 2011, 2010, 2009, 2008, and 2007 is set forth below:

| | December 31, | | | | |
|---|---|---|---|---|---|
| (Dollars in thousands) | 2011 | 2010 | 2009 | 2008 | 2007 |
| Nonaccrual | $3,833 | $7,906 | $14,391 | $14,047 | $179 |
| Restructured nonaccrual loans | 10,601 | 10,655 | 4,568 | 1,703 | — |
| | $14,434 | $18,561 | $18,959 | $15,750 | $179 |
| Accruing loans past due 90 days or more | — | — | — | — | — |
| Accruing troubled debt restructurings | 9,210 | — | — | — | — |
| Nonaccrual loans to total loans | 3.38 % | 4.30 % | 4.13 % | 3.25 % | 0.05 % |

Our consolidated financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on loans. Interest income from nonaccrual loans is recorded only if collection of principal in full is not in doubt and when and if received.

Loans are placed on nonaccrual status and any accrued but unpaid interest income is reversed and charged against income when the payment of interest or principal is 90 days or more past due. Loans in the nonaccrual category are treated as nonaccrual loans even though we may ultimately recover all or a portion of the interest due. These loans return to accrual status when the loan becomes contractually current, future collectibility of amounts due is reasonably assured, and a minimum of six months of satisfactory principal repayment performance has occurred. As of December 31, 2011, nonaccrual loans totaled $14,434,000 and interest foregone on nonaccrual loans totaled $954,000 for the year then ended. As of December 31, 2010, we had nonaccrual loans totaling $18,561,000 and interest foregone on nonaccrual loans totaled $1,228,000 for the year then ended. As of December 31, 2009, we had nonaccrual loans totaling $18,959,000 and interest foregone on nonaccrual loans totaled $852,000 for the year then ended. We had nonaccrual loans totaling $15,750,000 at December 31, 2008 and interest foregone on nonaccrual loans totaled $371,000 for the year then ended. As of December 31, 2007, we had nonaccrual loans totaling $179,000 and interest foregone on nonaccrual loans totaled $8,000 for the year then ended. See Note 5 of the Company's audited Consolidated Financial Statements in Item 8 of this Annual Report.

Included in nonaccrual loans at December 31, 2011 were six loans totaling $10,601,000 that were considered troubled debt restructurings (TDRs).  There are no outstanding commitments to lend additional funds to any of these borrowers.  Included in nonaccrual loans at December 31, 2010 were twelve loans that totaled $10,655,000 that were considered to be TDRs at December 31, 2010. The Company had seven loans at December 31, 2009 totaling $4,568,000 that were considered to be TDRs. As of December 31, 2008, the Company had two loans totaling $1,703,000 that were on nonaccrual and considered TDR.  At December 31, 2007 the Company had no restructured loans.  See Note 6 of the Company's audited Consolidated

Financial Statements in Item 8 of this Annual Report concerning our recorded investment in loans for which impairment has been recognized. Impaired loans are identified from internal credit review reports, past due reports, overdraft listings, and regulatory reports of examination. Borrowers experiencing problems such as operating losses, marginal working capital, inadequate cash flow or business interruptions which jeopardize collection of the loan are also reviewed for possible impairment classification.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Company measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the underlying collateral. We perform quarterly internal reviews on substandard loans. We place loans on nonaccrual status and classify them as impaired when a reasonable doubt exists as to the collectibility of interest and principal under the original contractual terms, or when loans are delinquent 90 days or more unless the loan is both well secured and in the process of collection. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on nonaccrual status until such time as management has determined that the loans are likely to remain current in future periods. Foregone interest on nonaccrual loans totaled $954,000 for the year ended December 31, 2011 of which $769,000 was attributable to troubled debt restructurings. Foregone interest on nonaccrual loans was $1,228,000 and $852,000 for 2010 and 2009, respectively of which $376,000 and $404,000 was attributable to troubled debt restructurings, respectively.

Other than as discussed above, as of December 31, 2011, we had no loans where known information about possible credit problems of borrowers caused management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in disclosure of such loans as impaired loans.

Table of Contents

Table G

SUMMARY OF LOAN LOSS EXPERIENCE

The following table summarizes loan loss experience as of and for the years ended December 31, 2011, 2010, 2009, 2008, and 2007.

| (Dollars in thousands) | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Loans outstanding at December 31, | $428,159 | $432,096 | $459,599 | $484,456 | $341,716 |
| Average loans outstanding during the year | $428,291 | $455,340 | $482,458 | $367,009 | $331,459 |
| Allowance for credit losses: | | | | | |
| Balance at beginning of year | $11,014 | $10,200 | $7,223 | $3,887 | $3,809 |
| Deduct loans charged-off: | | | | | |
| Commercial and industrial | (280) | (1,938) | (1,383) | (175) | (264) |
| Owner occupied | — | (218) | (1,160) | — | — |
| Real estate construction and other land loans | (286) | (823) | (569) | — | — |
| Commercial real estate | (26) | (11) | (1,588) | — | — |
| Other real estate | — | (453) | (2,450) | (393) | (12) |
| Consumer loans | (940) | (679) | (776) | (283) | (205) |
| Total loans charged-off | (1,532) | (4,122) | (7,926) | (851) | (481) |
| Add recoveries of loans previously charged off: | | | | | |
| Commercial and industrial | 286 | 429 | 45 | 22 | 15 |
| Owner occupied | — | 258 | 20 | — | — |
| Real estate construction and other land loans | 52 | 42 | 55 | — | — |
| Commercial real estate | 176 | — | 5 | — | — |
| Other real estate | — | 81 | 201 | 22 | 1 |
| Consumer loans | 350 | 326 | 63 | 67 | 63 |
| Total recoveries | 864 | 1,136 | 389 | 111 | 79 |
| Net charge-offs | (668) | (2,986) | (7,537) | (740) | (402) |
| Allowance acquired in mergers | — | — | — | 2,786 | — |
| Add provision charged to operating expense | 1,050 | 3,800 | 10,514 | 1,290 | 480 |
| Balance at end of year | $11,396 | $11,014 | $10,200 | $7,223 | $3,887 |
| Allowance for credit losses as a percentage of outstanding loan balance | 2.66 % | 2.55 % | 2.22 % | 1.49 % | 1.14 % |
| Net charge-offs to average loans outstanding | (0.16)% | (0.66)% | (1.56)% | (0.20)% | (0.12)% |

Managing credits identified through the risk evaluation methodology includes developing a business strategy with the customer to mitigate our losses. Our management continues to monitor these credits with a view to identifying as early as possible when, and to what extent, additional provisions may be necessary.

The allowance for credit losses is reviewed at least quarterly by the Bank's and our Board of Directors' Audit/Compliance Committee. Reserves are allocated to loan portfolio segments using percentages which are based on both historical risk elements such as delinquencies and losses and predictive risk elements such as economic,

competitive and environmental factors. We have adopted the specific reserve approach to allocate reserves to each impaired asset for the purpose of estimating potential loss exposure. Although the allowance for credit losses is allocated to various portfolio categories, it is general in nature and available for the loan portfolio in its entirety. Additions may be required based on the results of independent loan portfolio examinations, regulatory agency examinations, or our own internal review process. Additions are also required when, in management's judgment, the reserve does not properly reflect the potential loss exposure.

The provision for credit losses for the years ended December 31, 2011 was $1,050,000. The amount of provision is primarily the result of our assessment of the overall adequacy of the allowance for credit losses considering a number of

Table of Contents

factors, including the increase or decrease in the volume of outstanding loans and the level of net charge offs during the year. The decrease in the provision in 2011 was due to a reduction in net charge offs which were $668,000 and a period-to-period decrease in the level of outstanding loans. As in December 31, 2010 the provision decreased to $3,800,000 because of the reduction in net charge offs which were $2,986,000 with a period-to-period decrease in the level of outstanding loans. In 2009, the Bank added $10,514,000 to the provision. The increase in 2009 was primarily the result of our assessment of the overall adequacy of the allowance for credit losses including the increase in the volume of outstanding loans and the level of net charge offs during the year of $7,537,000. In 2008, the Bank added $1,290,000 to the allowance for credit losses. The increase in 2008 resulted from management's overall assessment of the probable losses within the loan portfolio at December 31, 2008, the growth in loans and considering the level of net charge-offs during the year of $740,000. For 2007, the Bank added $480,000 to the allowance for credit losses. The increase in 2007 was due in part to the growth in loans and the result of our assessment of probable losses within the loan portfolio.

Using the criteria on the previous page, the allocation of the allowance for credit losses is set forth below:

| | 2011 | | | 2010 | | | 2009 | | | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| (Dollars in thousands) | Amount | Percent of Loans in Each Category to Total Loans | | Amount | Percent of Loans in Each Category to Total Loans | | Amount | Percent of Loans in Each Category to Total Loans | | Amount | Percent of Loans in Each Category to Total Loans | | Amount | Percent of Loans in Each Category to Total Loans | |
| Commercial and industrial | $1,853 | 16.8 | % | $2,149 | 17.4 | % | $2,861 | 22.2 | % | $1,777 | 26.7 | % | $1,254 | 27.1 | % |
| Real estate construction, land development and other land loans | 2,954 | 7.7 | % | 1,791 | 7.4 | % | 836 | 10.3 | % | 820 | 9.6 | % | 312 | 10.5 | % |
| Real estate - other | 3,712 | 42.8 | % | 3,579 | 42.5 | % | 3,813 | 48.2 | % | 2,570 | 46.9 | % | 1,353 | 44.0 | % |
| Equity loans and lines of credit | 1,419 | 12.0 | % | 1,975 | 13.6 | % | 334 | 7.8 | % | 64 | 6.8 | % | 157 | 7.2 | % |
| Loans to finance agricultural and other loans to farmers | 831 | 16.9 | % | 674 | 15.1 | % | 708 | 7.8 | % | 235 | 6.7 | % | 501 | 9.4 | % |
| Loans to individuals for household, family and other personal expenditures and other loans | 417 | 2.3 | % | 528 | 2.6 | % | 423 | 2.4 | % | 593 | 3.1 | % | 236 | 1.7 | % |
| Other | 71 | 1.5 | % | 80 | 1.4 | % | 48 | 1.3 | % | 64 | 0.2 | % | 23 | 0.1 | % |
| Unallocated reserve | 139 | — | | 238 | — | | 1,177 | — | | 1,100 | — | | 51 | — | |
| | $11,396 | 100.0 | % | $11,014 | 100.0 | % | $10,200 | 100.0 | % | $7,223 | 100.0 | % | $3,887 | 100.0 | % |

Loans are charged to the allowance for credit losses when the loans are deemed uncollectible. It is the policy of management to make additions to the allowance so that it remains adequate to cover all probable loan charge-offs that exist in the portfolio at that time. In 2010 enhanced ALLL methodology enabled us to assign qualitative and quantitative factors (Q factors) to each loan category resulting in a decrease in unallocated reserves. Q factors include reserves held for the effects of lending policies, economic trends, and portfolio trends along with other dynamics which may cause additional stress to the portfolio.

15

Table of Contents

Table H

DEPOSITS

We have no known foreign deposits.  The following table sets forth the average amount of and the average rate paid on certain deposit categories which were in excess of 10% of average total deposits for the years ended December 31, 2011, 2010, and 2009.

| | 2011 | | | 2010 | | | 2009 | | |
|---|---|---|---|---|---|---|---|---|---|
| (Dollars in thousands) | Balance | Rate | | Balance | Rate | | Balance | Rate | |
| NOW accounts | $124,899 | 0.26 | % | $116,504 | 0.38 | % | $109,318 | 0.66 | % |
| Money market accounts | $174,049 | 0.40 | % | $157,761 | 0.66 | % | $136,104 | 0.93 | % |
| Time certificates of deposit | $166,731 | 0.96 | % | $183,109 | 1.19 | % | $211,193 | 1.82 | % |
| Non-interest bearing demand | $182,244 | — | | $152,946 | — | | $153,148 | — | |
| Total deposits | $677,789 | 0.39 | % | $636,166 | 0.58 | % | $632,263 | 0.93 | % |

Table I

TIME DEPOSITS

The following table sets forth the maturity of time certificates of deposit and other time deposits of $100,000 or more at December 31, 2011.

| (In thousands) | |
|---|---|
| Three months or less | $41,943 |
| Over 3 months through 6 months | 27,029 |
| Over 6 through 12 months | 27,586 |
| Over 12 months | 6,019 |
| | $102,577 |

Table J

FINANCIAL RATIOS

The following table sets forth certain financial ratios for the years ended December 31, 2011, 2010, and 2009.

| | 2011 | | 2010 | | 2009 | |
|---|---|---|---|---|---|---|
| Net income: | | | | | | |
| To average assets | 0.81 | % | 0.43 | % | 0.34 | % |
| To average shareholders’ equity | 6.26 | % | 3.41 | % | 3.10 | % |
| Dividends declared per share to net income per share | — | | — | | — | |
| Average shareholders’ equity to average assets | 12.92 | % | 12.67 | % | 11.08 | % |

Supervision and Regulation

GENERAL

The banking and financial services businesses in which we engage are highly regulated. Such regulation is intended, among other things, to protect depositors whose deposits are insured by the FDIC and the banking system as a whole. The monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Board of Governors, also influence the commercial banking business. The Board of Governors implements national monetary policies

(with objectives such as curbing inflation and combating recession) by its open-market operations in United States Government securities, by adjusting the required level of reserves for financial intermediaries subject to its reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the Board of Governors in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. Indirectly such actions may also affect the ability of non-bank financial institutions to compete with the Bank. The nature and impact of any future changes in monetary policies cannot be predicted.

The laws, regulations, and policies affecting financial services businesses are continuously under review by Congress and state legislatures, and federal and state regulatory agencies. From time to time, legislation is enacted which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial intermediaries. Proposals to change the laws and regulations governing the operations and taxation of banks, bank holding companies and other financial intermediaries are frequently made in Congress, in the California legislature and before various bank regulatory and other professional agencies. Changes in the laws, regulations or policies that affect us cannot necessarily be predicted, but they may have a material effect on our business and earnings.

BANK HOLDING COMPANY REGULATION

The Company, as a bank holding company, is subject to regulation under the BHC Act, and is subject to the supervision and examination of the Board of Governors. Pursuant to the BHC Act, we are required to obtain the prior approval of the Board of Governors before we may acquire all or substantially all of the assets of any bank, or ownership or control of voting shares of any bank if, after giving effect to such acquisition, we would own or control, directly or indirectly, more than five percent of such bank.

Under the BHC Act, we may not engage in any business other than managing or controlling banks or furnishing services to our subsidiaries that the Board of Governors deems to be so closely related to banking as to be a proper incident to banking. We are also prohibited, with certain exceptions, from acquiring direct or indirect ownership or control of more than five percent of the voting shares of any company unless the company is engaged in banking activities or the Board of Governors determines that the activity is so closely related to banking to be a proper incident to banking. The Board of Governors' approval must be obtained before the shares of any such company can be acquired and, in certain cases, before any approved company can open new offices.

The BHC Act and regulations of the Board of Governors also impose certain constraints on the redemption or purchase by a bank holding company of its own shares of stock.

Our earnings and activities are affected by legislation, by actions of regulators, and by local legislative and administrative bodies and decisions of courts in the jurisdictions in which both the Company and the Bank conduct business. For example, these include limitations on the ability of the Bank to pay dividends to the Company and the ability of the Company to pay dividends to its shareholders. It is the policy of the Board of Governors that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. Various federal and state statutory provisions limit the amount of dividends that subsidiary banks can pay to their holding companies without regulatory approval. In addition to these explicit limitations, the federal regulatory agencies are authorized to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

In addition, banking subsidiaries of bank holding companies are subject to certain restrictions imposed by federal law in dealings with their holding companies and other affiliates. Subject to certain exceptions set forth in the Federal Reserve Act and the recently enacted Regulation W, a bank can make a loan or extend credit to an affiliate, purchase or invest in the securities of an affiliate, purchase assets from an affiliate, accept securities of an affiliate as collateral security for a loan or extension of credit to any person or company, issue a guarantee, or accept letters of credit on behalf of an affiliate only if the aggregate amount of the above transactions of such subsidiary does not exceed 10 percent of such subsidiary's capital stock and surplus on a per affiliate basis or 20 percent of such subsidiary's capital stock and surplus on an aggregate affiliate basis. Such transactions must be on terms and conditions that are consistent with safe and sound banking practices. A bank and its subsidiaries generally may not purchase a "low-quality asset," as that term is defined in the Federal Reserve Act, from an affiliate. Such restrictions also generally prevent a holding company and its other affiliates from borrowing from a banking subsidiary of the holding company unless the loans are secured by collateral.

Table of Contents

A holding company and its banking subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, sale or lease of property or provision of services. For example, with certain exceptions a bank may not condition an extension of credit on a customer obtaining other services provided by it, a holding company or any of its other bank affiliates, or on a promise by the customer not to obtain other services from a competitor.

The Board of Governors has cease and desist powers over parent bank holding companies and non-banking subsidiaries where actions of a parent bank holding company or its non-financial institution subsidiaries represent an unsafe or unsound practice or violation of law. The Board of Governors has the authority to regulate debt obligations (other than commercial paper) issued by bank holding companies by imposing interest ceilings and reserve requirements on such debt obligations.

We are also a bank holding company within the meaning of Section 3700 of the California Financial Code. As such, we and our subsidiaries are subject to examination by the Department of Financial Institutions (DFI).

Further, we are required by the Board of Governors to maintain certain capital levels. See “Capital Standards.”

REGULATION OF THE BANK

Banks are extensively regulated under both federal and state law. The Bank, as a California state-chartered bank, is subject to primary supervision, regulation and periodic examination by the DFI and the FDIC. The Bank is not a member of the Federal Reserve System, but is nevertheless subject to certain regulations of the Board of Governors.

If, as a result of an examination of a bank, the FDIC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank’s operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, various remedies are available to the FDIC. Such remedies include the power to enjoin “unsafe or unsound” practices, to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the growth of the Bank, to assess civil monetary penalties, to remove officers and directors, and ultimately to terminate the Bank’s deposit insurance, which for a California chartered bank would result in a revocation of the Bank’s charter. The DFI has many of the same remedial powers.

The Bank is a member of the FDIC, which currently insures customer deposits in each member bank to a maximum of $250,000 per depositor. For this protection, the Bank is subject to the rules and regulations of the FDIC, and, as is the case with all insured banks, may be required to pay a semi-annual statutory assessment. As mandated by the Dodd-Frank Act, the FDIC Board approved the final rule that implemented unlimited deposit insurance coverage on noninterest-bearing transaction accounts beginning on December 31, 2010, and ending December 31, 2012. This coverage replaces the unlimited coverage under the Transaction Account Guarantee Program (the “TAGP”). Coverage under this program is confined to noninterest-bearing accounts and interest-bearing Lawyers Trust accounts (IOLTAs). The coverage will not include other accounts, such as traditional checking or demand deposit accounts that may earn interest, NOW accounts, and money-market deposit accounts.

Various requirements and restrictions under the laws of the State of California and the United States affect the operations of the Bank. State and federal statutes and regulations relate to many aspects of the Bank’s operations, including standards for safety and soundness, reserves against deposits, interest rates payable on deposits, loans, investments, mergers and acquisitions, borrowings, dividends, locations of branch offices, fair lending requirements, Community Reinvestment Act activities, and loans to affiliates.

PAYMENT OF DIVIDENDS

THE COMPANY

Our shareholders are entitled to receive dividends when and as declared by our Board of Directors, out of funds legally available, subject to the dividends preference, if any, on preferred shares that may be outstanding, and also subject to the restrictions of the California Corporations Code. See Note 12 of the Company's audited Consolidated Financial Statements in Item 8 of this Annual Report concerning preferred stock issued through the Small Business Lending Fund of the United States Department of the Treasury on August 18, 2011 and preferred stock and common stock issued pursuant to Stock Purchase Agreements with accredited private investors.

The principal source of cash revenue to the Company is dividends received from the Bank. The Bank's ability to make dividend payments to the Company is subject to state and federal regulatory restrictions.

Table of Contents

THE BANK

Dividends payable by the Bank to the Company are restricted under California law to the lesser of the Bank’s retained earnings, or the Bank’s net income for the latest three fiscal years, less dividends paid during that period, or, with the approval of the DFI, to the greater of the retained earnings of the Bank, the net income of the Bank for its last fiscal year or the net income of the Bank for its current fiscal year.

In addition to the regulations concerning minimum uniform capital adequacy requirements described below, the FDIC has established guidelines regarding the maintenance of an adequate allowance for credit losses. Therefore, the future payment of cash dividends by the Bank will generally depend, in addition to regulatory constraints, upon the Bank’s earnings during any fiscal period, the assessment of the Board of Directors of the capital requirements of the Bank and other factors, including the maintenance of an adequate allowance for credit losses.

CAPITAL STANDARDS

The Board of Governors, the FDIC and other federal banking agencies have issued risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization’s operations for both transactions reported on the balance sheet as assets, and transactions, such as letters of credit and recourse arrangements, which are reported as off-balance-sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. government securities, to 100% for assets with relatively higher credit risk, such as business loans.

A banking organization’s risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets and off-balance-sheet items. The regulators measure risk-adjusted assets and off-balance-sheet items against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. Tier 1 capital consists of common stock, retained earnings, noncumulative perpetual preferred stock and minority interests in certain subsidiaries, less most other intangible assets. Tier 2 capital may consist of a limited amount of the allowance for possible loan and lease losses and certain other instruments with some characteristics of equity. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies. Since December 31, 1992, the federal banking agencies have required a minimum ratio of qualifying total capital to risk-adjusted assets and off-balance-sheet items of 8%, and a minimum ratio of Tier 1 capital to risk-adjusted assets and off-balance-sheet items of 4%.

In addition to the risk-based guidelines, federal banking regulators require banking organizations to maintain a minimum amount of Tier 1 capital to average total assets, referred to as the leverage ratio. For a banking organization rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio of Tier 1 capital to total assets is 3%. It is improbable, however, that an institution with a 3% leverage ratio would receive the highest rating by the regulators since a strong capital position is a significant part of the regulators’ rating. For all banking organizations not rated in the highest category, the minimum leverage ratio is at least 100 to 200 basis points above the 3% minimum. Thus, the effective minimum leverage ratio, for all practical purposes, is at least 4% or 5%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

A bank that does not achieve and maintain the required capital levels may be issued a capital directive by the FDIC to ensure the maintenance of required capital levels. As discussed above, the Company and the Bank are required to maintain certain levels of capital. The regulatory capital guidelines as well as the actual capitalization for the Bank

and the Company on a consolidated basis as of December 31, 2011 are as follows:

| | REQUIREMENT | | ACTUAL | |
|---|---|---|---|---|
| | ADEQUATELY CAPITALIZED | FOR THE BANK TO BE WELL CAPITALIZED | BANK | COMPANY |
| Total risk-based capital ratio | 8.00 % | 10.00 % | 17.31 % | 17.49 % |
| Tier 1 risk-based capital ratio | 4.00 % | 6.00 % | 16.02 % | 16.20 % |
| Tier 1 leverage capital ratio | 4.00 % | 5.00 % | 10.01 % | 10.13 % |

Table of Contents

USA PATRIOT ACT

On October 26, 2001, the President signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001. The USA PATRIOT Act also made significant changes to the Bank Secrecy Act. Under the USA PATRIOT Act, financial institutions are subject to prohibitions against specified financial transactions and account relationships as well as enhanced due diligence and of identifying customers when establishing new relationships and standards in their dealings with foreign financial institutions and foreign customers. For example, the enhanced due diligence policies, procedures, and controls generally require financial institutions to take reasonable steps:

* To conduct enhanced scrutiny of account relationships to guard against money laundering and report any suspicious transaction;

* To ascertain the identity of the nominal and beneficial owners of, and the source of funds deposited into, each account as needed to guard against money laundering and report any suspicious transactions;

* To ascertain for any foreign bank, the shares of which are not publicly traded, the identity of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner; and

* To ascertain whether any foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related due diligence information.

Under the USA PATRIOT Act, financial institutions are to establish anti-money laundering programs to enhance their Bank Secrecy Act program. The USA PATRIOT Act sets forth minimum standards for these programs, including:

* The development of internal policies, procedures, and controls;

* The designation of a compliance officer;

* An ongoing employee training program; and

* An independent audit function to test the programs.

Bank management believes that the Bank is currently in compliance with the Act.

FINANCIAL SERVICES MODERNIZATION LEGISLATION

On November 12, 1999, President Clinton signed into law the Gramm-Leach-Bliley Act, also known as the Financial Services Modernization Act. This legislation eliminated many of the barriers that have separated the insurance, securities and banking industries since the Great Depression. The federal banking agencies (the Board of Governors, FDIC and the Office of the Comptroller of the Currency) among others, continue to draft regulations to implement the Gramm-Leach-Bliley Act. The Gramm-Leach-Bliley Act is the result of a decade of debate in the Congress regarding a fundamental reformation of the nation’s financial system. The law is subdivided into seven titles, by functional area.

The major provisions of the Gramm-Leach-Bliley Act are:

FINANCIAL HOLDING COMPANIES AND FINANCIAL ACTIVITIES. Title I establishes a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms, and other financial service providers by revising and expanding the BHC Act framework to permit a holding company system to engage

in a full range of financial activities through qualification as a new entity known as a financial holding company.

Final regulations adopted by the FDIC in January 2001, in the form of amendments to Part 362 of the FDIC rules and regulations, provide the framework for subsidiaries of state nonmember banks to engage in financial activities that the Gramm-Leach-Bliley Act permits national banks to conduct through a financial subsidiary.

Activities permissible for financial subsidiaries of national banks, and, pursuant to Section 362 of the FDIC rules and regulations, also permissible for financial subsidiaries of state nonmember banks, include, but are not limited to, the following: (a) Lending, exchanging, transferring, investing for others, or safeguarding money or securities;
(b) Insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as

principal, agent, or broker for purposes of the foregoing, in any State; (c) Providing financial, investment, or economic advisory services, including advising an investment company; (d) Issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly; and (e) Underwriting, dealing in, or making a market in securities.

SECURITIES ACTIVITIES. Title II narrows the exemptions from the securities laws previously enjoyed by banks and creates a new, voluntary investment bank holding company. The Board of Governors and the SEC continue to work together to draft rules governing certain securities activities of banks.

INSURANCE ACTIVITIES. Title III restates the proposition that the states are the functional regulators for all insurance activities, including the insurance activities of federally-chartered banks, and bars the states from prohibiting insurance activities by depository institutions.

PRIVACY. Under Title V, federal banking regulators were required to adopt rules that have limited the ability of banks and other financial institutions to disclose non-public information about consumers to nonaffiliated third parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. Federal banking regulators issued final rules on May 10, 2000 to implement the privacy provisions of Title V. Under the rules, financial institutions must provide:

* initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates;

* annual notices of their privacy policies to current customers; and

* a reasonable method for customers to “opt out” of disclosures to nonaffiliated third parties.

Compliance with these rules was mandatory after July 1, 2001. The Company and the Bank were in full compliance with the rules as of or prior to their respective effective dates.

SAFEGUARDING CONFIDENTIAL CUSTOMER INFORMATION. Under Title V, federal banking regulators are required to adopt rules requiring financial institutions to implement a program to protect confidential customer information. In January 2000, the federal banking agencies adopted guidelines requiring financial institutions to establish an information security program.

The Bank implemented a security program appropriate to its size and complexity and the nature and scope of its operations prior to the July 1, 2001 effective date of the regulatory guidelines, and since initial implementation has, as necessary, updated and improved that program.

COMMUNITY REINVESTMENT ACT SUNSHINE REQUIREMENTS. The federal banking agencies have adopted final regulations implementing Section 711 of Title VII of the Gramm-Leach-Bliley Act, the Sunshine Requirements. The regulations require nongovernmental entities or persons and insured depository institutions and affiliates that are parties to written agreements made in connection with the fulfillment of the institution’s CRA obligations to make available to the public and the federal banking agencies a copy of each agreement. Neither the Company nor the Bank is a party to any agreement that would be the subject of reporting pursuant to the CRA Sunshine Requirements.

The Company continues to evaluate the strategic opportunities presented by the broad powers granted to bank holding companies that elect to be treated as financial holding companies. In the event that the Company determines that

access to the broader powers of a financial holding company is in the best interests of the Company, its shareholders and the Bank, the Company will file the appropriate election with the Board of Governors.

The Company and the Bank intend to comply with all provisions of the Gramm-Leach-Bliley Act and all implementing regulations as they become effective.

CONSUMER PROTECTION LAWS AND REGULATIONS

The bank regulatory agencies are focusing greater attention on compliance with consumer protection laws and their implementing regulations. Examination and enforcement have become more intense in nature, and insured institutions have been advised to monitor carefully compliance with such laws and regulations. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.



---

Table of Contents

The Community Reinvestment Act (CRA) is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank's record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution's record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of "outstanding" to a low of "substantial noncompliance." The Bank was last examined for CRA compliance by its primary regulator, the FDIC, as of November 2009.

The Equal Credit Opportunity Act (ECOA) generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act (TILA) is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act (FH Act) regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Home Mortgage Disclosure Act (HMDA) grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a "fair lending" aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes.

Finally, the Real Estate Settlement Procedures Act (RESPA) requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties.

Due to heightened regulatory concern related to compliance with the CRA, TILA, FH Act, ECOA, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

CALIFORNIA FINANCIAL INFORMATION PRIVACY ACT/FAIR CREDIT REPORTING ACT

In 1970, the Federal Fair Credit Reporting Act (the FCRA) was enacted to insure the confidentiality, accuracy, relevancy and proper utilization of consumer credit report information. Under the framework of the FCRA, the United States has developed a highly advanced and efficient credit reporting system. The information contained in that broad system is used by financial institutions, retailers and other creditors of every size in making a wide variety of decisions regarding financial transactions. Employers and law enforcement agencies have also made wide use of the information collected and maintained in databases made possible by the FCRA. The FCRA affirmatively

preempts state law in a number of areas, including the ability of entities affiliated by common ownership to share and exchange information freely, and the requirements on credit bureaus to reinvestigate the contents of reports in response to consumer complaints, among others.

The California Financial Information Privacy Act, which was enacted in 2003, requires a financial institution to provide specific information to a consumer related to the sharing of that consumer's nonpublic personal information. The Act allows a consumer to direct the financial institution not to share his or her nonpublic personal information with affiliated or nonaffiliated companies with which a financial institution has contracted to provide financial products and services, and requires that permission from each such consumer be acquired by a financial institution prior to sharing such information.

The FACT Act, (Fair and Accurate Credit Transaction Act) became law in 2003, effectively extending and amending provisions of the Fair Credit Reporting Act (FCRA). The FACT Act created many new responsibilities for consumer reporting

agencies and users of consumer reports. It contains many new consumer disclosure requirements as well as provisions to address identity theft.

CHECK 21 ACT

On December 22, 2003, the Board of Governors amended Regulation CC and its commentary to implement the Check Clearing for the 21st Century Act (Check 21 Act). The Check 21 Act became effective on October 28, 2004.

To facilitate check truncation and electronic check exchange, the Check 21 Act authorizes a new negotiable instrument called a “substitute check” and provides that a properly prepared substitute check is the legal equivalent of the original check for all purposes. A substitute check is a paper reproduction of the original check that can be processed just like the original check. The Check 21 Act does not require any bank to create substitute checks or to accept checks electronically. The amendments: 1) set forth the requirements of the Check 21 Act that applies to banks; 2) provide a model disclosure and model notices relating to substitute checks; and 3) set forth bank endorsement and identification requirements for substitute checks.

The Bank has been imaging its customers’ checks since 2000. Check 21 Act has had limited impact on the Bank.

Recent Accounting Pronouncements

Determination of Whether a Restructuring is a Troubled Debt Restructuring

In April 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-02, A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring. This ASU provides for a more consistent application of the accounting guidance for troubled debt restructurings (TDRs). This ASU clarified guidance on a creditor's evaluation of whether it has granted a concession to a borrower, and clarified guidance to determine if a borrower is experiencing financial difficulties. This ASU also finalized the disclosures required in a creditor's financial statements related to TDRs. The new provisions of this standard became effective on July 1, 2011.

As a result of adopting ASU 2011-02, management reassessed all restructurings that occurred on or after January 1, 2011 and identified six loans totaling $15,293,000 that were not previously identified as TDRs which now qualify as TDRs under the guidance of ASU 2011-02. The identification of the $15,293,000 of TDRs resulted in an increase to the specific reserves added to the allowance for credit losses of $1,471,000 at December 31, 2011.

Impact of New Financial Accounting Standards

Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs

In May 2011, FASB issued ASU 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. This ASU represents the converged guidance of the FASB and the IASB (the Boards) on fair value measurement. The collective efforts of the Boards and their staffs, reflected in ASU 2011-04, have resulted in common requirements for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning of the term “fair value.” The Boards have concluded the common requirements will result in greater comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and IFRSs. The amendments to the FASB Accounting Standards Codification™ (Codification) in this ASU are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is

not permitted. Management does not believe the adoption of this ASU will have a significant impact on the Company's financial position, results of operations or cash flows.

Presentation of Comprehensive Income

In June 2011, FASB issued ASU 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. This ASU amends the FASB Accounting Standards Codification TM (Codification) to allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The amendments to the Codification in the ASU do not change the items that must be reported in other comprehensive income

or when an item of other comprehensive income must be reclassified to net income. In October 2011, FASB decided that the specific requirement to present items that are reclassified from other comprehensive income to net income alongside their respective components of net income and other comprehensive income will be deferred. Therefore, those requirements will not be effective for fiscal years and interim periods with those years beginning after December 15, 2011. The remaining provisions of ASU 2011-05 should be applied retrospectively. The amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. Management does not believe the adoption of this ASU will have a significant impact on the Company's financial position, results of operations or cash flows.

Intangibles - Goodwill and Other Topics

The FASB has issued ASU 2011-08, Intangibles-Goodwill and Other (Topic 350 ): Testing Goodwill for Impairment. ASU 2011-08 is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, Intangibles-Goodwill and Other. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The Company has elected to early-adopt the provisions of ASU 2011-08 and apply the provisions to management's annual evaluation of the Company's Goodwill as of September 30,2011. The impact of adoption was not material to the Company's financial position, results of operations or cash flows.

Other

Other legislation which has been or may be proposed to the United States Congress and the California Legislature and regulations which may be proposed by the Board of Governors, FDIC and the DFI may affect our business. It cannot be predicted whether any pending or proposed legislation or regulations will be adopted or the effect such legislation or regulations may have upon our business.

ITEM 1A - RISK FACTORS

An investment in our common stock is subject to risks inherent to our business. The material risks and uncertainties that Management believes may affect our business are described below. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included or incorporated by reference in this Annual Report. The risks and uncertainties described below are not the only ones facing our business. Additional risks and uncertainties that Management is not aware of or focused on or that Management currently deems immaterial may also impair our business operations. This Annual Report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, our financial condition and results of operations could be materially and adversely affected. If this were to happen, the value of our common stock could decline significantly, and you could lose all or part of your investment.

Worsening economic conditions could adversely affect our business.

The economic conditions in the United States in general and within California and in our operating markets may continue to deteriorate. Unemployment nationwide and in California has increased significantly through this economic downturn and is anticipated to remain elevated for the foreseeable future. Availability of credit and consumer spending, real estate values, and consumer confidence have all declined markedly. The volatility of the

capital markets and the credit, capital and liquidity problems confronting the U.S. financial system have not been resolved despite massive government expenditures and legislative efforts to stabilize the U.S. financial system. There is no assurance that such conditions will improve or be resolved in the foreseeable future.

The Bank conducts banking operations principally in California's Central Valley. As a result, our financial condition, results of operations and cash flows are subject to changes in the economic conditions in California's Central Valley. Our business results are dependent in large part upon the business activity, population, income levels, deposits and real estate activity in the Central Valley, and continued adverse economic conditions could have a material adverse effect upon us. In addition, the Central Valley remains largely dependent on agriculture. A downturn in agriculture and agricultural related business could indirectly and adversely affect our results of operations and financial condition.

We can provide no assurance that economic conditions in the United States in general and in the State of California

and within our operating markets will not further deteriorate or that such deterioration will not materially and adversely affect us. A further deterioration in economic conditions locally, regionally or nationally could result in a further economic downturn in the Central Valley with the following consequences, any of which could further adversely affect our business:

- loan delinquencies and defaults may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decline;
- low cost or noninterest bearing deposits may decrease;
- collateral for loans may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral as sources of repayment of existing loans;
- foreclosed assets may not be able to be sold;
- volatile securities market conditions could adversely affect valuations of investment portfolio assets; and
- reputational risk may increase due to public sentiment regarding the banking industry.

Non-performing assets take significant time to resolve and adversely affect our results of operations and financial condition.

At December 31, 2011, our non-performing loans and leases were 3.38% of total loans and leases compared to 4.30% at December 31, 2010, and 4.13% at December 31, 2009, our non-performing assets (which include foreclosed real estate) were 1.70% of total assets compared to 2.57% at December 31, 2010. The allowance for loan and lease losses as a percentage of non-performing loans and leases was 78.95% as of December 31, 2011 compared to 59.34% at December 31, 2010. Non-performing assets adversely affect our net income in various ways. Until economic and market conditions improve, we expect to be exposed to losses relating to an increase in non-performing assets. We generally do not record interest income on non-performing loans or other real estate owned, thereby adversely affecting our income and increasing our loan administration costs. When we take collateral in foreclosures and similar proceedings, we are required to mark the related asset to the then fair market value of the collateral, which may ultimately result in a loss. An increase in the level of non-performing assets increases our risk profile and may impact the capital levels our regulators believe are appropriate in light of the ensuing risk profile, which could result in a request to reduce our level of non-performing assets. When we reduce problem assets through loan sales, workouts, restructurings and otherwise, decreases in the value of the underlying collateral, or in these borrowers' performance or financial condition, whether or not due to economic and market conditions beyond our control, could adversely affect our business, results of operations and financial condition. In addition, the resolution of non-performing assets requires significant commitments of time from management and our directors, which can be detrimental to the performance of their other responsibilities. There can be no assurance that we will not experience future increases in non-performing assets or that the disposition of such non-performing assets will not adversely affect our profitability.

Tightening of credit markets and liquidity risk could adversely affect our business, financial condition and results of operations.

A tightening of the credit markets or any inability to obtain adequate funds for continued loan growth at an acceptable cost could adversely affect our asset growth and liquidity position and, therefore, our earnings capability. In addition to core deposit growth, maturity of investment securities and loan and lease payments, we also rely on alternative funding sources including unsecured borrowing lines with correspondent banks, secured borrowing lines with the Federal Home Loan Bank of San Francisco and the Federal Reserve Bank of San Francisco, and public time certificates of deposits. Our ability to access these sources could be impaired by deterioration in our financial condition as well as factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations for the financial services industry or serious dislocation in the general credit markets. In the event such a disruption should occur, our ability to access these sources could be adversely affected, both as to price and

availability, which would limit, or potentially raise the cost of, the funds available to us.

We have a concentration risk in real estate related loans.

At December 31, 2011, $310 million, or 72.4% of our total loan and lease portfolio, consisted of real estate related loans. Substantially all of our real property collateral is located in our operating markets in the Central Valley in California. The continuing trend of deteriorating economic conditions in California and in our operating markets has contributed to an overall decline in commercial and residential real estate values. A continuing substantial decline in commercial and residential real estate values in our primary market areas could occur as a result of worsening economic conditions or other events including natural disasters such as earthquakes, fires, and floods. Such a decline in values could have an adverse impact on us by limiting repayment of defaulted loans through sale of commercial and residential real estate collateral and by a likely increase in the number of defaulted loans to the extent that the financial condition of our borrowers is adversely affected by

such a decline in values. The adverse effects of the foregoing matters upon our real estate portfolio could necessitate a material increase in the provision for loan and lease losses.

If our allowance for credit losses is not sufficient to cover actual loan losses, our earnings could decrease.

Our loan customers may not repay their loans according to the terms of these loans, and the collateral securing the payment of these loans may be insufficient to assure repayment. We may experience significant credit losses that could have a material adverse effect on our operating results. We make various assumptions and judgments about the collectibility 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 size of the allowance, we rely on our experience and our evaluation of economic conditions. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover future loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in our loan portfolio. Significant additions to our allowance would materially decrease our net income.

In addition, federal and state regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or recognize further loan charge-offs, based on judgments different than those we make. Any increase in our allowance or charge-offs as required by these regulatory agencies could have a negative effect on us.

Our focus on lending to small to mid-sized community-based businesses may increase our credit risk.

Commercial real estate and commercial business loans generally are considered riskier than single-family residential loans because they have larger balances to a single borrower or group of related borrowers. Commercial real estate and commercial business loans involve risks because the borrowers' ability to repay the loans typically depends primarily on the successful operation of the businesses or the properties securing the loans. Most of the Bank's commercial real estate and commercial business loans are made to small to medium sized businesses who may have a heightened vulnerability to economic conditions. Moreover, a portion of these loans have been made by us in recent years and the borrowers may not have experienced a complete business or economic cycle. Furthermore, the deterioration of our borrowers' businesses may hinder their ability to repay their loans with us, which could adversely affect our results of operations.

Fluctuations in interest rates could reduce our profitability.

We realize income primarily from the difference between interest earned on loans and securities and the interest paid on deposits and borrowings. We expect that we will periodically experience "gaps" in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this "gap" will work against us, and our earnings may be negatively affected.

We are unable to predict fluctuations of market interest rates, which are affected by the following factors:

- inflation;
- recession;
- a rise in unemployment;
- tightening money supply;
- international disorder; and
- instability in domestic and foreign financial markets.

Our asset/liability management strategy, which is designed to address the risk from changes in market interest rates and the shape of the yield curve, may not prevent changes in interest rates from having a material adverse effect on our results of operations and financial condition.

Governmental monetary policies and intervention to stabilize the U.S. financial system may affect our business and are beyond our control.

The business of banking is affected significantly by the fiscal and monetary policies of the Federal government and its agencies. Such policies are beyond our control. We are particularly affected by the policies established by the Federal Reserve Board in relation to the supply of money and credit in the United States. The instruments of monetary policy available to the Federal Reserve Board can be used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits, and this can and does have a material effect on our business.

Table of Contents

Recent legislation including the Emergency Economic Stabilization Act of 2008 (the EESA), signed into law by President Bush on October 3, 2008, and the American Recovery and Reinvestment Act of 2009 (the ARRA), signed into law by President Obama on February 17, 2009, each include programs that are intended to help stabilize the U.S. financial system. However, it is uncertain whether such legislation will sufficiently resolve the volatility of capital and credit markets or improve capital and liquidity problems confronting the financial system. The failure of the EESA or ARRA to mitigate or eliminate such volatility and problems affecting the financial markets and a continuation or worsening of current financial market conditions could limit our access to capital or sources of liquidity in amounts and at times necessary to conduct operations in compliance with applicable regulatory requirements.

Competition with other financial institutions could adversely affect our profitability.

We face vigorous competition from banks and other financial institutions, including savings institutions, finance companies and credit unions. A number of these banks and other financial institutions have substantially greater resources and lending limits, larger branch systems and a wider array of banking services. To a limited extent, we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies and insurance companies. This competition may reduce or limit our margins on banking services, reduce our market share and adversely affect our results of operations and financial condition. Additionally, we face competition primarily from other banks in attracting, developing and retaining qualified banking professionals.

Technology implementation problems or computer system failures could adversely affect us.

Our future growth prospects will be highly dependent on our ability to implement changes in technology that affect the delivery of banking services such as the increased demand for computer access to bank accounts and the availability to perform banking transactions electronically. Our ability to compete will depend upon our ability to continue to adapt technology on a timely and cost-effective basis to meet such demands. In addition, our business and operations could be susceptible to adverse effects from computer failures, communication and energy disruption, and activities such as fraud of unethical individuals with the technological ability to cause disruptions or failures of our data processing system.

Information security breaches or other technological difficulties could adversely affect us.

We cannot be certain that the continued implementation of safeguards will eliminate the risk of vulnerability to technological difficulties or failures or ensure the absence of a breach of information security. We will continue to rely on the services of various vendors who provide data processing and communication services to the banking industry. Nonetheless, if information security is compromised or other technology difficulties or failures occur at the Bank or with one of our vendors, information may be lost or misappropriated, services and operations may be interrupted and the Bank could be exposed to claims from its customers as a result.

Our controls over financial reporting and related governance procedures may fail or be circumvented.

Management regularly reviews and updates our internal control over financial reporting, disclosure controls and procedures, and corporate governance policies and procedures. We maintain controls and procedures to mitigate risks such as processing system failures or errors and customer or employee fraud, and we maintain insurance coverage for certain of these risks. Any system of controls and procedures, however well designed and operated, is based in part on certain assumptions and provides only reasonable, not absolute, assurances that the objectives of the system are met. Events could occur which are not prevented or detected by our internal controls, are not insured against, or are in excess of our insurance limits. Any failure or circumvention of our controls and procedures, or failure to comply with

regulations related to controls and procedures, could have an adverse effect on our business.

We may not be successful in raising additional capital needed in the future.

If additional capital is needed in the future as a result of losses, our business strategy or regulatory requirements, there is no assurance that our efforts to raise such additional capital will be successful or that shares sold in the future will be sold at prices or on terms equal to or better than the current market price. The inability to raise additional capital when needed or at prices and terms acceptable to us could adversely affect our ability to implement our business strategies.

The effects of legislation in response to current credit conditions may adversely affect us.

Legislation that has or may be passed at the Federal level and/or by the State of California in response to current



---

conditions affecting credit markets could cause us to experience higher credit losses if such legislation reduces the amount that the Bank's borrowers are otherwise contractually required to pay under existing loan contracts. Such legislation could also result in the imposition of limitations upon the Bank's ability to foreclose on property or other collateral or make foreclosure less economically feasible. Such events could result in increased loan and lease losses and require a material increase in the allowance for loan and lease losses.

The effects of changes to FDIC insurance coverage limits are uncertain and increased premiums may adversely affect us.

As mandated by the Dodd-Frank Act, the FDIC Board approved the final rule that implemented unlimited deposit insurance coverage on noninterest-bearing transaction accounts beginning on December 31, 2010, and ending December 31, 2012. This coverage replaces the unlimited coverage under the Transaction Account Guarantee Program (the "TAGP"). Coverage under this program is confined to noninterest-bearing accounts and interest-bearing Lawyers Trust accounts (IOLTAs). The coverage will not include other accounts, such as traditional checking or demand deposit accounts that may earn interest, NOW accounts, and money-market deposit accounts.

It is not clear how depositors will respond regarding the increase in insurance coverage. Despite the increase, some depositors may reduce the amount of deposits held at the Bank if concerns regarding bank failures persist, which could affect the level and composition of the Bank's deposit portfolio and thereby directly impact the Bank's funding costs and net interest margin. The Bank's funding costs may also be adversely affected in the event that the activities of the Federal Reserve Board and the U.S. Treasury, intended to provide liquidity for the banking system and improvement in capital markets, are curtailed or unsuccessful. Such events could reduce liquidity in the markets, thereby increasing funding costs to the Bank or reducing the availability of funds to the Bank to finance its existing operations and thereby adversely affecting our results of operations.

Increases in FDIC insurance premiums will add to our cost of operations and could have a significant impact on us. Depending on any future losses that the FDIC insurance fund may suffer due to failed institutions, there can be no assurance that there will not be additional significant premium increases in order to replenish the fund. On November 12, 2009, the FDIC announced a final rule to require most banks to prepay their estimated quarterly risk-based assessments for 2010, 2011 and 2012. This prepaid amount for the Company was $2,054,000 on December 31, 2011. The prepayments result in a nominal decrease in earnings and liquidity.

On February 7, 2011, the FDIC Board of Directors adopted the final rule, which redefined the deposit insurance assessment base as required by the Dodd-Frank Act, and makes changes to assessment rates. The final rule redefined the deposit insurance assessment base as average consolidated total assets minus average tangible equity, defined as Tier 1 capital. The final rule adopted a new assessment rate schedule effective April 1, 2011, and in lieu of dividends, other rate schedules when the reserve ratio reaches certain levels and was paid at the end of September 2011. The rule lowers overall assessment rates in order to generate the same approximate amount of revenue under the new larger base as was raised under the old base. The assessment rates in total is between 2.5 and 9 basis points on the broader base for banks in the lowest risk category, and 30 to 45 basis points for banks in the highest risk category.

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

Our securities portfolio contains whole loan private mortgage-backed securities and currently includes securities with unrecognized losses and securities that have been downgraded to below investment grade by national rating agencies. We may continue to observe declines in the fair market value of these securities. We evaluate the securities portfolio for any other-than-temporary impairment each reporting period, as required by generally accepted accounting principles, and for the year ended December 31, 2011, we recorded an other-than-temporary impairment of $31,000.

There can be no assurance, however, that future evaluations of the securities portfolio will not require us to recognize further impairment charges with respect to these and other holdings.

In addition, as a condition to membership in the Federal Home Loan Bank of San Francisco (the FHLB), we are required to purchase and hold a certain amount of FHLB stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB. At December 31, 2011, we held stock in the FHLB totaling $2,893,000. The FHLB stock held by us is carried at cost and is subject to recoverability testing under applicable accounting standards. To date, the FHLB has not discontinued the distribution of dividends on its shares. However, there can be no assurance the FHLB's dividend paying practices will continue. As of December 31, 2011, we did not recognize an impairment charge related to our FHLB stock holdings. There can be no assurance, however, that future negative changes to the financial condition of the FHLB may not require us to recognize an impairment charge with respect to such holdings.

Table of Contents

If the goodwill we have recorded in connection with our acquisitions becomes impaired, it could have an adverse impact on our earnings and capital.

At December 31, 2011, we had approximately $23,577,000 of goodwill on our balance sheet attributable to our acquisitions of the Bank of Madera County in January 2005 and Service 1st Bancorp in November 2008. In accordance with generally accepted accounting principles, our goodwill is not amortized but rather evaluated for impairment on an annual basis or more frequently if events or circumstances indicate that a potential impairment exists. Such evaluation is based on a variety of factors, including the quoted price of our common stock, market prices of the common stock of other banking organizations, common stock trading multiples, discounted cash flows, and data from comparable acquisitions. There can be no assurance that future evaluations of goodwill will not result in findings of impairment and write-downs, which could be material.

We may raise additional capital, which could have a dilutive effect on the existing holders of our common stock and adversely affect the market price of our common stock.

We are not restricted from issuing additional shares of common stock or securities that are convertible into or exchangeable for, or that represent the right to receive, common stock. We frequently evaluate opportunities to access the capital markets taking into account our regulatory capital ratios, financial condition and other relevant considerations, and subject to market conditions, we may take further capital actions. Such actions could include, among other things, the issuance of additional shares of common stock in public or private transactions in order to further increase our capital levels above the requirements for a well-capitalized institution established by the Federal bank regulatory agencies as well as other regulatory targets.

The issuance of any additional shares of common stock or securities convertible into or exchangeable for common stock or that represent the right to receive common stock, or the exercise of such securities including, without limitation, securities issued upon exercise of outstanding stock options under our stock option plans, could be substantially dilutive to shareholders of our common stock. With the exception of one major shareholder, holders of our shares of common stock have no preemptive rights that entitle holders to purchase their pro rata share of any offering of shares of any class or series and, therefore, such sales or offerings could result in increased dilution to our shareholders. The market price of our common stock could decline as a result of sales of shares of our common stock or the perception that such sales could occur.

The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive.

The stock market and, in particular, the market for financial institution stocks, has experienced significant volatility, which, in recent quarters, has reached unprecedented levels. In some cases, the markets have produced downward pressure on stock prices for certain issuers without regard to those issuers' underlying financial strength. As a result, the trading volume in our common stock may fluctuate more than usual and cause significant price variations to occur. This may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive. The low trading volume in our common shares on the NASDAQ Capital Market means that our shares may have less liquidity than other publicly traded companies. We cannot ensure that the volume of trading in our common shares will be maintained or will increase in the future.

The trading price of the shares of our common stock will depend on many factors, which may change from time to time and which may be beyond our control, including, without limitation, our financial condition, performance, creditworthiness and prospects, future sales or offerings of our equity or equity related securities, and other factors identified above in the forward-looking statement discussion under the section titled "Cautionary Statements Regarding

Forward-Looking Statements" and below. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of our common stock. Among the factors that could affect our stock price are:

- actual or anticipated quarterly fluctuations in our operating results and financial condition;
- changes in financial estimates or publication of research reports and recommendations by financial analysts or actions taken by rating agencies with respect to our common stock or those of other financial institutions;
- failure to meet analysts' revenue or earnings estimates;
- speculation in the press or investment community generally or relating to our reputation, our market area, our competitors or the financial services industry in general;
- strategic actions by us or our competitors, such as acquisitions, restructurings, dispositions or financings;

Table of Contents

- actions by our current shareholders, including sales of common stock by existing shareholders and/or directors and executive officers;
- fluctuations in the stock price and operating results of our competitors;
- future sales of our equity, equity-related or debt securities;
- changes in the frequency or amount of dividends or share repurchases;
- proposed or adopted regulatory changes or developments;
- anticipated or pending investigations, proceedings, or litigation that involves or affects us;
- trading activities in our common stock, including short-selling;
- domestic and international economic factors unrelated to our performance; and
- general market conditions and, in particular, developments related to market conditions for the financial services industry.

A significant decline in our stock price could result in substantial losses for individual shareholders.

We may not be able to maintain our historical growth rate which may adversely impact our results of operations and financial condition.

We have initiated internal asset growth programs, completed various acquisitions and opened additional offices in the past few years. We may not be able to sustain our historical rate of asset growth or may not even be able to grow at all. We may not be able to obtain the financing necessary to fund additional asset growth and may not be able to find suitable candidates for acquisition. Various factors, such as economic conditions and competition, may impede or prohibit the opening of new branch offices. Further, our inability to attract and retain experienced bankers may adversely affect our internal asset growth. A significant decrease in our historical rate of asset growth may adversely impact our results of operations and financial condition.

We may be unable to complete future acquisitions, and once complete, may not be able to integrate our acquisitions successfully.

Our growth strategy includes our desire to acquire other financial institutions. We may not be able to complete any future acquisitions and, for completed acquisitions, we may not be able to successfully integrate the operations, management, products and services of the entities we acquire. We may not realize expected cost savings or make revenue enhancements. Following each acquisition, we must expend substantial managerial, operating, financial and other resources to integrate these entities. In particular, we may be required to install and standardize adequate operational and control systems, deploy or modify equipment, implement marketing efforts in new as well as existing locations and employ and maintain qualified personnel. Our failure to successfully integrate the entities we acquire into our existing operations may adversely affect our financial condition and results of operations.

We operate in a highly regulated environment and may be adversely affected by changes in federal and local laws and regulations.

We are subject to extensive regulation, supervision and examination by federal and state banking authorities. Any change in applicable regulations or federal or state legislation could have a substantial impact on us and our operations. Additional legislation and regulations may be enacted or adopted in the future that could significantly affect our powers, authority and operations, which could have a material adverse effect on our financial condition and results of operations. Further, regulators have significant discretion and power to prevent or remedy unsafe or unsound practices or violations of laws by banks and bank holding companies in the performance of their supervisory and enforcement duties. The exercise of this regulatory discretion and power may have a negative impact on us.

We are experiencing an influx of locally based competition that could affect near term results.

Recently, several new banks have opened in our service areas. We are seeing price competition from these new banks, as they work to establish their markets. The existence of competitors, large and small, is a normal and expected part of our operations, but in responding to the particular short-term impact on business of new entrants to the marketplace, we could see a negative impact on revenue and income. Moreover, these near term impacts could be accentuated by the seasonal impact on revenue and income generated by the borrowing and deposit habits of the agricultural community that comprises a significant component of our customer base.

Our outstanding preferred stock impacts net income available to our common stockholders and earnings per common share.



---

Table of Contents

The dividends declared on our outstanding preferred stock will reduce the net income available to common stockholders and our earnings per common share. The preferred stock will also receive preferential treatment in the event of our liquidation, dissolution or winding-up.

## ITEM 2 - DESCRIPTION OF PROPERTY.

The Company owns the property on which the Main Office, a full-service branch office, is located in Clovis, California. In addition, the Company owns the property on which the Foothill Office, a full-service branch office, is located in Prather, California, the property on which the Modesto office, a full-service branch office, is located in Modesto, California, and the property on which the Kerman Office, a full-service branch office, is located in Kerman, California.

All other property is leased by the Company, including the principal executive offices in Fresno. This facility houses the Company's corporate offices, comprised of various departments, including accounting, information services, human resources, real estate department, loan servicing, credit administration, branch support operations, and compliance.

The Company continually evaluates the suitability and adequacy of the Company's offices and has a program of relocating or remodeling them as necessary to be efficient and attractive facilities. Management believes that its existing facilities are adequate for its present purposes.

Properties owned by the Bank are held without loans or encumbrances. All of the property leased is leased directly from independent parties. Management considers the terms and conditions of each of the existing leases to be in the aggregate favorable to the Company. See Note 12 of the Company's audited Consolidated Financial Statements in Item 8 of this Annual Report.

## ITEM 3 - LEGAL PROCEEDINGS.

### Regent Hotel Litigation

On May 1, 2008, Regent Hotel, LLC ("Regent") filed a lawsuit in the Superior Court of California, County of Sacramento (the "Regent Litigation"). Regent Hotel, LLC, a California limited liability company and subsidiary of Regent Development, Inc., a California corporation, filed the Regent Litigation naming as defendants First Bank, as the lead bank in a loan participation, and East West Bank and S1 Bank, which was acquired by the Bank on November 13, 2008, which are participating in the loan. Regent claims that First Bank refused to fund a construction loan draw request and that East West Bank and S1 Bank interfered in the relationship between Regent and First Bank which affected the decision by First Bank not to fund the draw request. Through its acquisition of S1 Bank, the Bank was a 9.915% participant in the amount of approximately $4,000,000. Regent filed for Chapter 11 bankruptcy in 2008. The suit asked for actual and punitive damages in excess of $10,000,000. In addition, certain contractors filed mechanics liens against Regent, under which S1 Bank was named in the complaint. These complaints have been removed to the bankruptcy court.

In 2009, First Bank purchased the Bank's participating interest in the Regent Hotel loan at a discount and indemnified the Bank against any further actions pursuant to the lawsuit. Included in the merger consideration paid by the Company to acquire Service 1st was $3,500,000 which was placed into an escrow fund to protect the Company and the Bank from all losses and liabilities that related to the loan participation and/or the Regent Litigation. Consequent to the Lead Bank buying the Bank's position, the Bank collected $1,046,000 from the escrow fund to cover the portion of the loan that was not recovered, accrued and unpaid interest and other costs.

In 2010, settlement agreements between all parties were signed and the bankruptcy court approved the settlement. The Bank was removed from the mechanics liens in 2010 after the Bank acknowledged it no longer had an interest in the property. The settlement was finalized in 2011.

In accordance with the escrow agreement, once the litigation was completely satisfied and after reimbursing the Bank for any legal and escrow costs, the escrow fund was terminated and the remaining balance was disbursed for payment to former Service 1st shareholders. At December 31, 2011, $309,520 remained unclaimed.

The Company is subject to legal proceedings and claims which arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the consolidated financial position or consolidated results of operations of the Company.

Table of Contents

None of our directors, officers, affiliates, more than 5% shareholder or any associates of these persons is a party adverse to the Company or the Bank or has a material interest adverse to the Company or the Bank in any material legal proceeding.

ITEM 4 - MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5 - MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock is listed for trading on the Nasdaq Capital Market under the ticket symbol CVCY. As of March 14, 2012, we had approximately 763 shareholders of record.

The following table shows the high and low sales prices for the common stock for each quarter as reported by NASDAQ.

Common Stock Prices

| | Qtr 1 2010 | Qtr 2 2010 | Qtr 3 2010 | Qtr 4 2010 | Qtr 1 2011 | Qtr 2 2011 | Qtr 3 2011 | Qtr 4 2011 |
|---|---|---|---|---|---|---|---|---|
| High | $6.10 | $8.25 | $6.44 | $5.25 | $6.19 | $6.95 | $6.90 | $6.25 |
| Low | $5.34 | $5.13 | $5.40 | $6.00 | $5.61 | $6.19 | $5.20 | $5.25 |

We did not pay a cash dividend in 2011 or 2010. The Company's primary source of income with which to pay cash dividends are dividends from the Bank. The Bank would not pay any dividend that would cause it to be deemed not "well capitalized" under applicable banking laws and regulations. See Note 13 in the audited Consolidated Financial Statements in Item 8 of this Annual Report.

ISSUER PURCHASES OF EQUITY SECURITIES

Not Applicable

EQUITY COMPENSATION PLAN INFORMATION

The following chart sets forth information for the year ended December 31, 2011, regarding equity based compensation plans of the Company.

| | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|---|---|---|---|

| Plan Category | (a) | (b) | (c) |
| --- | --- | --- | --- |
| Equity compensation plans approved by security holders | 511,019 | $8.56 | 368,100 |
| Equity compensation plans not approved by security holders | N/A | N/A | N/A |
| Total | 511,019 | $8.56 | 368,100 |

There were no options granted in 2011.

Table of Contents

ITEM 6 - SELECTED CONSOLIDATED FINANCIAL DATA

| | Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| (In Thousands, except per share amounts) | 2011 | 2010 | 2009 | 2008 | 2007 |
| Statements of Income | | | | | |
| Total interest income | $34,299 | $36,013 | $40,734 | $31,845 | $32,566 |
| Total interest expense | 2,942 | 4,283 | 6,627 | 7,278 | 8,058 |
| Net interest income before provision for credit losses | 31,357 | 31,730 | 34,107 | 24,567 | 24,508 |
| Provision for credit losses | 1,050 | 3,800 | 10,514 | 1,290 | 480 |
| Net interest income after provision for credit losses | 30,307 | 27,930 | 23,593 | 23,277 | 24,028 |
| Non-interest income | 6,276 | 3,721 | 5,850 | 5,190 | 4,518 |
| | 36,583 | 31,651 | 29,443 | 28,467 | 28,546 |
| Non-interest expenses | 28,245 | 28,741 | 27,531 | 20,976 | 19,099 |
| Income before (benefit from) provision for income taxes | 8,338 | 2,910 | 1,912 | 7,491 | 9,447 |
| (Benefit from) provision for income taxes | 1,861 | (369) | (676) | 2,352 | 3,167 |
| Net income | 6,477 | 3,279 | 2,588 | 5,139 | 6,280 |
| Preferred stock dividends and accretion of discount | 486 | 395 | 365 | — | — |
| Net income available to common shareholders | $5,991 | $2,884 | $2,223 | $5,139 | $6,280 |
| Basic earnings per share | $0.63 | $0.31 | $0.29 | $0.83 | $1.05 |
| Diluted earnings per share | $0.63 | $0.31 | $0.28 | $0.79 | $0.99 |
| Cash dividends declared per common share | $— | $— | $— | $0.10 | $0.10 |

| | December 31, | | | | |
|---|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2009 | 2008 | 2007 |
| Balances at end of year: | | | | | |
| Investment securities, Federal funds sold and deposits in other banks | $353,808 | $280,967 | $232,142 | $194,215 | $98,909 |
| Net loans | 415,999 | 420,583 | 449,007 | 477,015 | 337,241 |
| Total deposits | 712,986 | 650,495 | 640,167 | 635,058 | 402,562 |
| Total assets | 849,023 | 777,594 | 765,488 | 752,713 | 483,685 |
| Shareholders’ equity | 107,482 | 97,391 | 91,223 | 75,375 | 54,194 |
| Earning assets | 777,088 | 713,971 | 696,914 | 681,280 | 441,825 |
| Average balances: | | | | | |
| Investment securities, Federal funds sold and deposits in other banks | $299,935 | $231,761 | $199,425 | $125,932 | $103,253 |
| Net loans | 417,273 | 444,418 | 473,850 | 362,333 | 327,665 |
| Total deposits | 677,789 | 636,166 | 632,263 | 445,285 | 417,691 |
| Total assets | 800,178 | 758,852 | 752,509 | 541,789 | 477,321 |
| Shareholders’ equity | 103,386 | 96,174 | 83,400 | 58,251 | 51,754 |
| Earning assets | 715,862 | 672,804 | 671,906 | 492,414 | 436,564 |

Data from 2008 reflects the partial year impact of the acquisition of Service 1st Bancorp and its subsidiary, Service 1st Bank.

## ITEM 7 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

Management's discussion and analysis should be read in conjunction with the Company's audited Consolidated Financial Statements, including the Notes thereto, in Item 8 of this Annual Report.

Certain matters discussed in this report constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained herein that are not historical facts, such as statements regarding the Company's current business strategy and the Company's plans for future development and operations, are based upon current expectations. These statements are forward-looking in nature and involve a number of risks and uncertainties. Such risks and uncertainties include, but are not limited to (1) significant increases in competitive pressure in the banking industry; (2) the impact of changes in interest rates, a decline in economic conditions at the international, national or local level on the Company's results of operations, the Company's ability to continue its internal growth at historical rates, the Company's ability to maintain its net interest margin, and the quality of the Company's earning assets; (3) changes in the regulatory environment; (4) fluctuations in the real estate market; (5) changes in business conditions and inflation; (6) changes in securities markets (7) risks associated with acquisitions, relating to difficulty in integrating combined operations and related negative impact on earnings, and incurrence of substantial expenses. Therefore, the information set forth in such forward-looking statements should be carefully considered when evaluating the business prospects of the Company.

When the Company uses in this Annual Report the words “anticipate,” “estimate,” “expect,” “project,” “intend,” “commit,” “b and similar expressions, the Company intends to identify forward-looking statements. Such statements are not guarantees of performance and are subject to certain risks, uncertainties and assumptions, including those described in this Annual Report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, expected, projected, intended, committed or believed. The future results and shareholder values of the Company may differ materially from those expressed in these forward-looking statements. Many of the factors that will determine these results and values are beyond the Company's ability to control or predict. For those statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. See also the discussion of risk factors in Item 1A, “Risk Factors.”

## INTRODUCTION

Central Valley Community Bancorp (NASDAQ: CVCY) (the Company) was incorporated on February 7, 2000. The formation of the holding company offered the Company more flexibility in meeting the long-term needs of customers, shareholders, and the communities it serves. The Company currently has one bank subsidiary, Central Valley Community Bank (the Bank) and one business trust subsidiary, Service 1st Capital Trust 1. The Bank of Madera County (BMC) was merged with and into the Bank on January 1, 2005. BMC had two branches in Madera County which continue to be operated by the Bank. After the close of business on November 12, 2008, Service 1st Bancorp (Service 1st) was merged with and into the Company, and Service 1st Bank was merged with and into the Bank. Service 1st Bank had three branches in Stockton, Tracy, and Lodi which continue to be operated by the Bank. Service 1st Capital Trust 1 (the Trust) is a business trust formed for the purpose of issuing trust preferred securities. The Company succeeded to all the rights and obligations of Service 1st in connection with the acquisition of Service 1st. The Trust is a subsidiary of the Company. The Company's market area includes the central valley area from Sacramento, California to Bakersfield, California.

During 2011, we focused on asset quality and capital adequacy due to the uncertainty created by the economy. We also focused on assuring that competitive products and services were made available to our clients while adjusting to

the many new laws and regulations that affect the banking industry. In 2011, the Company relocated the existing Modesto branch, a full service office, to a more desirable location. In 2009, we opened a new full service office in Merced, California and relocated our Oakhurst office to a new smaller facility in a more desirable location. During 2008 the Company acquired Service 1st Bancorp and its banking subsidiary adding three strategically located branches and we relocated our Herndon and Fowler branch from an in-store location to a new larger facility. During 2007, we relocated our Kerman branch to a new larger facility. During 2006, the Bank opened two full service retail offices in Fresno, one in the downtown area and one in the Sunnyside area of Fresno. In 2006, the Company consolidated its administrative offices into a single location in Fresno and opened a limited service branch there. The Bank now operates 17 full-service offices. The Bank has a Real Estate Division, an Agribusiness Center and an SBA Lending Division in Fresno. All real estate related transactions are conducted and processed through the Real Estate Division, including interim construction loans for single family residences and commercial buildings. We offer permanent single family residential loans through our mortgage broker services.

Table of Contents

ECONOMIC CONDITIONS

The economy in California's Central Valley has been negatively impacted by the recession that began in 2007 and the related real estate market and the slowdown in residential construction. The recession has impacted most industries in our market area. During the past three years, housing values throughout the nation and especially in the Central Valley have decreased dramatically, which in turn has negatively affected the personal net worth of much of the population in our service area. Housing in the Central Valley continues to be relatively more affordable than the major metropolitan areas in California.

Agriculture and agricultural related businesses remain a critical part of the Central Valley's economy. The Valley's agricultural production is widely diversified, producing nuts, vegetables, fruit, cattle, dairy products, and cotton. The continued future success of agriculture related businesses is highly dependent on the availability of water and is subject to fluctuation in worldwide commodity prices and demand.

OVERVIEW

Diluted earnings per share (EPS) for the year ended December 31, 2011 was $0.63 compared to $0.31 and $0.28 for the years ended December 31, 2010, and 2009, respectively. Net income for 2011 was $6,477,000 compared to $3,279,000 and $2,588,000 for the years ended December 31, 2011, 2010 and 2009, respectively. The increase in net income and EPS was primarily driven by lower provision for credit losses, decreases in non-interest expense and increases in non-interest income, partially offset by decreases in net interest income in 2011 compared to 2010. Total assets at December 31, 2011 were $849,023,000 compared to $777,594,000 at December 31, 2010.

Return on average equity for 2011 was 6.26% compared to 3.41% and 3.10% for 2010 and 2009, respectively. Return on average assets for 2011 was 0.81% compared to 0.43% and 0.34% for 2010 and 2009, respectively. Total equity was $107,482,000 at December 31, 2011 compared to $97,391,000 at December 31, 2010. The increase in assets and equity in 2011 compared to 2010 is due to an increase in deposits and increases in other comprehensive income and retained earnings and the exercise of stock options.

Average total loans decreased $27,049,000 or 5.94% to $428,291,000 in 2011 compared to $455,340,000 in 2010. In 2011, we recorded a provision for credit losses of $1,050,000 compared to $3,800,000 in 2010 and $10,514,000 in 2009. The Company had nonperforming assets totaling $14,434,000 at December 31, 2011. Nonperforming assets included nonaccrual loans totaling $14,434,000. At December 31, 2010 nonperforming assets totaled $19,984,000 consisting of $18,561,000 in nonaccrual loans, other real estate owned of $1,325,000 and $98,000 in other assets. Net charge-offs for 2011 were $668,000 compared to $2,986,000 for 2010 and $7,537,000 for 2009. Refer to "Asset Quality" below for further information.

Key Factors in Evaluating Financial Condition and Operating Performance

As a publicly traded community bank holding company, we focus on several key factors including:

•Return to our stockholders;
•Return on average assets;
•Development of core earnings, including net interest income and non-interest income;
•Asset quality;
•Asset growth;
•Capital adequacy;
•Operating efficiency; and

•Liquidity.

Return to Our Stockholders

Our return to our stockholders is measured in a ratio that measures the return on average equity (ROE). Our ROE was 6.26% for the year ended 2011 compared to 3.41% and 3.10% for the years ended 2010 and 2009, respectively. In 2011, compared to 2010 we experienced an increase in net income and an increase in capital due to increases in retained earnings, other comprehensive income, and the exercise of stock options.

Our net income for the year ended December 31, 2011 increased $3,198,000 compared to 2010 and increased $691,000 for 2010 compared to 2009. During 2011 net income increased primarily due to a decrease in the provision for credit losses, decreases in non-interest expense and increases in non-interest income, partially offset by decreases in net interest

Table of Contents

income in 2011 compared to 2010. Net interest income decreased because of decreases in loan and investment income, partially offset by decreases in interest expense on deposits. Non-interest income increased due to an Other-Than-Temporary-Impairment (OTTI) charge of $31,000 in 2011, compared to $1,587,000 in 2010, an increase in net realized gains on sales and calls of investment securities of $489,000, a $142,000 gain related to the final distribution of the Service 1st escrow account, an $85,000 gain related to the collection of life insurance proceeds, and an increase in gain of other real estate owned of $439,000.

Non-interest expenses decreased in 2011 compared to 2010 primarily due to decrease in OREO expenses of $1,056,000, legal fees of $160,000, and regulatory assessment of $346,000, partially offset by increases in salaries and employee benefits of $891,000. During 2011, our net interest margin (NIM) decreased 32 basis points compared to 2010. Basic EPS was $0.63 for 2011 compared to $0.31 and $0.29 for 2010 and 2009, respectively. Diluted EPS was $0.63 for 2011 compared to $0.31 and $0.28 for 2010 and 2009, respectively. The increase in EPS in 2011 was due primarily to the increase in net income.

Return on Average Assets

Our return on average assets (ROA) is a ratio that measures our performance compared with other banks and bank holding companies. Our ROA for the year ended 2011 was 0.81% compared to 0.43% and 0.34% for the years ended December 31, 2010 and 2009, respectively. The 2011 increase in ROA is due to the increase in net income, notwithstanding an increase in average assets. Annualized ROA for our peer group was 0.37% at December 31, 2011. Peer group information from SNL Financial data includes bank holding companies in central California with assets from $300M to $950M that are not subchapter S corporations.

Development of Core Earnings

Over the past several years, we have focused on not only our net income, but improving the consistency of our core earnings in order to create more predictable future earnings and reduce the effect of changes in our operating environment on our net income. Specifically, we have focused on net interest income through a variety of processes, including increases in average interest-earning assets through loan generation and retention. We minimized the effects of the recent interest rate decline on our net interest margin by focusing on core deposits and managing the cost of funds. Our net interest margin (fully tax equivalent basis) was 4.63% for the year ended December 31, 2011, compared to 4.95% and 5.31% for the years ended December 31, 2010 and 2009, respectively. The decrease in net interest margin compared to 2010 is principally due to a decrease in our yield on earning assets which was greater than the decrease in our cost of funds. In comparing the two periods, the effective yield on total earning assets decreased 55 basis points, while the cost of total interest-bearing liabilities decreased 27 basis points and the cost of total deposits decreased 19 basis points. Our cost of total deposits in 2011 was 0.39% compared to 0.58% for the same period in 2010 and 0.93% for the year ended December 31, 2009. Our net interest income before provision for credit losses decreased $373,000 or 1.18% to $31,357,000 for the year ended 2011 compared to $31,730,000 and $34,107,000 for the years ended 2010 and 2009, respectively.

Our non-interest income is generally made up of service charges and fees on deposit accounts, fee income from loan placements, appreciation in cash surrender value of bank owned life insurance, and net gains from sales and calls of investment securities. Non-interest income in 2011 increased $2,555,000 or 68.66% to $6,276,000 compared to $3,721,000 in 2010 and $5,850,000 in 2009. Customer service charges decreased $322,000 or 9.98% to $2,903,000 in 2011 compared to $3,225,000 and $3,509,000 in 2010 and 2009, respectively. Further detail on non-interest income is provided below.

Asset Quality

For all banks and bank holding companies, asset quality has a significant impact on the overall financial condition and results of operations. Asset quality is measured in terms of percentage of total loans and total assets, and is a key element in estimating the future earnings of a company. Total nonperforming assets were $14,434,000 and $19,984,000 at December 31, 2011 and 2010, respectively. Nonperforming assets included nonaccrual loans totaling $14,434,000 or 3.38% of gross loans as of December 31, 2011 and $18,561,000 or 4.30% of gross loans as of December 31, 2010. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on nonaccrual status until such time as management has determined that the loans are likely to remain current in future periods.

Asset Growth

As revenues from both net interest income and non-interest income are a function of asset size, the continued growth in assets has a direct impact in increasing net income and therefore ROE and ROA. The majority of our assets are loans and investment securities, and the majority of our liabilities are deposits, and therefore the ability to generate deposits as a funding

source for loans and investments is fundamental to our asset growth. Total assets increased 9.19% during 2011 to $849,023,000 as of December 31, 2011 from $777,594,000 as of December 31, 2010. Total gross loans decreased 0.97% to $427,395,000 as of December 31, 2011, compared to $431,597,000 at December 31, 2010. Total investment securities and Federal funds sold increased 71.60% to $329,341,000 as of December 31, 2011 compared to $191,925,000 as of December 31, 2010. Total deposits increased 9.61% to $712,986,000 as of December 31, 2011 compared to $650,495,000 as of December 31, 2010. Our loan to deposit ratio at December 31, 2011 was 59.94% compared to 66.35% at December 31, 2010. The loan to deposit ratio of our peers was 74.42% at December 31, 2011.

Capital Adequacy

At December 31, 2011, we had a total capital to risk-weighted assets ratio of 17.49%, a Tier 1 risk-based capital ratio of 16.20% and a leverage ratio of 10.13%. At December 31, 2010, we had a total capital to risk-weighted assets ratio of 15.42%, a Tier 1 risk-based capital ratio of 14.16% and a leverage ratio of 9.48%. At December 31, 2011, on a stand-alone basis, the Bank had a total risk-based capital ratio of 17.31%, a Tier 1 risk based capital ratio of 16.02% and a leverage ratio of 10.01%. At December 31, 2010, the Bank had a total risk-based capital ratio of 15.19%, Tier 1 risk-based capital of 13.92% and a leverage ratio of 9.32%. The improvement in 2011 is due to an increase in risk adjusted capital while risk weighted assets decreased. Note 13 of the audited Consolidated Financial Statements provides more detailed information concerning the Company’s capital amounts and ratios.

Operating Efficiency

Operating efficiency is the measure of how efficiently earnings before taxes are generated as a percentage of revenue. A lower ratio represents greater efficiency. The Company’s efficiency ratio (operating expenses, excluding amortization of intangibles and foreclosed property expense, divided by net interest income plus non-interest income, excluding net gains and losses from sale of securities) was 75.67% for 2011 compared to 73.53% for 2010 and 67.31% for 2009. The decline in the efficiency ratio in 2011 and 2010 is due to an increase in operating expenses and a decrease in net interest income. The efficiency ratio in 2009 improved as compared to 2008 due to an increase in net interest income and non-interest income. The Company’s net interest income before provision for credit losses plus non-interest income increased 6.15% to $37,633,000 in 2011 compared to $35,451,000 in 2010 and $39,957,000 in 2009, while operating expenses decreased 1.73% in 2011. Operating expenses increased 4.40% in 2010, and 31.25% in 2009.

Liquidity

Liquidity management involves our ability to meet cash flow requirements arising from fluctuations in deposit levels and demands of daily operations, which include providing for customers’ credit needs, funding of securities purchases, and ongoing repayment of borrowings. Our liquidity is actively managed on a daily basis and reviewed periodically by our management and Directors’ Asset/Liability Committee. This process is intended to ensure the maintenance of sufficient funds to meet our needs, including adequate cash flow for off-balance sheet commitments. Our primary sources of liquidity are derived from financing activities which include the acceptance of customer and, to a lesser extent, broker deposits, Federal funds facilities and advances from the Federal Home Loan Bank of San Francisco. We have available unsecured lines of credit with correspondent banks totaling approximately $44,000,000 and secured borrowing lines of approximately $125,122,000 with the Federal Home Loan Bank. These funding sources are augmented by collection of principal and interest on loans, the routine maturities and pay downs of securities from our investment securities portfolio, the stability of our core deposits, and the ability to sell investment securities. Primary uses of funds include origination and purchases of loans, withdrawals of and interest payments on deposits, purchases of investment securities, and payment of operating expenses.

We had liquid assets (cash and due from banks, interest-earning deposits in other banks, Federal funds sold and available-for-sale securities) totaling $373,217,000 or 43.96% of total assets at December 31, 2011 and $292,324,000 or 37.59% of total assets as of December 31, 2010.

## RESULTS OF OPERATIONS

### Net Income

Net income was $6,477,000 in 2011 compared to $3,279,000 and $2,588,000 in 2010 and 2009, respectively. Basic earnings per share was $0.63, $0.31, and $0.29 for 2011, 2010, and 2009, respectively. Diluted earnings per share was $0.63, $0.31, and $0.28 for 2011, 2010 and 2009, respectively. ROE was 6.26% for 2011 compared to 3.41% for 2010 and 3.10% for 2009. ROA for 2011 was 0.81% compared to 0.43% for 2010 and 0.34% for 2009.

Table of Contents

The increase in net income for 2011 compared to 2010 can be attributed to the decrease in the provision for credit losses and an increase in non-interest income, partially offset by decrease in interest income and increase in provision from income taxes. The decrease in net interest income for 2010 compared to 2009 was due primarily to the 36 basis point reduction in the net interest margin.

Interest Income and Expense

Net interest income is the most significant component of our income from operations. Net interest income (the interest rate spread) is the difference between the gross interest and fees earned on the loan and investment portfolios and the interest paid on deposits and other borrowings. Net interest income depends on the volume of and interest rate earned on interest-earning assets and the volume of and interest rate paid on interest-bearing liabilities.

The following table sets forth a summary of average balances with corresponding interest income and interest expense as well as average yield and cost information for the periods presented. Average balances are derived from daily balances, and nonaccrual loans are not included as interest-earning assets for purposes of this table.

Table of Contents

SCHEDULE OF AVERAGE BALANCES AND AVERAGE YIELDS AND RATES

| (Dollars in thousands) | Year Ended December 31, 2011 | | | Year Ended December 31, 2010 | | | Year Ended December 31, 2009 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Average Balance | Interest Income/ Expense | Average Interest Rate | Average Balance | Interest Income/ Expense | Average Interest Rate | Average Balance | Interest Income/ Expense | Average Interest Rate |
| ASSETS | | | | | | | | | |
| Interest-earning deposits in other banks | $73,016 | $187 | 0.26 % | $42,047 | $110 | 0.26 % | $3,008 | $8 | 0.27 % |
| Securities | | | | | | | | | |
| Taxable securities | 150,559 | 4,548 | 3.02 % | 124,163 | 5,472 | 4.41 % | 114,465 | 7,701 | 6.73 % |
| Non-taxable securities (1) | 75,665 | 5,248 | 6.94 % | 64,838 | 4,605 | 7.10 % | 64,325 | 4,632 | 7.20 % |
| Total investment securities | 226,224 | 9,796 | 4.33 % | 189,001 | 10,077 | 5.33 % | 178,790 | 12,333 | 6.90 % |
| Federal funds sold | 695 | 2 | 0.29 % | 713 | 2 | 0.28 % | 17,627 | 48 | 0.27 % |
| Total securities | 299,935 | 9,985 | 3.33 % | 231,761 | 10,189 | 4.40 % | 199,425 | 12,389 | 6.21 % |
| Loans (2) (3) | 412,969 | 26,098 | 6.32 % | 437,959 | 27,390 | 6.25 % | 469,341 | 29,920 | 6.37 % |
| Federal Home Loan Bank stock | 2,958 | 9 | 0.30 % | 3,084 | 11 | 0.36 % | 3,140 | 7 | 0.22 % |
| Total interest-earning assets | 715,862 | $36,092 | 5.04 % | 672,804 | $37,590 | 5.59 % | 671,906 | $42,316 | 6.30 % |
| Allowance for credit losses | (11,018 ) | | | (10,922 ) | | | (8,608 ) | | |
| Nonaccrual loans | 15,322 | | | 17,381 | | | 13,117 | | |
| Other real estate owned | 217 | | | 2,972 | | | 2,553 | | |
| Cash and due from banks | 17,977 | | | 16,479 | | | 17,401 | | |
| Bank premises and equipment | 5,788 | | | 6,089 | | | 6,629 | | |
| Other non-earning assets | 56,030 | | | 54,049 | | | 49,511 | | |
| Total average assets | $800,178 | | | $758,852 | | | $752,509 | | |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | | | | | |
| Interest-bearing liabilities: | | | | | | | | | |
| Savings and NOW accounts | $154,765 | $368 | 0.24 % | $142,350 | $498 | 0.35 % | $131,818 | $771 | 0.58 % |
| Money market accounts | 174,049 | 692 | 0.40 % | 157,761 | 1,036 | 0.66 % | 136,104 | 1,262 | 0.93 % |
| Time certificates of deposit, under $100,000 | 70,111 | 688 | 0.98 % | 69,066 | 866 | 1.25 % | 90,614 | 1,922 | 2.12 % |
| Time certificates of deposit, $100,000 and over | 96,620 | 914 | 0.95 % | 114,043 | 1,313 | 1.15 % | 120,579 | 1,912 | 1.59 % |
| Total interest-bearing deposits | 495,545 | 2,662 | 0.54 % | 483,220 | 3,713 | 0.77 % | 479,115 | 5,867 | 1.22 % |
| Other borrowed funds | 10,265 | 280 | 2.73 % | 19,634 | 570 | 2.90 % | 29,987 | 760 | 2.53 % |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Total interest-bearing liabilities | 505,810 | $2,942 | 0.58 % | 502,854 | $4,283 | 0.85 % | 509,102 | $6,627 | 1.30 % |
| Non-interest bearing demand deposits | 182,244 | | | 152,946 | | | 153,148 | | |
| Other liabilities | 8,738 | | | 6,878 | | | 6,859 | | |
| Shareholders’ equity | 103,386 | | | 96,174 | | | 83,400 | | |
| Total average liabilities and shareholders’ equity | $800,178 | | | $758,852 | | | $752,509 | | |
| Interest income and rate earned on average earning assets | | $36,092 | 5.04 % | | $37,590 | 5.59 % | | $42,316 | 6.30 % |
| Interest expense and interest cost related to average interest-bearing liabilities | | 2,942 | 0.58 % | | 4,283 | 0.85 % | | 6,627 | 1.30 % |
| Net interest income and net interest margin (4) | | $33,150 | 4.63 % | | $33,307 | 4.95 % | | $35,689 | 5.31 % |

(1) Calculated on a fully tax equivalent basis, which includes Federal tax benefits relating to income earned on municipal bonds totaling $1,784, $1,566, and $1,575 in 2011, 2010, and 2009, respectively.

(2) Loan interest income includes loan fees of $399 in 2011, $460 in 2010, and $544 in 2009.

(3) Average loans do not include nonaccrual loans.

(4) Net interest margin is computed by dividing net interest income by total average interest-earning assets.

Interest and fee income from loans decreased $1,292,000 or 4.72% in 2011 compared to 2010. Interest and fee income decreased $2,530,000 or 8.46% in 2010 compared to 2009. The decrease in 2011 is attributable to a decrease in average total loans outstanding combined with a 7 basis point decrease in the yield on loans. The decrease in 2010 is attributable to a decrease in average total loans outstanding and a 12 basis point decrease in yield on loans in 2010 compared to 2009. Average total loans for 2011 decreased $27,049,000 to $428,291,000 compared to $455,340,000 for 2010 and $482,458,000 for 2009. The yield on loans for 2011 was 6.32% compared to 6.25% and 6.37% for 2010 and 2009, respectively.

Interest income from total investments, (total investments include investment securities, Federal funds sold, interest-bearing deposits in other banks, and other securities) not on a fully tax equivalent basis, decreased $422,000 or 4.89% in 2011 compared to 2010 primarily due to a $68,174,000 increase in the average balance to $299,935,000 in 2011 compared to $231,761,000 in 2010, coupled with a decrease in yield on investments of 107 basis points. In 2010, total investment income decreased $2,191,000 or 20.26% from 2009 primarily due to a 16.21% increase in the average balances of these investments and a 181 basis point increase in the yields earned. Average total investments for 2010 were $231,761,000 compared to $199,425,000 for 2009.

A significant portion of the investment portfolio is mortgage-backed securities (MBS) and collateralized mortgage obligations (CMOs). At December 31, 2011, we held $211,942,000 or 64.54% of the total market value of the investment portfolio in MBS and CMOs with an average yield of 2.90%. We invest in Collateralized Mortgage Obligations (CMO) and Mortgage Backed Securities, (MBS) as part of the overall strategy to increase our net interest margin. CMOs and MBS by their nature react to changes in interest rates. In a normal declining rate environment, prepayments from MBS and CMOs would be expected to increase and the expected life of the investment would be expected to shorten. Conversely, if interest rates increase, prepayments normally would be expected to decline and the average life of the MBS and CMOs would be expected to extend. However, in the current economic environment, prepayments may not behave according to historical norms. Premium amortization and discount accretion of these investments affects our net interest income. Our management monitors the prepayment speed of these investments and adjusts premium amortization and discount accretion based on several factors. These factors include the type of investment, the investment structure, interest rates, interest rates on new mortgage loans, expectation of interest rate changes, current economic conditions, the level of principal remaining on the bond, the bond coupon rate, the bond origination date, and volume of available bonds in market. The calculation of premium amortization and discount accretion is by nature inexact, and represents management’s best estimate of principal pay downs inherent in the total investment portfolio.

The net of tax effect value of the change in market value of the available-for-sale investment portfolio was a gain of $4,124,000 and is reflected in the Company’s equity. At December 31, 2011, the average life of the investment portfolio was five years and the market value reflected a pre-tax gain of $7,008,000. Management reviews market value declines on individual investment securities to determine whether they represent other-than-temporary impairment (OTTI) and recorded a $31,000 OTTI loss for the year ended December 31, 2011. Future deterioration in the market values of our investment securities may require the Company to recognize additional OTTI losses.

A component of the Company’s strategic plan has been to use its investment portfolio to offset, in part, its interest rate risk relating to variable rate loans. Measured at December 31, 2011, an immediate rate increase of 200 basis points would result in an estimated decrease in the market value of the investment portfolio by approximately $26,725,000. Conversely, with an immediate rate decrease of 200 basis points, the estimated increase in the market value of the investment portfolio would be $32,215,000. The modeling environment assumes management would take no action during an immediate shock of 200 basis points. The likelihood of immediate changes of 200 basis points is contrary to expectation, as evidenced by the historical changes in interest rates that occurred in 2007 and 2008, which were in 25, 50 and 75 basis point increments. However, the Company uses those increments to measure its interest rate risk in

accordance with regulatory requirements and to measure the possible future risk in the investment portfolio. For further discussion of the Company's market risk, refer to Quantitative and Qualitative Disclosures about Market Risk.

Management's review of all investments before purchase includes an analysis of how the security will perform under several interest rate scenarios to monitor whether investments are consistent with our investment policy. The policy addresses issues of average life, duration, and concentration guidelines, prohibited investments, impairment, and prohibited practices.

Total interest income in 2011 decrease $1,714,000 to $34,299,000 compared to $36,013,000 in 2010 and $40,734,000 in 2009. The decrease was due to the 55 basis point decrease in the tax equivalent yield on average interest earning assets and a change in the mix of interest earning assets. The yield on interest earning assets decreased to 5.04% for the year ended December 31, 2011 from 5.59% for the year ended December 31, 2010. Average interest earning assets increased to $715,862,000 for the year ended December 31, 2011 compared to $672,804,000 for the year ended December 31, 2010.

Average interest-earning deposits in other banks increased $30,969,000 comparing 2011 to 2010. Average yield on these deposits was 0.26%. Average investments increased $37,223,000 but the tax equivalent yield on average investments decreased 100 basis points. Average loans decreased $27,049,000 and the yield on average loans decreased 7 basis points.

The decrease in total interest income in 2010 was due to the 71 basis point decrease in the tax equivalent yield on average interest earning assets and a change in the mix of interest earning assets. The yield on interest-earning assets decreased to 5.59% for the year ended December 31, 2010 from 6.30% for the year ended December 31, 2009. Average interest-earning assets increased to $672,804,000 for the year ended December 31, 2010 compared to $671,906,000 for the year ended December 31, 2009.

Interest expense on deposits in 2011 decreased $1,051,000 or 28.31% to $2,662,000 compared to $3,713,000 in 2010 and $5,867,000 in 2009. The decrease in interest expense in 2011 compared to 2010 was primarily due to the repricing of interest-bearing deposits which decreased 23 basis points to 0.54% in 2011 from 0.77% in 2010. This decrease was partially offset by a $12,325,000 or 2.55% increase in average interest-bearing deposits. The decrease in interest expense in 2010 compared to 2009 was due to repricing of interest-bearing deposits, which decreased 45 basis points to 0.77% in 2010 from1.22% in 2009, as a result of the decreases in the Federal funds interest rate. Average interest-bearing deposits were $495,545,000 for 2011 compared to $483,220,000 and $479,115,000 for 2010 and 2009, respectively. The increases in average interest-bearing deposits in 2010 and 2009 were the result of our own organic growth.

Average other borrowings decreased to $10,265,000 with an effective rate of 2.73% for 2011 compared to $19,634,000 with an effective rate of 2.90% for 2010. In 2009, the average other borrowings were $29,987,000 with an effective rate of 2.53%. Included in other borrowings are the junior subordinated deferrable interest debentures acquired from Service 1st, advances on lines of credit and advances from the Federal Home Loan Bank (FHLB). The FHLB advances are fixed rate short-term and long-term borrowings. Advances were utilized as part of a leveraged strategy in the first quarter of 2008 to purchase investment securities. The effective rate of the FHLB advances was 3.59% for 2011 and 3.20% for 2010 and 3.08% for 2009.

The cost of all of our interest-bearing liabilities decreased 27 basis points to 0.58% for 2011 compared to 0.85% for 2010 and 1.30% for 2009. The cost of total deposits decreased to 0.39% for the year ended December 31, 2011 compared to 0.58% and 0.93% for the years ended December 31, 2010 and 2009, respectively. Average demand deposits increased 19.16% to $182,244,000 in 2011 compared to $152,946,000 for 2010 and $153,148,000 for 2009. The ratio of non-interest demand deposits to total deposits increased to 26.89% for 2011 compared to 24.04% and 24.22% for 2010 and 2009, respectively.

Net Interest Income before Provision for Credit Losses

Net interest income before provision for credit losses for 2011 decreased $373,000 or 1.18% to $31,357,000 compared to $31,730,000 for 2010 and $34,107,000 for 2009. The decrease in 2011 was due to the 32 basis point decrease in our net interest margin (NIM). Yield on interest earning assets decreased 55 basis points while the effective rate on interest bearing liabilities only decreased 27 basis points. The change in the mix of average interest earning assets also affected NIM. Interest-earning deposits in other banks and investment securities, which tend to have lower effective yields, increased while higher yielding loans decreased as previously discussed. Net interest income before provision for credit losses decreased $2,377,000 in 2010 compared to 2009 mainly due to the 36 basis point decrease in our net interest margin (NIM). Average interest-earning assets were $715,862,000 for the year ended December 31, 2011 with a net interest margin (NIM) of 4.63% compared to $672,804,000 with a NIM of 4.95% in 2010, and $671,906,000 with a NIM of 5.31% in 2009. For a discussion of the repricing of our assets and liabilities, refer to Quantitative and Qualitative Disclosure about Market Risk.

Provision for Credit Losses

We provide for probable credit losses by a charge to operating income based upon the composition of the loan portfolio, delinquency levels, losses and nonperforming assets, economic and environmental conditions and other factors which, in management's judgment, deserve recognition in estimating credit losses. Loans are charged off when they are considered uncollectible or of such little value that continuance as an active earning bank asset is not warranted.

The establishment of an adequate credit allowance is based on both an accurate risk rating system and loan portfolio management tools. The Board has established initial responsibility for the accuracy of credit risk grades with the individual credit officer. The grading is then submitted to the Chief Credit Administrator (CCA), who reviews the grades for accuracy and gives final approval. The CCA is not involved in loan originations. The risk grading and reserve allocation is analyzed quarterly by the CCA and the Board and at least annually by a third party credit reviewer and by various regulatory agencies.

Table of Contents

Quarterly, the CCA sets the specific reserve for all adversely risk-graded credits. This process includes the utilization of loan delinquency reports, classified asset reports, and portfolio concentration reports to assist in accurately assessing credit risk and establishing appropriate reserves. Reserves are also allocated to credits that are not impaired.

The allowance for credit losses is reviewed at least quarterly by the Board's Audit/Compliance Committee and by the Board of Directors. Reserves are allocated to loan portfolio categories using percentages which are based on both historical risk elements such as delinquencies and losses and predictive risk elements such as economic, competitive and environmental factors. We have adopted the specific reserve approach to allocate reserves to each impaired asset for the purpose of estimating potential loss exposure. Although the allowance for credit losses is allocated to various portfolio categories, it is general in nature and available for the loan portfolio in its entirety. Additions may be required based on the results of independent loan portfolio examinations, regulatory agency examinations, or our own internal review process. Additions are also required when, in management's judgment, the allowance does not properly reflect the portfolio's probable loss exposure.

The allocation of the allowance for credit losses is set forth below:

| Loan Type (Dollars in thousands) | December 31, 2011 | % of Total Loans | | December 31, 2010 | % of Total Loans | |
|---|---|---|---|---|---|---|
| Commercial: | | | | | | |
| Commercial and industrial | $1,924 | 18.3 | % | $2,229 | 18.8 | % |
| Agricultural land and production | 342 | 7.0 | % | 208 | 4.8 | % |
| Real estate: | | | | | | |
| Owner occupied | 1,578 | 26.4 | % | 1,978 | 25.9 | % |
| Real estate construction and other land loans | 2,954 | 7.7 | % | 1,791 | 7.4 | % |
| Commercial real estate | 2,043 | 14.6 | % | 1,387 | 14.7 | % |
| Agricultural real estate | 489 | 9.9 | % | 466 | 10.3 | % |
| Other real estate | 91 | 1.8 | % | 214 | 1.9 | % |
| Total real estate | 7,155 | 60.4 | % | 5,836 | 60.2 | % |
| Consumer: | | | | | | |
| Equity loans and lines of credit | 1,419 | 12.0 | % | 1,975 | 13.6 | % |
| Consumer and installment | 417 | 2.3 | % | 528 | 2.6 | % |
| Unallocated reserves | 139 | | | 238 | | |
| Total allowance for credit losses | $11,396 | | | $11,014 | | |

Loans are charged to the allowance for credit losses when the loans are deemed uncollectible. It is the policy of management to make additions to the allowance so that it remains adequate to cover all probable loan charge-offs that exist in the portfolio at that time. In 2010 enhanced methodology enabled us to assign qualitative and quantitative factors (Q factors) to each loan category resulting in a decrease in unallocated reserves. Q factors include reserves held for the effects of lending policies, economic trends, and portfolio trends along with other dynamics which may cause additional stress to the portfolio.

Managing credits identified through the risk evaluation methodology includes developing a business strategy with the customer to mitigate our potential losses. Management continues to monitor these credits with a view to identifying as early as possible when, and to what extent, additional provisions may be necessary.

The provisions for credit losses in 2011, 2010 and 2009 were $1,050,000, $3,800,000, and $10,514,000, respectively. These provisions are primarily the result of our assessment of the overall adequacy of the allowance for credit losses

considering a number of factors as discussed in the “Allowance for Credit Losses” section below. During the year ended December 31, 2011, the Company had net charge offs totaling 668,000 compared to 2,986,000 and 7,537,000 for the same periods in 2010 and 2009, respectively. The decrease in provision for credit losses in 2011 compared to 2010 resulted from a decrease in the level of outstanding loans and a decrease in net charge offs. The net charge off ratio, which reflects net charge-offs to average loans, was 0.16%, 0.66% and 1.56% for 2011, 2010, and 2009, respectively.

Nonperforming loans were $14,434,000 and $18,561,000 at December 31, 2011 and 2010, respectively. Nonperforming loans as a percentage of total loans were 3.38% at December 31, 2011 compared to 4.30% at December 31, 2010. There was no other real estate owned at December 31, 2011 compared to $1,325,000 net of a valuation allowance of $309,000 at December 31, 2010 and $2,832,000 net of a valuation allowance of $356,000 in 2009.

Losses in the real estate segments of the loan portfolio in 2011 decreased compared to 2010. With real estate appraised values reflecting lower levels, additions to the reserves were required. We had loans past due, not including non accrual loans, totaling $1,741,000 at December 31, 2011 compared to $3,421,000 at December 31, 2010. Losses in the loan portfolio and non-accruing balances remain elevated relative to historical periods and an increase in the level of charge-offs and the number and dollar volume of past due and nonperforming loans may result in further provisions to the allowance for credit losses.

We believe the significant economic downturn that has continued throughout 2011 has had a considerable impact on the ability of certain borrowers to satisfy their obligations, resulting in loan downgrades and corresponding increases in credit loss provisions. Additionally, we estimate the impact certain economic factors will have on various credits within the portfolio. Negative economic trends contributed substantially to increases in the required allowance to cover probable losses in the loan portfolio resulting in additional provisions.

We anticipate weakness in economic conditions on national, state and local levels to continue. Continued economic pressures may negatively impact the financial condition of borrowers to whom the Company has extended credit and as a result we may be required to make further significant provisions to the allowance for credit losses in the future. We have been and will continue to be proactive in looking for signs of deterioration within the loan portfolio in an effort to manage credit quality and work with borrowers where possible to mitigate any further losses.

As of December 31, 2011, we believe, based on all current and available information, the allowance for credit losses is adequate to absorb current estimable losses within the loan portfolio. However, no assurance can be given that we may not sustain charge-offs which are in excess of the allowance in any given period. Refer to “Allowance for Credit Losses” below for further information.

Net Interest Income after Provision for Credit Losses

Net interest income, after the provision for credit losses of $1,050,000 in 2011, $3,800,000 in 2010, and $10,514,000 in 2009, was $30,307,000 for 2011 compared to $27,930,000 and $23,593,000 for 2010 and 2009, respectively.

Non-Interest Income

Non-interest income is comprised of customer service charges, gains on sales and calls of investment securities, income from appreciation in cash surrender value of bank owned life insurance, loan placement fees, Federal Home Loan Bank dividends, and other income. Non-interest income was $6,276,000 in 2011 compared to $3,721,000 and $5,850,000 in 2010 and 2009, respectively. The $2,555,000 or 68.66% increase in non-interest income was due to increases in gains on sales and calls of investment securities, a gain on disposal of other real estate owned, and a decrease in other-than-temporary impairment write down on certain investment securities. The $2,129,000 decrease in non-interest income comparing 2010 to 2009 was due to decreases in gains on sales and calls of investment securities, an other-than-temporary impairment write down on certain investment securities, and a decrease in customer service charges.

Customer service charges decreased $322,000 to $2,903,000 in 2011 compared to $3,225,000 in 2010 and $3,509,000 in 2009. The decrease from 2011 to 2010 and 2010 to 2009 is mainly due to decreases in overdraft fee income.

During the year ended December 31, 2011, we realized net gain on sales and calls of investment securities of $298,000 from sales and calls of securities. In 2010 we realized a net loss of $191,000 compared to a net gain of $766,000 in 2009 from sales and calls of securities. In 2009, investment securities that had been marked to market when we acquired Service 1st were subsequently called at par value resulting in gains. For the year ended December 31, 2011, we realized a $31,000 other-than-temporary impairment write down on certain investment

securities. See Footnote 3 to the audited Consolidated Financial Statements for more detail.

Income from the appreciation in cash surrender value of bank owned life insurance (BOLI) totaled $382,000 in 2011 compared to $392,000 and $391,000 in 2010 and 2009, respectively. The Bank's salary continuation and deferred compensation plans and the related BOLI are used as a retention tool for directors and key executives of the Bank.

We earn loan placement fees from the brokerage of single-family residential mortgage loans provided for the convenience of our customers. Loan placement fees decreased $26,000 in 2011 to $274,000 compared to $300,000 in 2010 and $231,000 in 2009. Fees were higher in 2011 and 2010, compared to 2009, as refinancing and new mortgage activity increased due to the historically low mortgage rates, a decline in housing values and first time home buyer tax incentives.

Table of Contents

The Bank holds stock from the Federal Home Loan Bank in relationship with its borrowing capacity and generally receives quarterly dividends. As of December 31, 2011 we held $2,893,000 in FHLB stock compared to $3,050,000 at December 31, 2010. Dividends in 2011 decreased to $9,000 compared to $11,000 in 2010 and $7,000 in 2009.

Other income increased to $1,826,000 in 2011 compared to $1,395,000 and $1,246,000 in 2010 and 2009, respectively. The period-to-period increases in 2011 compared to 2010 and 2009 were due to an increase in electronic funds transfer fee income, a $142,000 gain related to the final distribution of the Service 1st escrow account, and an $85,000 gain related to the collection of life insurance proceeds.

Non-Interest Expenses

Salaries and employee benefits, occupancy, regulatory assessments, data processing expenses, and professional services are the major categories of non-interest expenses. Non-interest expenses decreased $496,000 or 1.73% to $28,245,000 in 2011 compared to $28,741,000 in 2010, which was an increase of $1,210,000 in 2010 compared to $27,531,000 in 2009.

Our efficiency ratio, measured as the percentage of non-interest expenses (exclusive of amortization of core deposit intangibles and other real estate owned expenses) to net interest income before provision for credit losses plus non-interest income (exclusive of realized gains or losses on sale and calls of investments) was 75.67% for 2011 compared to 73.53% for 2010 and 67.31% for 2009. The decline in the efficiency ratio in 2011 resulted from an increase in operating expense and a decrease in net interest income. Our efficiency ratio deteriorated in 2010 compared to 2009 due to a 112.77% decrease in net interest income plus non-interest income.

Salaries and employee benefits increased 891,000 or 5.99% to $15,762,000 in 2011 compared to $14,871,000 in 2010 and $13,926,000 in 2009. The increase in salaries and employee benefits for the 2011 period can be attributed to normal cost increases. Full time equivalents were 210 at December 31, 2011 compared to 217 at December 31, 2010. The increase in salaries and employee benefits in 2010 compared to 2009 can be attributed to the addition of personnel in connection with the expansion of offices in Modesto and Merced and other new positions along with normal cost increases.

At December 31, 2011 we had two share based compensation plans under which compensation expense is recognized based on the estimated fair value of the awards at the date of the grant. The Central Valley Community Bancorp 2000 Stock Option Plan (2000 Plan) for which 416,769 shares remain reserved for issuance for options already granted under incentive and nonstatutory agreements. This plan expired in November 2010 and no new options will be granted under this plan. The Central Valley Community Bancorp 2005 Omnibus Incentive Plan (2005 Plan) provides for awards in the form of incentive stock options, non-statutory stock options, stock appreciation rights, and restricted stock. Currently under the 2005 Plan, there are 94,250 shares reserved for issuance for options already granted to employees and directors.

The Company bases the fair value of the options previously granted on the date of grant using a Black-Scholes Merton option pricing model that uses assumptions based on expected option life, the level of estimated forfeitures, expected stock volatility and the risk-free interest rate. Stock volatility is based on the historical volatility of the Company's stock. The risk-free rate is based on the U.S. Treasury yield curve and the expected term of the options. The expected term of the options represents the period that the Company's options are expected to be outstanding.

For the years ended December 31, 2011, 2010 and 2009, the compensation cost recognized for share based compensation was $196,000, $239,000 and $284,000, respectively.

As of December 31, 2011, there was $197,000 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the two plans. The cost is expected to be recognized over a weighted average period of 2.5 years. See Notes 1 and 14 to the audited Consolidated Financial Statements for more detail.

In 2010, options to purchase 15,200 shares of the Company's common stock were granted from the 2000 Plan at an exercise price of $5.76 and options to purchase 67,800 shares of common stock were granted from the 2005 Plan at exercise prices between $5.30 and $5.76. In 2009, options to purchase 13,500 shares of the Company's common stock were granted at exercise prices of between $5.06 and $6.40 from the 2005 Plan. All options were granted with an exercise price equal to the market value on the grant date.

Occupancy and equipment expense decreased $72,000 or 1.86% to $3,795,000 in 2011 compared to $3,867,000 in 2010 and $3,812,000 in 2009. The increase in 2010 can be principally attributed to the expansion of our Modesto loan production office to a full service office and the relocation of our Merced and Oakhurst offices to larger facilities.

Table of Contents

Regulatory assessments decreased $346,000 or 29.05% to $845,000 in 2011 compared to $1,191,000 and $1,604,000 in 2010 and 2009, respectively. The FDIC finalized a new assessment system which took effect the third quarter of 2011. That final rule changed the assessment base from domestic deposits to average assets minus average tangible equity. There was no special assessment in 2010 which is the main reason for the decrease comparing 2010 to 2009. The FDIC imposed Special Assessment of $343,000 that was effective during the second quarter of 2009.

Data processing expenses were $1,178,000 in 2011 compared to $1,197,000 in 2010 and $1,316,000 in 2009. The $19,000 or 1.59% decrease in 2011, and the $119,000 decrease in 2010 compared to 2009 is a result of a reduction in terms of our core processing contract.

Legal fees decreased $160,000 or 32.32% to $335,000 for the year ended December 31, 2011 compared to $495,000 and $330,000 in 2010 and 2009, respectively. The higher legal fees in increases in 2010 and 2009 are primarily due to issues related to nonperforming assets and other loan related legal expenses.

Total other real estate owned (OREO) expenses decreased $1,056,000 or 98.60% to $15,000 for the year ended December 31, 2011 compared to $1,071,000 for the same period in 2010. OREO expenses in 2010 were primarily the result of the write downs of several OREO properties to their estimated fair value resulting in a valuation expense totaling $591,000. Carrying costs and property taxes totaled $371,000 related to the OREO portfolio and we realized a $109,000 loss on disposition of OREO property for the year ended December 31, 2010.

Amortization of core deposit intangibles was $414,000 for the years ended December 31, 2011, 2010 and 2009.

Other non-interest expenses increased $210,000 or 4.71% to $4,670,000 in 2011 compared to $4,460,000 in 2010 and $4,370,000 in 2009.

The following table describes significant components of other non-interest expense as a percentage of average assets.

| For the years ended December 31, (Dollars in thousands) | Other Expense 2011 | % Average Assets | | Other Expense 2010 | % Average Assets | | Other Expense 2009 | % Average Assets | |
|---|---|---|---|---|---|---|---|---|---|
| ATM/debit card expenses | $369 | 0.05 | % | $354 | 0.05 | % | $419 | 0.06 | % |
| Consulting | 340 | 0.04 | % | 212 | 0.03 | % | 454 | 0.06 | % |
| License and maintenance contracts | 324 | 0.04 | % | 275 | 0.04 | % | 251 | 0.03 | % |
| Stationery/supplies | 245 | 0.03 | % | 271 | 0.04 | % | 271 | 0.04 | % |
| Telephone | 236 | 0.03 | % | 305 | 0.04 | % | 272 | 0.04 | % |
| Amortization of software | 232 | 0.03 | % | 195 | 0.03 | % | 194 | 0.03 | % |
| Director fees and related expenses | 219 | 0.03 | % | 209 | 0.03 | % | 205 | 0.03 | % |
| Postage | 198 | 0.02 | % | 218 | 0.03 | % | 233 | 0.03 | % |
| Donations | 154 | 0.02 | % | 148 | 0.02 | % | 99 | 0.01 | % |
| Education/training | 160 | 0.02 | % | 139 | 0.02 | % | 85 | 0.01 | % |
| Operating losses | 125 | 0.02 | % | 44 | 0.01 | % | 47 | 0.01 | % |
| General insurance | 125 | 0.02 | % | 130 | 0.02 | % | 144 | 0.02 | % |
| Appraisal fees | 112 | 0.01 | % | 165 | 0.02 | % | 125 | 0.02 | % |
| Other | 1,831 | 0.23 | % | 1,795 | 0.24 | % | 1,571 | 0.21 | % |
| Total other non-interest expense | $4,670 | 0.58 | % | $4,460 | 0.59 | % | $4,370 | 0.58 | % |

For the year ended December 31, 2011, the $128,000 increase in consulting was related to assistance various financial and tax planning projects. License and maintenance contract expense increased in 2011 as a result of annual increases on various contracts in addition to new contracts for new products, services and software put in place during 2010. In

2010, the $40,000 increase in appraisal fees was related to nonperforming assets and updating appraisals for certain loans collateralized by real estate. Education and training expenses increased $54,000 mainly due to the implementation of a management training program. In 2009 the $262,000 increase in consulting expenses was related to assistance with renegotiating our core processor contracts. The $120,000 increase in appraisal fees is primarily due to issues related to nonperforming assets and other loan related expenses. The increase in various other expenses was principally due to the addition of the Service 1st offices and the new Oakhurst and Merced offices.

Table of Contents

Provision for Income Taxes

Our effective income tax rate was 22.32% for 2011 compared to (12.68%) for 2010 and (35.36%) for 2009. The Company reported an income tax provision of $1,861,000 for the year ended December 31, 2011, compared to a benefit totaling $369,000 and $676,000 for the years ended December 31, 2010 and 2009, respectively. The increase in the effective tax rate in 2011 compared to 2010 was a result of an increase in net income before tax.

Preferred Stock Dividends and Accretion

On August 18, 2011, the Company entered into a Securities Purchase Agreement with the Small Business Lending Fund of the United States Department of the Treasury (the "Treasury"), under which the Company issued 7,000 shares of Senior Non-Cumulative Perpetual Preferred Stock, Series C (the "Preferred Shares") to the Treasury for an aggregate purchase price of $7,000,000. Simultaneously, the Company agreed with Treasury under a Letter Agreement to redeem, for an aggregate price of $7,000,000, the 7,000 shares of the Company's Series A Fixed Rate Cumulative Preferred Stock ("Series A Stock")originally issued pursuant to the Treasury's Capital Purchase Program ("CPP") in 2009. The redemption of the Series A Stock resulted in an acceleration of the remaining discount booked at the time of the CPP transaction.

In connection with the repurchase of the Series A Stock, the Company also notified the Treasury of the Company's intent to repurchase the warrant (the "Warrant") to purchase 79,037 shares of the Company's common stock that was originally issued to Treasury in connection with the CPP transaction. On September 28, 2011, the Company completed the repurchase of the Warrant for total consideration of $185,000.

We accrued preferred stock dividends to the Treasury and accretion of the issuance discount in the amount of $486,000 and $395,000 during the years ended December 31, 2011 and 2010, respectively.

FINANCIAL CONDITION

Summary of Changes in Consolidated Balance Sheets

December 31, 2011 compared to December 31, 2010

As of December 31, 2011, total assets were $849,023,000 an increase of 9.19%, or $71,429,000 compared to $777,594,000 as of December 31, 2010. Total gross loans decreased 0.97%, or $4,202,000 to $427,395,000 as of December 31, 2011 compared to $431,597,000 as of December 31, 2010. Total investment portfolio increased 71.65% to $328,413,000. Total deposits increased 9.61%, or $62,491,000 to $712,986,000 as of December 31, 2011 compared to $650,495,000 as of December 31, 2010. Shareholders' equity increased 10.36%, or $10,091,000, to $107,482,000 as of December 31, 2011 compared to $97,391,000 as of December 31, 2010.

Fair Value

The Company measures the fair values of its financial instruments utilizing a hierarchical disclosure framework associated with the level of observable pricing scenarios utilized in measuring financial instruments at fair value. The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of the observable pricing scenario. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of observable pricing and a lesser degree of judgment utilized in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have little or no observable pricing and a higher degree of judgment utilized in measuring fair value.

Observable pricing scenarios are impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established and the characteristics specific to the transaction.

See Note 2 of the audited Consolidated Financial Statements for additional information about the level of pricing transparency associated with financial instruments carried at fair value.

Investments

Our investment portfolio consists primarily of agency securities, mortgage backed securities, municipal securities, collateralized mortgage obligations, corporate debt securities, and overnight investments in the Federal funds market and are classified at the date of acquisition as available for sale or held to maturity. As of December 31, 2011, investment securities

46

Table of Contents

with a fair value of $109,119,000, or 33.23% of our investment securities portfolio, were held as collateral for public funds, short and long-term borrowings, treasury, tax, and for other purposes. Our investment policies are established by the Board of Directors and implemented by our Investment/Asset Liability Committee. They are designed primarily to provide and maintain liquidity, to enable us to meet our pledging requirements for public money and borrowing arrangements, to generate a favorable return on investments without incurring undue interest rate and credit risk, and to complement our lending activities.

The level of our investment portfolio is generally considered higher than our peers due primarily to a comparatively low loan to deposit ratio. Our loan to deposit ratio at December 31, 2011 was 59.94% compared to 66.35% at December 31, 2010. The loan to deposit ratio of our peers was 74.42% at December 31, 2011. The total investment portfolio, including Federal funds sold, increased 71.60% or $137,416,000 to $328,413,000 at December 31, 2011 from $191,325,000 at December 31, 2010 primarily due to purchases of securities. The market value of the portfolio reflected an unrealized gain of $7,008,000 at December 31, 2011 compared to $1,643,000 at December 31, 2010.

We periodically evaluate each investment security for other-than-temporary impairment, relying primarily on industry analyst reports, observation of market conditions and interest rate fluctuations. As of December 31, 2011, the Company performed an analysis of the investment portfolio to determine whether any of the investments held in the portfolio had an other-than-temporary impairment (OTTI). Under ASC 320-10, the portion of the impairment that is attributable to a shortage in the present value of expected future cash flows relative to the amortized cost should be recorded as a current period charge to earnings. The discount rate in this analysis is the original yield expected at time of purchase.

As of December 31, 2011, the Company performed an analysis of the investment portfolio to determine whether any of the investments held in the portfolio had an other-than-temporary impairment (OTTI). Management evaluated all available-for-sale investment securities with an unrealized loss at December 31, 2011, and identified those that had an unrealized loss for at least a consecutive 12 month period, which had an unrealized loss at December 31, 2011 greater than 10% of the recorded book value on that date, or which had an unrealized loss of more than $10,000. Management also analyzed any securities that may have been down graded by credit rating agencies. Management retained the services of a third party in November 2011 to provide independent valuation and OTTI analysis of private label residential mortgage backed securities (PLRMBS).

For those bonds that met the evaluation criteria management obtained and reviewed the most recently published national credit ratings for those bonds. For those bonds that were municipal debt securities with an investment grade rating by the rating agencies, management also evaluated the financial condition of the municipality and any applicable municipal bond insurance provider and concluded that no credit related impairment existed.

The evaluation for PLRMBS also includes estimating projected cash flows that the Company is likely to collect based on an assessment of all available information about the applicable security on an individual basis, the structure of the security, and certain assumptions, such as the remaining payment terms for the security, prepayment speeds, default rates, loss severity on the collateral supporting the security based on underlying loan-level borrower and loan characteristics, expected housing price changes, and interest rate assumptions, to determine whether the Company will recover the entire amortized cost basis of the security. In performing a detailed cash flow analysis, the Company identified the most likely estimate of the cash flows expected to be collected. If this estimate results in a present value of expected cash flows (discounted at the security's original yield at time of purchase) that is less than the amortized cost basis of the security, an OTTI is considered to have occurred.

To assess whether it expects to recover the entire amortized cost basis of its PLRMBS, the Company performed a cash flow analysis for all of its PLRMBS as of December 31, 2011. In performing the cash flow analysis for each security, the Company uses a third-party model. The model considers borrower characteristics and the particular attributes of the loans underlying the Company's securities, in conjunction with assumptions about future changes in home prices and other assumptions, to project prepayments, default rates, and loss severities.

The month-by-month projections of future loan performance are allocated to the various security classes in each securitization structure in accordance with the structure's prescribed cash flow and loss allocation rules. When the credit enhancement for the senior securities in a securitization is derived from the presence of subordinated securities, losses are allocated first to the subordinated securities until their principal balance is reduced to zero. The projected cash flows are based on a number of assumptions and expectations, and the results of these models can vary significantly with changes in assumptions and expectations. The scenario of cash flows determined based on the model approach described above reflects a best-estimate scenario.

At each quarter end, the Company compares the present value of the cash flows expected to be collected on its PLRMBS to the amortized cost basis of the securities to determine whether a credit loss exists.

The unrealized losses associated with PLRMBS are primarily driven by higher projected collateral losses, wider credit spreads, and changes in interest rates. The Company assesses for credit impairment using a discounted cash flow model. The key assumptions include default rates, severities, discount rates and prepayment rates. Losses are estimated to a security by forecasting the underlying mortgage loans in each transaction. The forecasted loan performance is used to project cash flows to the various tranches in the structure. Based upon management's assessment of the expected credit losses of the security given the performance of the underlying collateral compared with our credit enhancement (which occurs as a result of credit loss protection provided by subordinated tranches), the Company expects to recover the entire amortized cost basis of these securities, with the exception of certain securities for which OTTI was previously recorded.

At December 31, 2011, the Company had a total of 27 PLRMBS with a remaining principal balance of $8,408,000 and a net unrealized loss of approximately $1,010,000. Eight of these securities account for $1,255,000 of the unrealized loss at December 31, 2011 offset by 19 of these securities with gains totaling $245,000. Seven of these PLRMBS with a remaining principal balance of $6,224,000 had credit ratings below investment grade. The Company continues to perform extensive analyses on these securities as well as all whole loan CMOs. Several of these investment securities continue to demonstrate cash flows and credit support as expected and the expected cash flows of the security discounted at the security's original yield at time of purchase are greater than the book value of the security, therefore management does not consider these securities to be other than temporarily impaired. No credit related OTTI charges related to PLRMBS were recorded during the year ended December 31, 2011.

See Note 3 to the audited Consolidated Financial Statements for carrying values and estimated fair values of our investment securities portfolio.

Loans

Total gross loans decreased to $427,395,000 as of December 31, 2011 compared to $431,597,000 as of December 31, 2010.

The following table sets forth information concerning the composition of our loan portfolio as of and for the years ended December 31, 2011, 2010, 2009, 2008, and 2007.

Table of Contents

| Loan Type | 2011 Amount | 2011 % of Total Loans | | 2010 Amount | 2010 % of Total Loans | | 2009 Amount | 2009 % of Total Loans | | 2008 Amount | 2008 % of Total Loans | | 2007 Amount | 2007 % of Total Loans | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars in thousands) | | | | | | | | | | | | | | |
| Commercial: | | | | | | | | | | | | | | | |
| Commercial and industrial | $78,089 | 18.3 | % | $81,318 | 18.8 | % | $93,282 | 20.3 | % | $109,664 | 22.6 | % | $71,416 | 20.9 | % |
| Agricultural land and production | 29,958 | 7.0 | % | 20,604 | 4.8 | % | 13,903 | 3.0 | % | 20,406 | 4.2 | % | 17,584 | 5.2 | % |
| Total commercial | 108,047 | 25.3 | % | 101,922 | 23.6 | % | 107,185 | 23.3 | % | 130,070 | 26.8 | % | 89,000 | 26.1 | % |
| Real estate: | | | | | | | | | | | | | | | |
| Owner occupied | 113,183 | 26.4 | % | 111,888 | 25.9 | % | 106,606 | 23.2 | % | 113,414 | 23.4 | % | 76,808 | 22.5 | % |
| Real estate-construction and other land loans | 33,047 | 7.7 | % | 32,038 | 7.4 | % | 51,633 | 11.2 | % | 57,923 | 12.0 | % | 48,593 | 14.2 | % |
| Agricultural real estate | 62,523 | 14.6 | % | 63,627 | 14.7 | % | 71,420 | 15.6 | % | 64,358 | 13.3 | % | 43,334 | 12.7 | % |
| Commercial real estate | 42,596 | 9.9 | % | 44,397 | 10.3 | % | 38,759 | 8.4 | % | 32,136 | 6.6 | % | 26,796 | 7.9 | % |
| Other real estate | 7,892 | 1.8 | % | 8,103 | 1.9 | % | 4,610 | 1.0 | % | 2,926 | 0.6 | % | 1,772 | 0.5 | % |
| Total real estate | 259,241 | 60.4 | % | 260,053 | 60.2 | % | 273,028 | 59.4 | % | 270,757 | 55.9 | % | 197,303 | 57.8 | % |
| Consumer: | | | | | | | | | | | | | | | |
| Equity loans and lines of credit | 51,106 | 12.0 | % | 58,860 | 13.6 | % | 65,353 | 14.2 | % | 63,828 | 13.2 | % | 46,575 | 13.7 | |