

HANMI FINANCIAL CORP  
Form 10-Q  
August 09, 2005

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q**

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

**For the Quarterly Period Ended June 30, 2005**

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: 000-30421**

**HANMI FINANCIAL CORPORATION**

*(Exact Name of Registrant as Specified in its Charter)*

**Delaware**

**95-4788120**

*(State or Other Jurisdiction of Incorporation or  
Organization)*

*(I.R.S. Employer Identification No.)*

**3660 Wilshire Boulevard, Penthouse Suite A  
Los Angeles, California**

**90010**

*(Address of Principal Executive Offices)*

*(Zip Code)*

**(213) 382-2200**

*(Registrant's Telephone Number, Including Area Code)*

**Not Applicable**

*(Former Name, Former Address and Former Fiscal Year, If Changed Since Last Report)*

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes  No

As of August 1, 2005, there were 49,702,443 outstanding shares of the issuer's Common Stock.

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**HANMI FINANCIAL CORPORATION**  
**QUARTERLY REPORT ON FORM 10-Q FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2005**  
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**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)***(Dollars in Thousands)*

|  | <b>June 30,<br/>2005</b> | <b>December 31,<br/>2004</b> |
|--|--------------------------|------------------------------|
| <b>ASSETS</b>  |                          |                              |
| Cash and Due from Banks  | \$ 96,850                | \$ 55,164                    |
| Federal Funds Sold and Securities Purchased Under Agreements to Resell   | 7,000                    | 72,000                       |
| Cash and Cash Equivalents  | 103,850                  | 127,164                      |
| Federal Reserve Bank Stock   | 12,153                   | 12,099                       |
| Federal Home Loan Bank Stock   | 11,977                   | 9,862                        |
| Securities Held to Maturity, at Amortized Cost (Fair Value: June 30, 2005 \$1,068; December 31, 2004 \$1,093)                    | 1,063                    | 1,090                        |
| Securities Available for Sale, at Fair Value   | 410,778                  | 417,883                      |
| Loans Receivable, Net of Allowance for Loan Losses of \$22,049 and \$22,702 at June 30, 2005 and December 31, 2004, Respectively | 2,403,161                | 2,230,992                    |
| Loans Held for Sale, at the Lower of Cost or Fair Value  | 875                      | 3,850                        |
| Customers' Liability on Acceptances  | 10,154                   | 4,579                        |
| Premises and Equipment, Net  | 20,557                   | 19,691                       |
| Accrued Interest Receivable  | 12,105                   | 10,029                       |
| Deferred Income Taxes  | 4,536                    | 5,009                        |
| Servicing Asset  | 3,434                    | 3,846                        |
| Goodwill   | 209,058                  | 209,643                      |
| Core Deposit Intangible  | 10,030                   | 11,476                       |
| Bank-Owned Life Insurance - Cash Surrender Value   | 22,283                   | 21,868                       |
| Other Assets   | 15,778                   | 15,107                       |
| <b>TOTAL ASSETS</b>  | <b>\$3,251,792</b>       | <b>\$3,104,188</b>           |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                          |                              |
| <b>LIABILITIES:</b>  |                          |                              |
| Deposits:  |                          |                              |
| Non-Interest-Bearing   | \$ 757,482               | \$ 729,583                   |
| Interest-Bearing:  |                          |                              |
| Money Market Checking  | 518,893                  | 613,662                      |
| Savings  | 141,440                  | 153,862                      |
| Time Deposits of \$100,000 or More   | 916,212                  | 756,580                      |
| Other Time Deposits  | 225,950                  | 275,120                      |
| Total Deposits   | 2,559,977                | 2,528,807                    |
| Accrued Interest Payable   | 8,367                    | 7,100                        |
| Acceptances Outstanding  | 10,154                   | 4,579                        |
| Other Borrowed Funds   | 147,647                  | 69,293                       |
| Junior Subordinated Debentures   | 82,406                   | 82,406                       |

|  |                    |                    |
|--|--------------------|--------------------|
| Other Liabilities  | 18,411             | 12,093             |
| Total Liabilities  | 2,826,962          | 2,704,278          |
| <b>SHAREHOLDERS EQUITY:</b>  |                    |                    |
| Common Stock, \$.001 Par Value; Authorized 200,000,000 Shares; Issued and Outstanding, 49,651,477 Shares and 49,330,704 Shares at June 30, 2005 and December 31, 2004, Respectively                          | 50                 | 49                 |
| Additional Paid-In Capital   | 338,538            | 334,932            |
| Unearned Compensation  | (1,331)            |                    |
| Accumulated Other Comprehensive Income Unrealized Gain on Securities Available for Sale and Interest Rate Swaps, Net of Income Taxes of \$156 and \$744 at June 30, 2005 and December 31, 2004, Respectively | 273                | 1,035              |
| Retained Earnings  | 87,300             | 63,894             |
| Total Shareholders Equity  | 424,830            | 399,910            |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>   | <b>\$3,251,792</b> | <b>\$3,104,188</b> |

See Accompanying Notes to Consolidated Financial Statements

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (LOSS)**  
**(UNAUDITED)**

*(Dollars in Thousands, Except Per Share Data)*

|   | <b>Three Months Ended</b> |               | <b>Six Months Ended</b> |               |
|---|---------------------------|---------------|-------------------------|---------------|
|   | <b>June 30,</b>           |               | <b>June 30,</b>         |               |
|   | <b>2005</b>               | <b>2004</b>   | <b>2005</b>             | <b>2004</b>   |
| <b>Interest Income:</b>                                       |                           |               |                         |               |
| Interest and Fees on Loans                                    | \$ 42,650                 | \$ 26,984     | \$ 80,725               | \$ 45,164     |
| Interest on Investments                                       | 4,734                     | 4,424         | 9,382                   | 8,220         |
| Interest on Federal Funds Sold                                | 123                       | 50            | 458                     | 72            |
| <b>Total Interest Income</b>                                  | <b>47,507</b>             | <b>31,458</b> | <b>90,565</b>           | <b>53,456</b> |
| Interest Expense  | 13,462                    | 7,484         | 24,809                  | 12,654        |
| <b>Net Interest Income Before Provision for Credit Losses</b> | <b>34,045</b>             | <b>23,974</b> | <b>65,756</b>           | <b>40,802</b> |
| Provision for Credit Losses                                   | 450                       | 850           | 586                     | 1,750         |
| <b>Net Interest Income After Provision for Credit Losses</b>  | <b>33,595</b>             | <b>23,124</b> | <b>65,170</b>           | <b>39,052</b> |
| <b>Non-Interest Income:</b>                                   |                           |               |                         |               |
| Service Charges on Deposit Accounts                           | 3,868                     | 3,524         | 7,598                   | 6,191         |
| Trade Finance Fees  | 1,036                     | 1,030         | 1,981                   | 1,835         |
| Remittance Fees   | 550                       | 436           | 1,018                   | 693           |
| Other Service Charges and Fees                                | 789                       | 560           | 1,519                   | 821           |
| Bank-Owned Life Insurance Income                              | 210                       | 183           | 415                     | 297           |
| Change in Fair Value of Derivatives                           | 370                       | (57)          | 789                     | 23            |
| Other Income  | 554                       | 492           | 1,175                   | 741           |
| Gain on Sales of Loans  | 56                        | 833           | 364                     | 1,302         |
| Gain on Sales of Securities Available for Sale                | 14                        | 6             | 96                      | 9             |
| <b>Total Non-Interest Income</b>                              | <b>7,447</b>              | <b>7,007</b>  | <b>14,955</b>           | <b>11,912</b> |
| <b>Non-Interest Expenses:</b>                                 |                           |               |                         |               |
| Salaries and Employee Benefits                                | 8,545                     | 7,924         | 17,712                  | 13,574        |
| Occupancy and Equipment                                       | 2,171                     | 2,132         | 4,402                   | 3,517         |
| Data Processing   | 1,245                     | 1,064         | 2,410                   | 1,884         |
| Supplies and Communication                                    | 729                       | 621           | 1,308                   | 978           |
| Professional Fees   | 560                       | 613           | 1,039                   | 883           |
| Advertising and Promotional Expense                           | 563                       | 878           | 1,257                   | 1,423         |
| Amortization of Core Deposit Intangible                       | 714                       | 469           | 1,446                   | 499           |
| Decrease in Fair Value of Embedded Option                     | 2                         |               | 575                     |               |
| Other Operating Expense                                       | 2,192                     | 2,333         | 3,977                   | 3,640         |
| Merger-Related Expenses                                       | (509)                     | 1,728         | (509)                   | 1,728         |

|  |                  |                 |                  |                  |
|--|------------------|-----------------|------------------|------------------|
| Total Non-Interest Expenses  | 16,212           | 17,762          | 33,617           | 28,126           |
| Income Before Provision for Income Taxes   | 24,830           | 12,369          | 46,508           | 22,838           |
| Provision for Income Taxes   | 9,792            | 4,824           | 18,138           | 8,907            |
| <b>NET INCOME</b>  | <b>\$ 15,038</b> | <b>\$ 7,545</b> | <b>\$ 28,370</b> | <b>\$ 13,931</b> |
| Earnings Per Share:  |                  |                 |                  |                  |
| Basic  | \$ 0.30          | \$ 0.18         | \$ 0.57          | \$ 0.39          |
| Diluted  | \$ 0.30          | \$ 0.18         | \$ 0.56          | \$ 0.39          |
| Weighted-Average Shares Outstanding:   |                  |                 |                  |                  |
| Basic  | 49,556,926       | 42,157,546      | 49,508,917       | 35,280,368       |
| Diluted  | 50,213,725       | 42,843,712      | 50,218,948       | 35,924,798       |
| Dividends Declared Per Share   | \$ 0.05          | \$ 0.05         | \$ 0.10          | \$ 0.10          |
| <b>COMPREHENSIVE INCOME (LOSS):</b>  |                  |                 |                  |                  |
| Net Income   | \$ 15,038        | \$ 7,545        | \$ 28,370        | \$ 13,931        |
| Other Comprehensive Income (Loss),<br>Net of Tax:  |                  |                 |                  |                  |
| Unrealized Gain (Loss) Arising During<br>the Period  | 3,116            | (7,245)         | (320)            | (4,549)          |
| Less Reclassification Adjustment for<br>Realized Gain on Securities Available<br>for Sale Included in Net Income | (4)              | 382             | (114)            | (4)              |
| Unrealized Gain (Loss) on Cash Flow<br>Hedge   | 474              | (1,547)         | (328)            | (723)            |
| Total Other Comprehensive Income<br>(Loss), Net of Tax   | 3,586            | (8,410)         | (762)            | (5,276)          |
| <b>Total Comprehensive Income (Loss)</b>   | <b>\$ 18,624</b> | <b>\$ (865)</b> | <b>\$ 27,608</b> | <b>\$ 8,655</b>  |

See Accompanying Notes to Consolidated Financial Statements

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

*(In Thousands)*

|  | <b>Six Months Ended June 30,</b> |                 |
|--|----------------------------------|-----------------|
|  | <b>2005</b>                      | <b>2004</b>     |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                  |                 |
| Net Income   | \$ 28,370                        | \$ 13,931       |
| Adjustments to Reconcile Net Income to Net Cash and Cash Equivalents Provided By Operating Activities: |                                  |                 |
| Depreciation and Amortization of Premises and Equipment  | 1,268                            | 1,144           |
| Amortization of Premiums and Discounts on Investments  | (17)                             | 2,359           |
| Amortization of Core Deposit Intangible  | 1,446                            | 499             |
| Amortization of Unearned Compensation  | 484                              |                 |
| Provision for Credit Losses  | 586                              | 1,750           |
| Federal Reserve Bank Stock and Federal Home Loan Bank Stock Dividend                                   | (103)                            | (903)           |
| Gain on Sales of Securities Available for Sale   | (96)                             | (9)             |
| Change in Fair Value of Derivatives  | (214)                            | (23)            |
| Gain on Sales of Loans   | (364)                            | (1,302)         |
| Loss on Sales of Premises and Equipment  | 18                               | 9               |
| Deferred Tax (Benefit) Provision   | 44                               | (11,264)        |
| Origination of Loans Held for Sale   | (10,026)                         | (18,576)        |
| Proceeds from Sales of Loans Held for Sale   | 13,365                           | 13,727          |
| Change In:   |                                  |                 |
| (Increase) Decrease in Accrued Interest Receivable   | (2,076)                          | 542             |
| Increase in Cash Surrender Value of Bank-Owned Life Insurance  | (415)                            | (297)           |
| (Increase) Decrease in Other Assets  | (5,249)                          | 4,200           |
| Increase (Decrease) in Accrued Interest Payable  | 1,267                            | (1,408)         |
| Increase (Decrease) in Other Liabilities   | 11,971                           | (1,402)         |
| <b>Net Cash and Cash Equivalents Provided By Operating Activities</b>                                  | <b>40,259</b>                    | <b>2,977</b>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                  |                 |
| Proceeds from Matured or Called Securities Available for Sale  | 49,000                           | 69,755          |
| Proceeds from Matured or Called Securities Held to Maturity  | 27                               | 102             |
| Proceeds from Sale of Securities Available for Sale  | 6,456                            | 49,400          |
| Net Increase in Loans Receivable   | (172,619)                        | (80,352)        |
| Purchases of Federal Reserve Bank Stock and Federal Home Loan Bank Stock                               | (2,066)                          |                 |
| Purchases of Securities Available for Sale   | (48,238)                         | (12,095)        |
| Purchase of Bank-Owned Life Insurance  |                                  | (10,000)        |
| Purchases of Premises and Equipment, Net   | (2,152)                          | (563)           |
| Acquisition of PUB, Net of Cash Acquired   |                                  | (63,455)        |
| <b>Net Cash and Cash Equivalents Used In Investing Activities</b>                                      | <b>(169,592)</b>                 | <b>(47,208)</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |                                  |                 |



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|   |                   |                   |
|---|-------------------|-------------------|
| Increase (Decrease) in Deposits                                       | 31,170            | (37,238)          |
| Issuance of Junior Subordinated Debentures                            |                   | 82,406            |
| Stock Issued Through Private Placement                                |                   | 71,710            |
| Proceeds from Exercise of Stock Options                               | 1,455             | 1,084             |
| Cash Dividends Paid   | (4,960)           | (3,870)           |
| Decrease (Increase) in Other Borrowed Funds                           | 78,354            | (24,928)          |
| <b>Net Cash and Cash Equivalents Provided By Financing Activities</b> | <b>106,019</b>    | <b>89,164</b>     |
| <b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>           | <b>(23,314)</b>   | <b>44,933</b>     |
| Cash and Cash Equivalents, Beginning of Period                        | 127,164           | 62,595            |
| <b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>                       | <b>\$ 103,850</b> | <b>\$ 107,528</b> |
| <b>Supplemental Disclosures of Cash Flow Information:</b>             |                   |                   |
| Interest Paid   | \$ 26,076         | \$ 10,921         |
| Income Taxes Paid   | \$ 14,150         | \$ 15,094         |
| <b>Reconciliation of Acquisition of PUB, Net of Cash Acquired:</b>    |                   |                   |
| Fair Value of Assets Acquired   | \$                | \$ 1,383,739      |
| Cash and Cash Equivalents Acquired                                    |                   | (104,383)         |
| Non-Cash Financing of Purchase Price and Liabilities Assumed:         |                   |                   |
| Issuance of Common Stock  |                   | (156,750)         |
| Liabilities Assumed   |                   | (1,059,151)       |
| <b>Acquisition of PUB, Net of Cash Acquired</b>                       | <b>\$</b>         | <b>\$ 63,455</b>  |

See Accompanying Notes to Consolidated Financial Statements

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004**

**NOTE 1 HANMI FINANCIAL CORPORATION**

Hanmi Financial Corporation ( Hanmi Financial , we or our ) is a Delaware corporation that is the holding company for Hanmi Bank (the Bank ) and is subject to the Bank Holding Company Act of 1956, as amended.

Hanmi Bank, our primary subsidiary, is a commercial bank licensed by the California Department of Financial Institutions. The Bank s deposit accounts are insured under the Federal Deposit Insurance Act, up to the applicable limits thereof. The Bank is a member of the Federal Reserve System.

Our primary operations are related to traditional banking activities, including the acceptance of deposits and the lending and investing of money through operation of the Bank. Hanmi Bank is a community bank conducting general business banking with its primary market encompassing the multi-ethnic population of Los Angeles, Orange, San Diego, San Francisco and Santa Clara counties. Hanmi Bank s full-service offices are located in business areas where many of the businesses are run by immigrants and other minority groups. Hanmi Bank s client base reflects the multi-ethnic composition of these communities. The Bank is a California state-chartered, FDIC-insured financial institution.

On April 30, 2004, we completed the acquisition of Pacific Union Bank ( PUB ), a \$1.2 billion (assets) commercial bank headquartered in Los Angeles that also served primarily the Korean-American community. As of June 30, 2005, the Bank maintained a branch network of 22 locations, serving individuals and small- to medium-sized businesses in Los Angeles and surrounding areas.

**NOTE 2 BASIS OF PRESENTATION**

In the opinion of management, the consolidated financial statements of Hanmi Financial Corporation and subsidiary reflect all adjustments of a normal recurring nature that are necessary for a fair presentation of the results for the interim periods ended June 30, 2005, but are not necessarily indicative of the results that will be reported for the entire year. In the opinion of management, the aforementioned consolidated financial statements are in conformity with accounting principles generally accepted in the United States of America. The interim information should be read in conjunction with our 2004 Annual Report on Form 10-K.

Descriptions of our significant accounting policies are included in Note 1 Summary of Significant Accounting Policies in our 2004 Annual Report on Form 10-K. Certain reclassifications were made to the prior periods presentation to conform to the current period s presentation.

On January 20, 2005, our Board of Directors declared a two-for-one stock split, to be effected in the form of a 100 percent common stock dividend. The new shares were distributed on February 15, 2005 to shareholders of record on the close of business on January 31, 2005. All share and per share amounts for the prior periods have been restated to reflect the stock dividend.

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004 (Continued)**

**NOTE 3 EMPLOYEE STOCK-BASED COMPENSATION**

Our employee stock-based compensation arrangements are measured under the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*. Accordingly, no compensation expense has been recognized for the stock option plan, as stock options were granted at fair value at the date of grant. Had compensation expense for the stock option plan been determined based on the fair values estimated using the Black-Scholes model at the grant dates for previous awards, our net income and earnings per share would have been reduced to the pro forma amounts indicated below:

|  | <b>Three Months Ended</b>                            |                | <b>Six Months Ended</b> |                 |
|--|--|----------------|-------------------------|-----------------|
|  | <b>June 30,</b>                                      |                | <b>June 30,</b>         |                 |
|  | <b>2005</b>  | <b>2004</b>    | <b>2005</b>             | <b>2004</b>     |
|  | <i>(Dollars in Thousands; Except Per Share Data)</i> |                |                         |                 |
| Net Income As Reported   | \$15,038   | \$7,545        | \$28,370                | \$13,931        |
| Add Stock-Based Employee Compensation Expense Included in Reported Net Income, Net of Related Tax Effects (Restricted Stock Grant)                                 | 55   |                | 297                     |                 |
| Deduct Total Stock-Based Employee Compensation Expense Determined Under Fair Value Based Method for All Awards Subject to SFAS No. 123, Net of Related Tax Effects | (350)  | (59)           | (877)                   | (210)           |
| <b>Net Income Pro Forma</b>  | <b>\$14,743</b>                                      | <b>\$7,486</b> | <b>\$27,790</b>         | <b>\$13,721</b> |
| Earnings Per Share As Reported:  |  |                |                         |                 |
| Basic  | \$ 0.30  | \$ 0.18        | \$ 0.57                 | \$ 0.39         |
| Diluted  | \$ 0.30  | \$ 0.18        | \$ 0.56                 | \$ 0.39         |
| Earnings Per Share Pro Forma:  |  |                |                         |                 |
| Basic  | \$ 0.30  | \$ 0.18        | \$ 0.56                 | \$ 0.39         |
| Diluted  | \$ 0.29  | \$ 0.17        | \$ 0.55                 | \$ 0.38         |

In February 2005, 100,000 shares of restricted stock were granted to Dr. Sung Won Sohn, our Chief Executive Officer. 20,000 of these shares vested immediately, and an additional 20,000 shares will vest each year over the next four years on the anniversary date of the grant. The market value of the shares awarded totaled \$1,815,000. The 20,000 shares that vested immediately were recorded as compensation expense and the remaining 80,000 shares were recorded as unearned compensation, a separate component of shareholders' equity. Unearned compensation is being amortized against income over the four-year vesting period. For the three and six months ended June 30, 2005, compensation expense of \$91,000 and \$484,000, respectively, was recognized in the consolidated statements of income.

**NOTE 4 EARNINGS PER SHARE**

Earnings per share (EPS) is calculated on both a basic and a diluted basis. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to

issue common stock were exercised or converted into common stock or resulted from the issuance of common stock that then shared in earnings, excluding common shares in treasury.

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004 (Continued)**

**NOTE 4 EARNINGS PER SHARE (Continued)**

The following table presents a reconciliation of the components used to derive basic and diluted EPS for the periods indicated.

|                                    | <b>Income<br/>(Numerator)</b>                        | <b>Weighted-<br/>Average<br/>Shares<br/>(Denominator)</b> | <b>Per<br/>Share<br/>Amount</b> |         |
|------------------------------------|--|---|---------------------------------|---------|
|                                    | <i>(Dollars in Thousands, Except Per Share Data)</i> |   |                                 |         |
| <b>Three Months Ended June 30:</b> |  |   |                                 |         |
| <b>2005:</b>                       |  |   |                                 |         |
| Basic EPS                          | Income Available to Common Shareholders              | \$ 15,038   | 49,556,926                      | \$ 0.30 |
|                                    | Effect of Dilutive Securities                        |   | Options and Warrants<br>656,799 |         |
| Diluted EPS                        | Income Available to Common Shareholders              | \$ 15,038   | 50,213,725                      | \$ 0.30 |
| <b>2004:</b>                       |  |   |                                 |         |
| Basic EPS                          | Income Available to Common Shareholders              | \$ 7,545  | 42,157,546                      | \$ 0.18 |
|                                    | Effect of Dilutive Securities                        |   | Options and Warrants<br>686,166 |         |
| Diluted EPS                        | Income Available to Common Shareholders              | \$ 7,545  | 42,843,712                      | \$ 0.18 |
| <b>Six Months Ended June 30:</b>   |  |   |                                 |         |
| <b>2005:</b>                       |  |   |                                 |         |
| Basic EPS                          | Income Available to Common Shareholders              | \$ 28,370   | 49,508,917                      | \$ 0.57 |
|                                    | Effect of Dilutive Securities                        |   | Options and Warrants<br>710,031 | (0.01)  |
| Diluted EPS                        | Income Available to Common Shareholders              | \$ 28,370   | 50,218,948                      | \$ 0.56 |
| <b>2004:</b>                       |  |   |                                 |         |
| Basic EPS                          | Income Available to Common Shareholders              | \$ 13,931   | 35,280,368                      | \$ 0.39 |
|                                    | Effect of Dilutive Securities                        |   | Options and Warrants<br>644,430 |         |
| Diluted EPS                        | Income Available to Common Shareholders              | \$ 13,931   | 35,924,798                      | \$ 0.39 |

For the three and six months ended June 30, 2005, there were 430,554 and 395,554 options outstanding, respectively, that were not included in the computation of diluted EPS because their exercise price was greater than the average market price of the common shares and, therefore, the effect would be anti-dilutive. For the three and six months ended June 30, 2004, there were 386,500 and 382,500 options outstanding, respectively, that were not included in the computation of diluted EPS.

**NOTE 5 DERIVATIVE FINANCIAL INSTRUMENTS**

During 2004, the Bank entered into one interest rate swap agreement, wherein the Bank received a fixed rate of 7.29 percent at quarterly intervals, and paid Prime-based floating rates, at quarterly intervals, on a total notional amount of \$10.0 million. This swap agreement matures in 2009 and was designated as a cash flow hedge for accounting purposes. During 2003, the Bank entered into four interest rate swap agreements, wherein the Bank

received fixed rates of 5.77 percent, 6.37 percent, 6.51 percent and 6.76 percent, at quarterly intervals, and paid Prime-based floating rates, at quarterly intervals, on a total notional amount of \$60.0 million. All four of the swap agreements mature in 2008. These swaps were designated as hedges for accounting purposes. As of June 30, 2005, the total notional amount of interest rate swaps was \$70.0 million.

As of June 30, 2005, the fair value of the interest rate swaps was in an unfavorable position of \$859,000. A total of (\$532,000), net of tax, was included in Other Comprehensive Income. No income related to hedge ineffectiveness was recognized for the six months ended June 30, 2005.

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004 (Continued)**

**NOTE 5 DERIVATIVE FINANCIAL INSTRUMENTS (Continued)**

In 2004, the Bank offered a certificate of deposit ( CD ) product that pays interest tied to the movement in the Standard & Poor's 500 Index. The economic characteristics and risks of the embedded option are not clearly and closely related to the CD. Therefore, the embedded option is separated from the CD and accounted for separately in liabilities. As of June 30, 2005, the fair value of the embedded option was \$990,000 and the change in the liability during the six months ended June 30, 2005 was \$406,000. The change was recognized in earnings.

To economically hedge the interest risk, the Bank entered into an agreement to purchase an equity swap. As of June 30, 2005, the fair value of the equity swap was \$4,000, which was also equal to the change during the year. The change was recognized in earnings.

**NOTE 6 OFF-BALANCE SHEET ARRANGEMENTS**

As part of the Bank's services to small- and medium-sized business customers, the Bank issues formal loan commitments and letters of credit. These commitments can be either secured or unsecured. They may be in the form of revolving lines of credit for seasonal working capital needs or may take the form of commercial letters of credit or standby letters of credit. Commercial letters of credit facilitate import trade. Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party.

The following table shows the distribution of the Hanmi Bank's undisbursed loan commitments and letters of credit as of the dates indicated.

|   | <b>June 30,<br/>2005</b> | <b>December 31,<br/>2004</b> |
|---|--------------------------|------------------------------|
|   | <i>(In Thousands)</i>    |                              |
| Commitments to Extend Credit                                    | \$465,482                | \$367,708                    |
| Standby Letters of Credit                                       | 40,053                   | 47,901                       |
| Commercial Letters of Credit                                    | 63,915                   | 49,699                       |
| Unused Credit Card Lines  | 13,731                   | 14,324                       |
| <b>Total Undisbursed Loan Commitments and Letters of Credit</b> | <b>\$583,181</b>         | <b>\$479,632</b>             |

**NOTE 7 CURRENT ACCOUNTING MATTERS**

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 123 (Revised 2004), *Share-Based Payment* ( SFAS No. 123R ). SFAS No. 123R addresses the accounting for share-based payment transactions in which a company receives employee services in exchange for either equity instruments of the company or liabilities that are based on the fair value of the company's equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using the intrinsic method that is currently used and requires that such transactions be accounted for using a fair value-based method and recognized as expense in the Consolidated Statements of Income. SFAS No. 123R was to be effective as of the beginning of the third quarter of 2005; however, on April 14, 2005, the Securities and Exchange Commission adopted a new rule that deferred the required adoption date to the beginning of the first quarter of 2006. We have provided pro forma disclosures under SFAS No. 123 in Note 3 Employee Stock-Based Compensation.

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**HANMI FINANCIAL CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004 (Continued)**

**NOTE 7 CURRENT ACCOUNTING MATTERS (Continued)**

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*. SFAS No. 154 is a replacement of Accounting Principles Board ( APB ) Opinion No. 20, *Accounting Changes*, and FASB Statement No. 3, *Reporting Accounting Changes in Interim Financial Statements (an Amendment of APB Opinion No. 28)*. SFAS No. 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application as the required method for reporting a change in accounting principle. SFAS No. 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. The reporting of a correction of an error by restating previously issued financial statements is also addressed by SFAS No. 154. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 31, 2005. We will adopt this pronouncement beginning in fiscal year 2006.

**NOTE 8 SUBSEQUENT EVENT**

On July 20, 2005, following a joint regular examination by the Federal Reserve Bank ( FRB ) and the California Department of Financial Institutions, the Bank s Board of Directors, approved and signed an informal memorandum of understanding ( Memorandum ) in connection with certain deficiencies identified by the regulators relating to the Bank s compliance with certain provisions of the Bank Secrecy Act (the BSA ) and anti-money laundering regulations. Under the terms of the Memorandum, the Bank must comply in all material respects with the BSA and take certain actions within various timeframes. The Memorandum requires in part that the Bank enhance its written programs designed to ensure and maintain compliance with the BSA and anti-money laundering regulations, improve documentation of its compliance with suspicious activity reporting provisions of applicable regulations and provide regular compliance reports to the regulators. The implementation of these programs will include revisions of the Bank s policies, processes and procedures, enhancements of the Bank s system of internal controls for BSA compliance, retention of and support from an increased compliance staff and improved ongoing employee training.

Management expects additional BSA compliance expenses for the Bank resulting from the Memorandum, although these expenses are not anticipated to have a material financial impact on our financial position or results of operations. The Memorandum may also affect the timing or ability of the Bank or Hanmi Financial to engage in or obtain regulatory approval for certain expansionary activities.



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**ITEM 2. MANAGEMENT'S  
DISCUSSION  
AND ANALYSIS  
OF FINANCIAL  
CONDITION  
AND RESULTS  
OF  
OPERATIONS**

The following is management's discussion and analysis of the major factors that influenced our results of operations and financial condition for the three and six months ended June 30, 2005. This analysis should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2004 and with the unaudited consolidated financial statements and notes thereto set forth in this Report.

**CRITICAL ACCOUNTING POLICIES**

We have established various accounting policies that govern the application of accounting principles generally accepted in the United States of America in the preparation of our financial statements. Our significant accounting policies are described in our Annual Report on Form 10-K for the year ended December 31, 2004. Certain accounting policies require us to make significant estimates and assumptions that have a material impact on the carrying value of certain assets and liabilities, and we consider these to be critical accounting policies. The estimates and assumptions we use are based on historical experience and other factors, which we believe to be reasonable under the circumstances. Actual results could differ significantly from these estimates and assumptions that could have a material impact on the carrying value of assets and liabilities at the balance sheet dates and our results of operations for the reporting periods. Management has discussed the development and selection of these critical accounting policies with the Audit Committee of our Board of Directors.

We believe the allowance for loan losses and allowance for off-balance sheet items, such as unfunded loan commitments and letters of credit, are critical accounting policies that require significant estimates and assumptions that are particularly susceptible to significant change in the preparation of our financial statements. See Item 2. Management's Discussion and Analysis of Results of Operations and Financial Condition—Financial Condition Allowance for Loan Losses and Allowance for Off-Balance Sheet Items for a description of the methodology used to determine the allowance for loan losses and allowance for off-balance sheet items.

During the year ended December 31, 2004, the application of SFAS No. 141, *Business Combinations*, to the purchase of Pacific Union Bank (PUB) required significant estimates and assumptions. We engaged outside experts including appraisers to assist in estimating the fair values of certain assets acquired, particularly the loan portfolio, core deposit intangible asset and fixed assets. The fair values of financial assets, including the investments portfolio, deposits and borrowings, were estimated by the Bank, using market data regarding securities market prices and interest rates. We also evaluated long-lived assets for impairment and recorded any necessary adjustments. In accordance with Emerging Issues Task Force Issue No. 95-3, *Recognition of Liabilities in Connection With a Purchase Business Combination*, we recognized liabilities assumed for costs to involuntarily terminate employees of PUB and costs to exit activities of PUB under an exit plan approved by Hanmi Bank's board of directors.

**Table of Contents****SELECTED FINANCIAL DATA**

The following tables sets forth certain selected financial data for the periods indicated.

|   | <b>As of and for the<br/>Three Months Ended<br/>June 30,</b> |             |
|---|--|-------------|
|   | <b>2005</b>  | <b>2004</b> |
|   | <i>(Dollars in Thousands)</i>                                |             |
| <b>Average Balances:</b>                                  |  |             |
| Average Gross Loans                                       | \$2,334,803  | \$1,909,491 |
| Average Interest-Earning Assets                           | 2,793,143  | 2,385,167   |
| Average Total Assets                                      | 3,168,995  | 2,669,930   |
| Average Deposits  | 2,542,886  | 2,120,450   |
| Average Interest-Bearing Liabilities                      | 1,960,987  | 1,672,371   |
| Average Shareholders' Equity                              | 416,465  | 302,765     |
| Average Tangible Equity <sup>(1)</sup>                    | 197,080  | 153,057     |
| <b>Selected Performance Ratios:</b>                       |  |             |
| Return on Average Total Assets <sup>(2) (3)</sup>         | 1.90%  | 1.14%       |
| Return on Average Shareholders' Equity <sup>(2) (4)</sup> | 14.48%   | 10.02%      |
| Return on Average Tangible Equity <sup>(2) (5)</sup>      | 30.61%   | 19.83%      |
| Net Interest Margin <sup>(6)</sup>                        | 4.89%  | 4.04%       |
| Average Shareholders' Equity to Average Total Assets      | 13.14%   | 11.34%      |
| Efficiency Ratio <sup>(7) (8)</sup>                       | 40.30%   | 57.33%      |
| Dividend Payout Ratio <sup>(9)</sup>                      | 16.67%   | 27.78%      |

<sup>(1)</sup> *Average tangible equity is calculated by subtracting average goodwill and average core deposit intangible assets from average shareholders equity.*

<sup>(2)</sup> *Calculation based upon annualized net income.*

<sup>(3)</sup> *Net income divided by average total assets.*

- (4) *Net income divided by average shareholders equity.*
- (5) *Net income divided by average tangible equity.*
- (6) *Represents net interest income before provision for credit losses as a percentage of average interest-earning assets.*
- (7) *The efficiency ratio is calculated as the ratio of total non-interest expenses to the sum of net interest income before provision for credit losses and total non-interest income including securities gains and losses.*
- (8) *Excludes reversal of merger-related expenses totaling \$509,000 for the three months ended June 30, 2005.*
- (9) *Dividends declared per share divided by basic earnings*

*per share.*

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|   | <b>As of and for the<br/>Six Months Ended<br/>June 30,</b> |             |
|---|--|-------------|
|   | <b>2005</b>  | <b>2004</b> |
|   | <i>(Dollars in Thousands;<br/>Except Per Share Data)</i>   |             |
| <b>Average Balances:</b>  |  |             |
| Average Gross Loans   | \$2,287,253  | \$1,592,785 |
| Average Interest-Earning Assets                                   | 2,765,114  | 2,034,382   |
| Average Total Assets  | 3,136,419  | 2,220,208   |
| Average Deposits  | 2,531,123  | 1,771,622   |
| Average Interest-Bearing Liabilities                              | 1,943,789  | 1,424,531   |
| Average Shareholders' Equity                                      | 411,270  | 224,489     |
| Average Tangible Equity <sup>(1)</sup>                            | 191,159  | 148,620     |
| <b>Selected Performance Ratios:</b>                               |  |             |
| Return on Average Total Assets <sup>(2)(3)</sup>                  | 1.82%  | 1.26%       |
| Return on Average Shareholders' Equity <sup>(2)(4)</sup>          | 13.91%   | 12.48%      |
| Return on Average Tangible Equity <sup>(2)(5)</sup>               | 29.93%   | 18.85%      |
| Net Interest Margin <sup>(6)</sup>                                | 4.80%  | 4.03%       |
| Average Shareholders' Equity to Average Total Assets              | 13.11%   | 10.11%      |
| Efficiency Ratio <sup>(7)(8)</sup>                                | 42.28%   | 53.36%      |
| Dividend Payout Ratio <sup>(9)</sup>                              | 17.54%   | 25.64%      |
| <b>Selected Capital Ratios: <sup>(10)</sup></b>                   |  |             |
| Tier 1 Capital to Average Total Assets:                           |  |             |
| Hanmi Financial   | 9.65%  | 9.66%       |
| Hanmi Bank  | 9.61%  | 9.57%       |
| Tier 1 Capital to Total Risk-Weighted Assets:                     |  |             |
| Hanmi Financial   | 11.22%   | 10.10%      |
| Hanmi Bank  | 11.18%   | 10.02%      |
| Total Capital to Total Risk-Weighted Assets:                      |  |             |
| Hanmi Financial   | 12.17%   | 11.18%      |
| Hanmi Bank  | 12.13%   | 11.11%      |
| Book Value Per Share <sup>(11)(12)</sup>                          | \$ 8.56  | \$ 7.65     |
| <b>Selected Asset Quality Ratios:</b>                             |  |             |
| Net Loan Charge-Offs to Average Total Gross Loans <sup>(13)</sup> | 0.10%  | 0.21%       |
| Allowance for Loan Losses to Total Gross Loans at End of Period   | 0.91%  | 1.06%       |
| Allowance for Loan Losses to Non-Performing Loans                 | 361.6%   | 281.3%      |
| Non-Performing Assets to Total Assets <sup>(14)</sup>             | 0.19%  | 0.27%       |

<sup>(1)</sup> Average tangible equity is calculated by subtracting average goodwill and

*average core  
deposit  
intangible assets  
from average  
shareholders  
equity.*

- (2) *Calculation  
based upon  
annualized net  
income.*
- (3) *Net income  
divided by  
average total  
assets.*
- (4) *Net income  
divided by  
average  
shareholders  
equity.*
- (5) *Net income  
divided by  
average tangible  
equity.*
- (6) *Represents net  
interest income  
before provision  
for credit losses  
as a percentage  
of average  
interest-earning  
assets.*
- (7) *The efficiency  
ratio is  
calculated as the  
ratio of total  
non-interest  
expenses to the  
sum of net  
interest income  
before provision  
for credit losses  
and total  
non-interest  
income  
including*

*securities gains  
and losses.*

- (8) *Excludes reversal of merger-related expenses totaling \$509,000 for the six months ended June 30, 2005.*
- (9) *Dividends declared per share divided by basic earnings per share.*
- (10) *The required ratios for a well-capitalized institution, as defined by regulations of the Board of Governors of the Federal Reserve System, are 5 percent leverage capital, 6 percent Tier 1 risk-based capital and 10 percent total risk-based capital.*
- (11) *2004 book value per share has been restated for a 100 percent stock dividend declared in January 2005.*
- (12) *Shareholders equity divided by common shares outstanding.*

- (13) *Calculation based upon annualized net loan charge-offs.*
- (14) *Non-performing assets consist of non-performing loans (non-accrual loans, loans past due 90 days or more and restructured loans where the terms of repayment have been renegotiated and resulted in a reduction or deferral of interest or principal) and other real estate owned.*



**Table of Contents****FORWARD-LOOKING STATEMENTS**

Some of the statements under Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this Form 10-Q constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. In some cases, you can identify forward-looking statements by terminology such as may, will, should, could, expect, plans, intends, anticipates, believes, estimates, predicts, potential, or continue, or the negative of such terms and comparable terminology. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ from those expressed or implied by the forward-looking statement. For additional information concerning these factors, see our Form 10-K filed with the Securities and Exchange Commission on March 16, 2005 under the headings Factors That May Affect Future Results of Operations, Interest Rate Risk Management and Liquidity and Capital Resources. We undertake no obligation to update these forward-looking statements to reflect events or circumstances that occur after the date on which such statements were made.

**RESULTS OF OPERATIONS****Overview**

On April 30, 2004, we completed the merger with Pacific Union Bank ( PUB ). As a result, operating results for the three and six months ended June 30, 2004 include only two months of results following the merger with PUB. Operating results reflect the resulting increase in average total assets from \$2.67 billion and \$2.22 billion in the three and six month periods ended June 30, 2004, respectively, to \$3.17 billion and \$3.14 billion in the three and six month periods ended June 30, 2005, respectively.

For the three months ended June 30, 2005, net income was \$15.0 million, or \$0.30 per diluted share, compared to \$7.5 million, or \$0.18 per diluted share, for the three months ended June 30, 2004. The 99.3 percent increase in net income for 2005 as compared to 2004 was primarily due to an increase of 85 basis points in the net interest margin, the acquisition of PUB and asset growth subsequent to the acquisition of PUB. Net interest income before provision for credit losses increased \$10.1 million, or 42.0 percent, due to ongoing growth in the loan portfolio as well as the newly acquired interest-earning assets from PUB. Non-interest income increased by \$440,000, or 6.3 percent, due to a 12.5 percent increase in services charges and fees and an increase in the fair value of derivatives, partially offset by a 93.3 percent decrease in gain on sales of loans. Non-interest expenses decreased by \$1.6 million, or 8.7 percent, due to one-time merger-related expenses in the prior year. The annualized return on average assets was 1.90 percent for the three months ended June 30, 2005, compared to an annualized return on average assets of 1.14 percent for the same period of 2004, an increase of 76 basis points. The annualized return on average shareholders' equity was 14.48 percent for the three months ended June 30, 2005, and the annualized return on average tangible equity was 30.61 percent, compared to 10.02 percent and 19.83 percent, respectively, for the same period in 2004.

For the six months ended June 30, 2005, net income was \$28.4 million, or \$0.56 per diluted share, compared to \$13.9 million, or \$0.39 per diluted share, for the six months ended June 30, 2004. The 103.6 percent increase in net income for 2005 as compared to 2004 was primarily due to an increase of 77 basis points in the net interest margin, the acquisition of PUB and asset growth subsequent to the acquisition of PUB. Net interest income before provision for credit losses increased \$25.0 million, or 61.2 percent, due to ongoing growth in the loan portfolio as well as the newly acquired interest-earning assets from PUB. Non-interest income increased by \$3.0 million, or 25.5 percent, mainly due to an increase in service charges on deposit accounts. Non-interest expenses increased by \$5.5 million, or 19.5 percent, due to the additional salaries and employee benefits, occupancy, professional fees, data processing and core deposit intangible amortization expenses incurred following the merger, offset by decreased merger-related expenses. The annualized return on average assets was 1.82 percent for the six months ended June 30, 2005, compared to an annualized return on average assets of 1.26 percent for the same period of 2004, an increase of 56 basis points. The annualized return on average shareholders' equity was 13.91 percent for the six months ended June 30, 2005, and the annualized return on average tangible equity was 29.93 percent, compared to 12.48 percent and 18.85 percent, respectively, for the same period in 2004.

Return on average tangible equity is supplemental financial information determined by a method other than in accordance with accounting principles generally accepted in the United States of America ( GAAP ). This non-GAAP measure is used by management in the analysis of Hanmi Financial s performance. Average tangible equity is calculated by subtracting average goodwill and average core deposit intangible assets from average shareholders equity. Banking and financial institution regulators also exclude goodwill and intangibles from shareholders equity when assessing the capital adequacy of a financial institution. Management believes the presentation of this financial measure excluding the impact of these items provides useful supplemental information that is essential to a proper understanding of the financial results of Hanmi Financial, as it provides a method to assess management s success in utilizing tangible capital. This disclosure should not be viewed as a substitution for results determined in accordance with GAAP, nor is it necessarily comparable to non-GAAP performance measures that may be presented by other companies.

The following table reconciles this non-GAAP performance measure to the GAAP performance measure for the periods indicated:

|  | <b>Three Months Ended</b>     |                   | <b>Six Months Ended</b> |                   |
|--|-------------------------------|-------------------|-------------------------|-------------------|
|  | <b>June 30,</b>               |                   | <b>June 30,</b>         |                   |
|  | <b>2005</b>                   | <b>2004</b>       | <b>2005</b>             | <b>2004</b>       |
|  | <i>(Dollars in Thousands)</i> |                   |                         |                   |
| Average Shareholders Equity                            | \$ 416,465                    | \$ 302,765        | \$ 411,270              | \$ 224,489        |
| Less Average Goodwill and Core Deposit Intangible      | (219,385)                     | (149,708)         | (220,111)               | (75,869)          |
| <b>Average Tangible Equity</b>                         | <b>\$ 197,080</b>             | <b>\$ 153,057</b> | <b>\$ 191,159</b>       | <b>\$ 148,620</b> |
| Return on Average Shareholders Equity                  | 14.48%                        | 10.02%            | 13.91%                  | 12.48%            |
| Effect of Average Goodwill and Core Deposit Intangible | 16.13%                        | 9.81%             | 16.02%                  | 6.37%             |
| <b>Return on Average Tangible Equity</b>               | <b>30.61%</b>                 | <b>19.83%</b>     | <b>29.93%</b>           | <b>18.85%</b>     |

**Table of Contents****Net Interest Income Before Provision for Credit Losses**

Our earnings depend largely upon the difference between the interest income received from the loan portfolio and other interest-earning assets and the interest paid on deposits and borrowings. The difference is net interest income. Net interest income, when expressed as a percentage of average total interest-earning assets, is referred to as the net interest margin. Net interest income is affected by the change in the level and mix of interest-earning assets and interest-bearing liabilities, referred to as volume changes. Net interest income is also affected by changes in the yields earned on assets and rates paid on liabilities, referred to as rate changes. Interest rates charged on loans are affected principally by the demand for such loans, the supply of money available for lending purposes and competitive factors. Those factors are, in turn, affected by general economic conditions and other factors beyond our control, such as Federal economic policies, the general supply of money in the economy, income tax policies, governmental budgetary matters and the actions of the Federal Reserve Bank.

For the three months ended June 30, 2005, net interest income before provision for credit losses was \$34.0 million. This represented an increase of \$10.1 million, or 42.0 percent, over net interest income before provision for credit losses of \$24.0 million for the three months ended June 30, 2004. The interest rate spread increased to 4.07 percent for the three months ended June 30, 2005, from 3.50 percent for the same period in 2004. The change was mainly due to an increase in rates received on loans and investments as our prime rate and the Wall Street Journal prime rate both increased by a total of 50 basis points during the second quarter. Approximately 86.0 percent of our loan portfolio is tied to the Wall Street Journal prime rate or our prime rate. We also emphasized spread income and disposed of certain low yielding assets in the first and second quarters of 2004 and reinvested the proceeds from the amortization of our investment portfolio into loan production. Average loans outstanding increased from 80.1 percent of average interest-earning assets in the second quarter of 2004 to 83.6 percent of average interest-earning assets in the second quarter of 2005. The net interest margin also increased by 85 basis points to 4.89 percent for the three months ended June 30, 2005, from 4.04 percent for the same period in 2004, due to an increase in the volume of interest-earning assets with higher interest rates.

For the six months ended June 30, 2005, net interest income before provision for credit losses was \$65.8 million. This represented an increase of \$25.0 million, or 61.2 percent, over net interest income before provision for credit losses of \$40.8 million for the six months ended June 30, 2004. The interest rate spread increased to 4.03 percent for the six months ended June 30, 2005, from 3.49 percent for the same period in 2004. The change was mainly due to an increase in rates received on loans and investments as we increased our prime rate by a total of 100 basis points during the first half of 2005. We also emphasized spread income and disposed of certain low yielding assets in the first and second quarters of 2004 and reinvested the proceeds from the amortization of our investment portfolio into loan production. Average loans outstanding increased from 78.3 percent of average interest-earning assets in the first half of 2004 to 82.7 percent of average interest-earning assets in the first half of 2005. The net interest margin also increased by 77 basis points to 4.80 percent for the six months ended June 30, 2005, from 4.03 percent for the same period in 2004, due to an increase in the volume of interest-earning assets with higher interest rates.

Total interest income increased \$16.0 million, or 51.0 percent, to \$47.5 million for the three months ended June 30, 2005, from \$31.5 million for the three months ended June 30, 2004. The increase was the result of a yield increase of 152 basis points on average interest-earning assets and an increase in average interest-earning assets of \$408.0 million, or 17.1 percent, to \$2.79 billion, compared to \$2.39 billion a year ago. Total interest income increased \$37.1 million, or 69.4 percent, to \$90.6 million for the six months ended June 30, 2005, from \$53.5 million for the six months ended June 30, 2004. The increase was the result of a yield increase of 132 basis points on average interest-earning assets and an increase in average interest-earning assets of \$730.7 million, or 35.9 percent, to \$2.77 billion, compared to \$2.03 billion a year ago.

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Total interest expense increased \$6.0 million, or 79.9 percent, to \$13.5 million for the three months ended June 30, 2005, from \$7.5 million for the three months ended June 30, 2004. The increase reflects an increase in average interest-bearing liabilities and higher interest rates paid to depositors. Average interest-bearing liabilities increased by \$288.6 million, or 17.3 percent, to \$1.96 billion, compared to \$1.67 billion a year ago. The cost of average interest-bearing liabilities increased to 2.75 percent for the three months ended June 30, 2005, compared to 1.80 percent for the same period in 2004. Total interest expense increased \$12.2 million, or 96.1 percent, to \$24.8 million for the six months ended June 30, 2005, from \$12.7 million for the six months ended June 30, 2004. The increase reflects an increase in interest-bearing liabilities and higher interest rates paid to depositors. Average interest-bearing liabilities increased by \$519.3 million, or 36.5 percent, to \$1.94 billion, compared to \$1.42 billion a year ago. The cost of average interest-bearing liabilities increased to 2.57 percent for the six months ended June 30, 2005, compared to 1.79 percent for the same period in 2004.

The following tables present the average balances of assets, liabilities and shareholders' equity; the amount of interest income or interest expense; the average yield or rate for each category of interest-earning assets and interest-bearing liabilities; and the net interest spread and the net interest margin for the periods indicated. All average balances are daily average balances.

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|   | June 30, 2005      |                         | Three Months Ended |                    | June 30, 2004           |                    |
|---|--------------------|-------------------------|--------------------|--------------------|-------------------------|--------------------|
|   | Average Balance    | Interest Income/Expense | Average Yield/Rate | Average Balance    | Interest Income/Expense | Average Yield/Rate |
| <b>Assets</b>   |                    |                         |                    |                    |                         |                    |
| Interest-Earning Assets:                              |                    |                         |                    |                    |                         |                    |
| Gross Loans, Net of Deferred Loan Fees <sup>(1)</sup> | \$2,334,803        | \$42,650                | 7.33%              | \$1,909,491        | \$26,984                | 5.68%              |
| Municipal Securities <sup>(2)</sup>                   | 73,223             | 780                     | 6.57%              | 70,101             | 737                     | 6.51%              |
| Obligations of Other U.S. Government Agencies         | 97,953             | 933                     | 3.82%              | 96,901             | 872                     | 3.62%              |
| Other Debt Securities                                 | 246,536            | 2,690                   | 4.38%              | 274,190            | 2,568                   | 3.77%              |
| Equity Securities                                     | 23,618             | 330                     | 5.60%              | 15,453             | 247                     | 6.43%              |
| Federal Funds Sold                                    | 16,941             | 123                     | 2.91%              | 19,031             | 50                      | 1.06%              |
| Interest-Earning Deposits                             | 69                 | 1                       | 3.57%              |                    |                         |                    |
| <b>Total Interest-Earning Assets</b>                  | <b>2,793,143</b>   | <b>47,507</b>           | <b>6.82%</b>       | <b>2,385,167</b>   | <b>31,458</b>           | <b>5.30%</b>       |
| Non-Interest-Earning Assets:                          |                    |                         |                    |                    |                         |                    |
| Cash and Cash Equivalents                             | 90,351             |                         |                    | 79,118             |                         |                    |
| Allowance for Loan Losses                             | (22,271)           |                         |                    | (20,246)           |                         |                    |
| Premises and Equipment, Net                           | 20,877             |                         |                    | 13,820             |                         |                    |
| Accrued Interest Receivable                           | 12,448             |                         |                    | 8,260              |                         |                    |
| Other Assets  | 274,447            |                         |                    | 203,811            |                         |                    |
| <b>Total Non-Interest-Earning Assets</b>              | <b>375,852</b>     |                         |                    | <b>284,763</b>     |                         |                    |
| <b>Total Assets</b>                                   | <b>\$3,168,995</b> |                         |                    | <b>\$2,669,930</b> |                         |                    |
| <b>Liabilities and Shareholders Equity</b>            |                    |                         |                    |                    |                         |                    |
| Interest-Bearing Liabilities:                         |                    |                         |                    |                    |                         |                    |
| Deposits:   |                    |                         |                    |                    |                         |                    |
| Money Market Checking                                 | \$ 539,229         | 3,084                   | 2.29%              | \$ 430,468         | 1,720                   | 1.61%              |
| Savings   | 143,948            | 548                     | 1.53%              | 131,049            | 404                     | 1.24%              |
| Time Deposits of \$100,000 or More                    | 875,297            | 6,423                   | 2.94%              | 612,487            | 2,554                   | 1.68%              |

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|  |                    |                 |              |                    |                 |              |
|--|--------------------|-----------------|--------------|--------------------|-----------------|--------------|
| Other Time Deposits                              | 225,961            | 1,290           | 2.29%        | 260,802            | 1,238           | 1.91%        |
| Other Borrowed Funds                             | 176,552            | 2,117           | 4.81%        | 237,565            | 1,568           | 2.65%        |
| <b>Total Interest-Bearing Liabilities</b>        | <b>1,960,987</b>   | <b>13,462</b>   | <b>2.75%</b> | <b>1,672,371</b>   | <b>7,484</b>    | <b>1.80%</b> |
| <b>Non-Interest-Bearing Liabilities:</b>         |                    |                 |              |                    |                 |              |
| Demand Deposits                                  | 758,451            |                 |              | 685,644            |                 |              |
| Other Liabilities                                | 33,092             |                 |              | 9,150              |                 |              |
| <b>Total Non-Interest-Bearing Liabilities</b>    | <b>791,543</b>     |                 |              | <b>694,794</b>     |                 |              |
| <b>Total Liabilities</b>                         | <b>2,752,530</b>   |                 |              | <b>2,367,165</b>   |                 |              |
| <b>Shareholders Equity</b>                       | <b>416,465</b>     |                 |              | <b>302,765</b>     |                 |              |
| <b>Total Liabilities and Shareholders Equity</b> | <b>\$3,168,995</b> |                 |              | <b>\$2,669,930</b> |                 |              |
| <b>Net Interest Income</b>                       |                    | <b>\$34,045</b> |              |                    | <b>\$23,974</b> |              |
| <b>Net Interest Spread <sup>(3)</sup></b>        |                    |                 | <b>4.07%</b> |                    |                 | <b>3.50%</b> |
| <b>Net Interest Margin <sup>(4)</sup></b>        |                    |                 | <b>4.89%</b> |                    |                 | <b>4.04%</b> |

*(1) Loans are net of deferred fees and related direct costs, but excluding the allowance for loan losses. Non-accrual loans are included in the average loan balance. Loan fees have been included in the calculation of interest income. Loan fees were \$1.7 million and \$1.6 million for the three months*

*ended June 30,  
2005 and 2004,  
respectively.*

- (2) Yields on  
tax-exempt  
income have  
been computed  
on a  
tax-equivalent  
basis using a  
rate of  
35 percent.*
- (3) Represents the  
average rate  
earned on  
interest-earning  
assets less the  
average rate  
paid on  
interest-bearing  
liabilities.*
- (4) Represents  
annualized net  
interest income  
as a percentage  
of average  
interest-earning  
assets.*

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|  | <b>Six Months Ended</b>       |   |                                    |                            |   |                                    |
|--|-------------------------------|---|------------------------------------|----------------------------|---|------------------------------------|
|  | <b>June 30, 2005</b>          |   | <b>June 30, 2004</b>               |                            |   |                                    |
|  | <b>Average<br/>Balance</b>    | <b>Interest<br/>Income/<br/>Expense</b> | <b>Average<br/>Yield/<br/>Rate</b> | <b>Average<br/>Balance</b> | <b>Interest<br/>Income/<br/>Expense</b> | <b>Average<br/>Yield/<br/>Rate</b> |
|  | <i>(Dollars in Thousands)</i> |   |                                    |                            |   |                                    |
| <b>Assets</b>  |                               |   |                                    |                            |   |                                    |
| Interest-Earning Assets:                                 |                               |   |                                    |                            |   |                                    |
| Gross Loans, Net of<br>Deferred Loan Fees <sup>(1)</sup> | \$2,287,253                   | \$80,725                                | 7.12%                              | \$1,592,785                | \$45,164                                | 5.70%                              |
| Municipal Securities <sup>(2)</sup>                      | 73,634                        | 1,556                                   | 6.56%                              | 68,069                     | 1,446                                   | 6.57%                              |
| Obligations of Other U.S.<br>Government Agencies         | 97,090                        | 1,867                                   | 3.88%                              | 86,684                     | 1,549                                   | 3.59%                              |
| Other Debt Securities                                    | 248,511                       | 5,355                                   | 4.35%                              | 259,918                    | 4,888                                   | 3.78%                              |
| Equity Securities  | 22,794                        | 603                                     | 5.33%                              | 12,906                     | 334                                     | 5.20%                              |
| Federal Funds Sold                                       | 35,797                        | 458                                     | 2.58%                              | 13,542                     | 72                                      | 1.07%                              |
| Interest-Earning Deposits                                | 35                            | 1                                       | 1.79%                              | 478                        | 3                                       | 1.26%                              |
| <b>Total Interest-Earning<br/>Assets</b>                 | <b>2,765,114</b>              | <b>90,565</b>                           | <b>6.60%</b>                       | <b>2,034,382</b>           | <b>53,456</b>                           | <b>5.28%</b>                       |
| Non-Interest-Earning<br>Assets:                          |                               |   |                                    |                            |   |                                    |
| Cash and Cash<br>Equivalents                             | 87,520                        |   |                                    | 95,133                     |   |                                    |
| Allowance for Loan<br>Losses                             | (22,499)                      |   |                                    | (16,346)                   |   |                                    |
| Premises and Equipment,<br>Net                           | 20,586                        |   |                                    | 15,777                     |   |                                    |
| Accrued Interest<br>Receivable                           | 11,781                        |   |                                    | 8,850                      |   |                                    |
| Other Assets   | 273,917                       |   |                                    | 82,412                     |   |                                    |
| <b>Total<br/>Non-Interest-Earning<br/>Assets</b>         | <b>371,305</b>                |   |                                    | <b>185,826</b>             |   |                                    |
| <b>Total Assets</b>                                      | <b>\$3,136,419</b>            |   |                                    | <b>\$2,220,208</b>         |   |                                    |
| <b>Liabilities and Shareholders Equity</b>               |                               |   |                                    |                            |   |                                    |
| Interest-Bearing<br>Liabilities:                         |                               |   |                                    |                            |   |                                    |
| Deposits:  |                               |   |                                    |                            |   |                                    |
| Money Market Checking                                    | \$ 565,574                    | 6,092                                   | 2.17%                              | \$ 345,575                 | 2,730                                   | 1.59%                              |
| Savings  | 147,087                       | 1,104                                   | 1.51%                              | 112,382                    | 722                                     | 1.29%                              |
| Time Deposits of<br>\$100,000 or More                    | 836,435                       | 11,425                                  | 2.75%                              | 506,187                    | 4,302                                   | 1.71%                              |



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|  |                    |                 |              |                    |                 |              |
|--|--------------------|-----------------|--------------|--------------------|-----------------|--------------|
| Other Time Deposits                              | 230,287            | 2,535           | 2.22%        | 249,840            | 2,438           | 1.96%        |
| Other Borrowed Funds                             | 164,406            | 3,653           | 4.48%        | 210,547            | 2,462           | 2.35%        |
| <b>Total Interest-Bearing Liabilities</b>        | <b>1,943,789</b>   | <b>24,809</b>   | <b>2.57%</b> | <b>1,424,531</b>   | <b>12,654</b>   | <b>1.79%</b> |
| <b>Non-Interest-Bearing Liabilities:</b>         |                    |                 |              |                    |                 |              |
| Demand Deposits                                  | 751,740            |                 |              | 557,638            |                 |              |
| Other Liabilities                                | 29,620             |                 |              | 13,550             |                 |              |
| <b>Total Non-Interest-Bearing Liabilities</b>    | <b>781,360</b>     |                 |              | <b>571,188</b>     |                 |              |
| <b>Total Liabilities</b>                         | <b>2,725,149</b>   |                 |              | <b>1,995,719</b>   |                 |              |
| <b>Shareholders Equity</b>                       | <b>411,270</b>     |                 |              | <b>224,489</b>     |                 |              |
| <b>Total Liabilities and Shareholders Equity</b> | <b>\$3,136,419</b> |                 |              | <b>\$2,220,208</b> |                 |              |
| <b>Net Interest Income</b>                       |                    | <b>\$65,756</b> |              |                    | <b>\$40,802</b> |              |
| <b>Net Interest Spread <sup>(3)</sup></b>        |                    |                 | <b>4.03%</b> |                    |                 | <b>3.49%</b> |
| <b>Net Interest Margin <sup>(4)</sup></b>        |                    |                 | <b>4.80%</b> |                    |                 | <b>4.03%</b> |

*(1) Loans are net of deferred fees and related direct costs, but excluding the allowance for loan losses. Non-accrual loans are included in the average loan balance. Loan fees have been included in the calculation of interest income. Loan fees were \$3.0 million and \$2.5 million for the six months*

*ended June 30,  
2005 and 2004,  
respectively.*

- (2) Yields on  
tax-exempt  
income have  
been computed  
on a  
tax-equivalent  
basis using a  
rate of  
35 percent.*
- (3) Represents the  
average rate  
earned on  
interest-earning  
assets less the  
average rate  
paid on  
interest-bearing  
liabilities.*
- (4) Represents  
annualized net  
interest income  
as a percentage  
of average  
interest-earning  
assets.*

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The following tables show changes in interest income and interest expense and the amounts attributable to variations in interest rates and volumes for the periods indicated. The variances attributable to simultaneous volume and rate changes have been allocated to the change due to volume and the change due to rate categories in proportion to the relationship of the absolute dollar amount attributable solely to the change in volume and to the change in rate.

|   | <b>Three Months Ended<br/>June 30, 2005 vs. 2004<br/>Increases (Decreases)<br/>Due to Change in</b> |                                    |                 |
|---|---|------------------------------------|-----------------|
|   | <b>Volume</b>   | <b>Rate<br/>(In<br/>Thousands)</b> | <b>Total</b>    |
| <b>Interest Income:</b>                       |   |                                    |                 |
| Gross Loans, Net of Deferred Loan Fees        | \$6,753   | \$ 8,913                           | \$15,666        |
| Municipal Securities                          | 31  | 12                                 | 43              |
| Obligations of Other U.S. Government Agencies | 9   | 52                                 | 61              |
| Other Debt Securities                         | (279)   | 401                                | 122             |
| Equity Securities                             | 117   | (34)                               | 83              |
| Federal Funds Sold                            | (7)   | 80                                 | 73              |
| Interest-Earning Deposits                     | (1)   | 2                                  | 1               |
| <b>Total Interest Income</b>                  | <b>6,623</b>  | <b>9,426</b>                       | <b>16,049</b>   |
| <b>Interest Expense:</b>                      |   |                                    |                 |
| Money Market Checking                         | 503   | 861                                | 1,364           |
| Savings                                       | 42  | 102                                | 144             |
| Time Deposits of \$100,000 or More            | 1,397   | 2,472                              | 3,869           |
| Other Time Deposits                           | (180)   | 232                                | 52              |
| Other Borrowed Funds                          | (484)   | 1,033                              | 549             |
| <b>Total Interest Expense</b>                 | <b>1,278</b>  | <b>4,700</b>                       | <b>5,978</b>    |
| <b>Change in Net Interest Income</b>          | <b>\$5,345</b>  | <b>\$ 4,726</b>                    | <b>\$10,071</b> |

|   | <b>Six Months Ended<br/>June 30, 2005 vs. 2004<br/>Increases (Decreases)<br/>Due to Change in</b> |                                    |              |
|---|---|------------------------------------|--------------|
|   | <b>Volume</b>   | <b>Rate<br/>(In<br/>Thousands)</b> | <b>Total</b> |
| <b>Interest Income:</b>                       |   |                                    |              |
| Gross Loans, Net of Deferred Loan Fees        | \$22,822  | \$ 12,739                          | \$35,561     |
| Municipal Securities                          | 122   | (12)                               | 110          |
| Obligations of Other U.S. Government Agencies | 196   | 122                                | 318          |
| Other Debt Securities                         | (218)   | 685                                | 467          |
| Equity Securities                             | 261   | 8                                  | 269          |
| Federal Funds Sold                            | 208   | 178                                | 386          |

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|                                      |                 |                 |                 |
|--------------------------------------|-----------------|-----------------|-----------------|
| Interest-Earning Deposits            | (7)             | 5               | (2)             |
| Total Interest Income                | 23,384          | 13,725          | 37,109          |
| <b>Interest Expense:</b>             |                 |                 |                 |
| Money Market Checking                | 2,142           | 1,220           | 3,362           |
| Savings                              | 248             | 134             | 382             |
| Time Deposits of \$100,000 or More   | 3,689           | 3,434           | 7,123           |
| Other Time Deposits                  | (197)           | 294             | 97              |
| Other Borrowed Funds                 | (632)           | 1,823           | 1,191           |
| Total Interest Expense               | 5,250           | 6,905           | 12,155          |
| <b>Change in Net Interest Income</b> | <b>\$18,134</b> | <b>\$ 6,820</b> | <b>\$24,954</b> |

Table of Contents**Provision for Credit Losses**

Provisions to the allowance for loan losses and allowance for off-balance sheet items, such as unfunded loan commitments and letters of credit, are made at least quarterly, in anticipation of probable loan losses. The provision is based on the allowance need, which is calculated using a formula designed to provide adequate allowances for anticipated losses and allowance for off-balance sheet items. See Allowance for Loan Losses and Allowance for Off-Balance Sheet Items section below for further discussion on methodologies used to determine the allowance for loan losses and allowance for off-balance sheet items.

For the three months ended June 30, 2005, the provision for credit losses was \$450,000, compared to \$850,000 for the three months ended June 30, 2004, a decrease of 47.1 percent. For the three months ended June 30, 2005, net charge-offs were \$1.0 million, compared to \$81,000 net charge-offs in the first quarter of 2005 and \$211,000 net recoveries in the second quarter of 2004. The level of non-performing loans remained substantially unchanged during 2005, as the balances were \$6.0 million at December 31, 2004 and \$6.1 million at June 30, 2005.

For the six months ended June 30, 2005, the provision for credit losses was \$586,000, compared to \$1.8 million for the six months ended June 30, 2004, a decrease of 66.5 percent. The decrease in the provision was caused by the low level of net charge-offs in recent quarters, which caused historical loss percentages to decrease. For the six months ended June 30, 2005, net charge-offs were \$1.1 million, compared to \$1.6 million net charge-offs for the six months ended June 30, 2004.

**Non-Interest Income**

The following tables set forth the various components of non-interest income for the periods indicated:

|  | <b>Three Months Ended</b>     |                | <b>Increase (Decrease)</b> |                   |
|--|-------------------------------|----------------|----------------------------|-------------------|
|  | <b>2005</b>                   | <b>2004</b>    | <b>Amount</b>              | <b>Percentage</b> |
|  | <i>(Dollars in Thousands)</i> |                |                            |                   |
| Service Charges on Deposit Accounts            | \$3,868                       | \$3,524        | \$ 344                     | 9.8%              |
| Trade Finance Fees                             | 1,036                         | 1,030          | 6                          | 0.6%              |
| Remittance Fees                                | 550                           | 436            | 114                        | 26.1%             |
| Other Service Charges and Fees                 | 789                           | 560            | 229                        | 40.9%             |
| Bank-Owned Life Insurance Income               | 210                           | 183            | 27                         | 14.8%             |
| Increase in Fair Value of Derivatives          | 370                           | (57)           | 427                        | (749.1%)          |
| Other Income                                   | 554                           | 492            | 62                         | 12.6%             |
| Gain on Sales of Loans                         | 56                            | 833            | (777)                      | (93.3%)           |
| Gain on Sales of Securities Available for Sale | 14                            | 6              | 8                          | 133.3%            |
| <b>Total Non-Interest Income</b>               | <b>\$7,447</b>                | <b>\$7,007</b> | <b>\$ 440</b>              | <b>6.3%</b>       |

|                                       | <b>Six Months Ended</b>       |             | <b>Increase (Decrease)</b> |                   |
|---------------------------------------|-------------------------------|-------------|----------------------------|-------------------|
|                                       | <b>2005</b>                   | <b>2004</b> | <b>Amount</b>              | <b>Percentage</b> |
|                                       | <i>(Dollars in Thousands)</i> |             |                            |                   |
| Service Charges on Deposit Accounts   | \$ 7,598                      | \$ 6,191    | \$1,407                    | 22.7%             |
| Trade Finance Fees                    | 1,981                         | 1,835       | 146                        | 8.0%              |
| Remittance Fees                       | 1,018                         | 693         | 325                        | 46.9%             |
| Other Service Charges and Fees        | 1,519                         | 821         | 698                        | 85.0%             |
| Bank-Owned Life Insurance Income      | 415                           | 297         | 118                        | 39.7%             |
| Increase in Fair Value of Derivatives | 789                           | 23          | 766                        | 3,330.4%          |
| Other Income                          | 1,175                         | 741         | 434                        | 58.6%             |
| Gain on Sales of Loans                | 364                           | 1,302       | (938)                      | (72.0%)           |

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|  |                 |                 |                |              |
|--|-----------------|-----------------|----------------|--------------|
| Gain on Sales of Securities Available for Sale | 96              | 9               | 87             | 966.7%       |
| <b>Total Non-Interest Income</b>               | <b>\$14,955</b> | <b>\$11,912</b> | <b>\$3,043</b> | <b>25.5%</b> |

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|   | <b>Six Months Ended</b> |                 | <b>Increase (Decrease)</b>    |                   |
|---|-------------------------|-----------------|-------------------------------|-------------------|
|   | <b>2005</b>             | <b>2004</b>     | <b>Amount</b>                 | <b>Percentage</b> |
|   |                         |                 | <i>(Dollars in Thousands)</i> |                   |
| Salaries and Employee Benefits            | \$17,712                | \$13,574        | \$ 4,138                      | 30.5%             |
| Occupancy and Equipment                   | 4,402                   | 3,517           | 885                           | 25.2%             |
| Data Processing                           | 2,410                   | 1,884           | 526                           | 27.9%             |
| Supplies and Communications               | 1,308                   | 978             | 330                           | 33.7%             |
| Professional Fees                         | 1,039                   | 883             | 156                           | 17.7%             |
| Advertising and Promotional Expense       | 1,257                   | 1,423           | (166)                         | (11.7%)           |
| Amortization of Core Deposit Intangible   | 1,446                   | 499             | 947                           | 189.8%            |
| Decrease in Fair Value of Embedded Option | 575                     |                 | 575                           |                   |
| Other Operating Expense                   | 3,977                   | 3,640           | 337                           | 9.3%              |
| Merger-Related Expenses                   | (509)                   | 1,728           | (2,237)                       | (129.5%)          |
| <b>Total Non-Interest Expenses</b>        | <b>\$33,617</b>         | <b>\$28,126</b> | <b>\$ 5,491</b>               | <b>19.5%</b>      |

For the three and six months ended June 30, 2005, non-interest expenses were \$16.2 million and \$33.6 million, respectively, a decrease of \$1.6 million, or 8.7 percent, and an increase of \$5.5 million, or 19.5 percent, respectively, from \$17.8 million and \$28.1 million, respectively, for the three and six months ended June 30, 2004. These fluctuations were primarily due to the PUB merger, which closed on April 30, 2004.

Salaries and employee benefits expenses increased by \$621,000, or 7.8 percent, and \$4.1 million, or 30.5 percent, respectively, from \$7.9 million and \$13.6 million, respectively, for the three and six months ended June 30, 2004 to \$8.5 million and \$17.7 million, respectively, for three and six months ended June 30, 2005. The increase was due to an increase in the number of employees following the acquisition of PUB and increases in bonus accruals of \$700,000 and \$1.6 million for the three and six months ended June 30, 2005.

Occupancy and equipment expenses increased by \$39,000, or 1.8 percent, and \$885,000, or 25.2 percent, respectively, from \$2.1 million and \$3.5 million, respectively, for the three and six months ended June 30, 2004 to \$2.2 million and \$4.4 million, respectively, for three and six months ended June 30, 2005. This increase was due to the acquisition of twelve former PUB branches.

Data processing expense increased by \$181,000, or 17.0 percent, and \$526,000, or 27.9 percent, respectively, from \$1.1 million and \$1.9 million, respectively, for the three and six months ended June 30, 2004 to \$1.2 million and \$2.4 million, respectively, for three and six months ended June 30, 2005. The additional expense was incurred mainly due to an increase in loan and deposits volume related to the acquisition.

Core deposit premium amortization increased by \$245,000, or 52.2 percent, and \$947,000, or 189.8 percent, respectively, from \$469,000 and \$499,000, respectively, for the three and six months ended June 30, 2004 to \$714,000 and \$1.4 million, respectively, for three and six months ended June 30, 2005. The increase is attributable to the core deposits acquired from PUB.

For the three and six months ended June 30, 2005, merger-related expenses were a credit of \$509,000, compared to \$1.7 million for the three and six months ended June 30, 2004, a decrease of 129.5 percent. The \$509,000 credit in merger-related expenses for the three and six months ended June 30, 2005 was due to the reversal of restructuring reserves that were no longer needed.

**Provision for Income Taxes**

For the three and six months ended June 30, 2005, we recognized provisions for income taxes of \$9.8 million and \$18.1 million, respectively, on net income before tax of \$24.8 million and \$46.5 million, respectively, representing an effective tax rate of 39.44 percent and 39.00 percent, respectively. The tax rate for the three- and six-month periods ended June 30, 2004 was 39.00 percent.



**Table of Contents****FINANCIAL CONDITION****Summary of Changes in Balance Sheets June 30, 2005 Compared to December 31, 2004**

As of June 30, 2005, total assets were \$3.25 billion, an increase of \$147.6 million, or 4.8 percent, from the December 31, 2004 balance of \$3.10 billion. The increase in assets was mainly funded by deposits, which increased by \$31.2 million, or 1.2 percent, to \$2.56 billion at June 30, 2005 from \$2.53 billion at December 31, 2004, and additional borrowings, which increased by \$78.4 million, or 113.1 percent, to \$147.6 million at June 30, 2005 from \$69.3 million at December 31, 2004. Loans increased by \$169.2 million, or 7.6 percent, to \$2.40 billion at June 30, 2005 from \$2.23 billion at December 31, 2004. Investment securities decreased \$7.1 million, or 1.7 percent, to \$411.8 million at June 30, 2005 from \$419.0 million at December 31, 2004.

**Investment Securities**

Securities are classified as held to maturity or available for sale in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Those securities that we have the ability and intent to hold to maturity are classified as held to maturity securities. All other securities are classified as available for sale. There were no trading securities at June 30, 2005. Securities classified as held to maturity are stated at cost, adjusted for amortization of premiums and accretion of discounts, and available for sale securities are stated at fair value. The securities currently held consist primarily of U.S. agency securities, mortgage-backed securities, collateralized mortgage obligations and municipal bonds.

As of June 30, 2005, held to maturity securities totaled \$1.1 million and available for sale securities totaled \$410.8 million, compared to \$1.1 million and \$417.9 million, respectively, at December 31, 2004.

|  | June 30, 2005     |                  |   | December 31, 2004 |                  |                              |
|--|-------------------|------------------|---|-------------------|------------------|------------------------------|
|  | Amortized<br>Cost | Fair<br>Value    | Unrealized<br>Gain<br>(Loss)<br><i>(In Thousands)</i> | Amortized<br>Cost | Fair<br>Value    | Unrealized<br>Gain<br>(Loss) |
| <b>Held to Maturity:</b>               |                   |                  |   |                   |                  |                              |
| Municipal Bonds                        | \$ 692            | \$ 692           | \$  | \$ 691            | \$ 691           | \$                           |
| Mortgage-Backed<br>Securities          | 371               | 377              | 6   | 399               | 402              | 3                            |
| <b>Total Held to Maturity</b>          | <b>\$ 1,063</b>   | <b>\$ 1,069</b>  | <b>\$ 6</b>   | <b>\$ 1,090</b>   | <b>\$ 1,093</b>  | <b>\$ 3</b>                  |
| <b>Available for Sale:</b>             |                   |                  |   |                   |                  |                              |
| Mortgage-Backed<br>Securities          | \$144,235         | \$144,312        | \$ 77   | \$148,706         | \$149,174        | \$ 468                       |
| U.S. Government<br>Agency Securities   | 94,511            | 94,258           | (253)   | 89,345            | 89,677           | 332                          |
| Collateralized Mortgage<br>Obligations | 84,967            | 84,163           | (804)   | 93,172            | 92,539           | (633)                        |
| Municipal Bonds                        | 72,245            | 74,599           | 2,354   | 71,771            | 73,616           | 1,845                        |
| Corporate Bonds                        | 8,308             | 8,330            | 22  | 8,380             | 8,444            | 64                           |
| Other Securities                       | 5,111             | 5,116            | 5   | 4,437             | 4,433            | (4)                          |
| <b>Total Available for Sale</b>        | <b>\$409,377</b>  | <b>\$410,778</b> | <b>\$1,401</b>  | <b>\$415,811</b>  | <b>\$417,883</b> | <b>\$2,072</b>               |

All individual securities that have been in a continuous unrealized loss position for 12 months or longer at June 30, 2005 had investment grade ratings upon purchase. The issuers of these securities have not, to our knowledge, established any cause for default on these securities and the various rating agencies have reaffirmed these securities

long-term investment grade status at June 30, 2005. These securities have fluctuated in value since their purchase dates as market interest rates have fluctuated. However, the Company has the ability, and management intends to hold these securities until their fair values recover to cost. Therefore, in management's opinion, all securities that have been in a continuous unrealized loss position for the past 12 months or longer as of June 30, 2005 are not other-than-temporarily impaired, and therefore, no impairment charges as of June 30, 2005 are warranted.

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The following table summarizes the maturity and/or repricing schedule for investment securities and their weighted-average yield as of June 30, 2005:

|   | Within<br>One Year |              | After One<br>But Within<br>Five Years |              | After Five<br>But Within<br>Ten Years |              | After<br>Ten Years |              |
|---|--------------------|--------------|---------------------------------------|--------------|---------------------------------------|--------------|--------------------|--------------|
|   | Amount             | Yield        | Amount                                | Yield        | Amount                                | Yield        | Amount             | Yield        |
| Mortgage-Backed<br>Securities <sup>(1)</sup>                                  | \$ 63,216          | 4.30%        | \$ 48,950                             | 4.65%        | \$ 27,266                             | 4.76%        | \$ 5,251           | 3.97%        |
| Obligations of<br>Other U.S.<br>Government<br>Agencies                        | 72,430             | 3.72%        | 21,828                                | 3.82%        |                                       |              |                    | 3.72%        |
| Collateralized<br>Mortgage<br>Obligations <sup>(1)</sup>                      | 19,405             | 3.92%        | 57,310                                | 4.33%        | 7,448                                 | 3.99%        |                    |              |
| Obligations of<br>State and Local<br>Political<br>Subdivisions <sup>(2)</sup> | 532                | 7.05%        | 1,484                                 | 4.82%        | 5,214                                 | 5.75%        | 68,061             | 6.38%        |
| Corporate Bonds   |                    |              | 8,330                                 | 4.38%        |                                       |              |                    |              |
| Other Securities  | 5,116              | 6.48%        |                                       |              |                                       |              |                    |              |
|   | <b>\$160,699</b>   | <b>4.07%</b> | <b>\$137,902</b>                      | <b>4.37%</b> | <b>\$39,928</b>                       | <b>4.75%</b> | <b>\$73,312</b>    | <b>6.29%</b> |

<sup>(1)</sup> Collateralized mortgage obligations and mortgage-backed securities have contractual maturities through 2034. The above table is based on the expected prepayment schedule.

<sup>(2)</sup> The yield on obligations of state and local political subdivisions has been computed on a tax-equivalent

basis, using an effective marginal rate of 32 percent.

### Loan Portfolio

All loans are carried at face amount, less principal repayments collected, net of deferred loan origination fees and costs, and the allowance for loan losses. Interest on all loans is accrued daily on a simple interest basis. Once a loan is placed on non-accrual status, the accrual of interest is discontinued and previously accrued interest is reversed. Loans are placed on non-accrual status when principal and interest on a loan is past due 90 days or more, unless a loan is both well secured and in the process of collection.

The following table shows the loan composition by type, including loans held for sale, as of the dates indicated.

|  | June 30,<br>2005   | December 31,<br>2004 | Increase (Decrease)           |               |
|--|--------------------|----------------------|-------------------------------|---------------|
|  |                    |                      | Amount                        | Percentage    |
|  |                    |                      | <i>(Dollars in Thousands)</i> |               |
| Real Estate Loans:                           |                    |                      |                               |               |
| Commercial Property                          | \$ 726,977         | \$ 783,539           | \$ (56,562)                   | (7.2%)        |
| Construction                                 | 124,466            | 92,521               | 31,945                        | 34.5%         |
| Residential Property                         | 83,346             | 80,786               | 2,560                         | 3.2%          |
| <b>Total Real Estate Loans</b>               | <b>934,789</b>     | <b>956,846</b>       | <b>(22,057)</b>               | <b>(2.3%)</b> |
| Commercial and Industrial Loans:             |                    |                      |                               |               |
| Commercial Term Loans                        | 884,115            | 754,108              | 130,007                       | 17.2%         |
| Commercial Lines of Credit                   | 243,186            | 201,940              | 41,246                        | 20.4%         |
| SBA Loans <sup>(1)</sup>                     | 179,590            | 166,285              | 13,305                        | 8.0%          |
| International Loans                          | 101,577            | 95,936               | 5,641                         | 5.9%          |
| <b>Total Commercial and Industrial Loans</b> | <b>1,408,468</b>   | <b>1,218,269</b>     | <b>190,199</b>                | <b>15.6%</b>  |
| Consumer Loans                               | 87,287             | 87,526               | (239)                         | (0.3%)        |
| <b>Total Loans Gross</b>                     | <b>2,430,544</b>   | <b>2,262,641</b>     | <b>167,903</b>                | <b>7.4%</b>   |
| Deferred Loan Fees                           | (4,459)            | (5,097)              | 638                           | (12.5%)       |
| Allowance for Loan Losses                    | (22,049)           | (22,702)             | 653                           | (2.9%)        |
| <b>Net Loans Receivable</b>                  | <b>\$2,404,036</b> | <b>\$2,234,842</b>   | <b>\$169,194</b>              | <b>7.6%</b>   |

<sup>(1)</sup> Amount includes loans held for sale, at the lower of cost or market, of \$875,000 and \$3.9 million at June 30, 2005 and December 31, 2004, respectively.



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At June 30, 2005 and December 31, 2004, loans, net of deferred loan fees and allowance for loan losses, totaled \$2.40 billion and \$2.23 billion, respectively. Real estate loans, composed of commercial property, residential property and construction loans, decreased \$22.1 million, or 2.3 percent, to \$934.8 million at June 30, 2005 from \$956.8 million at December 31, 2004. The decrease in the real estate loan portfolio reflects management's emphasis on controlling exposure to a concentration in commercial real estate loans.

Total commercial and industrial loans, composed of commercial term loans and lines of credit, trade financing and SBA loans, were \$1.41 billion at June 30, 2005, which represented an increase of \$190.2 million, or 15.6 percent, from \$1.22 billion at December 31, 2004. The increase was primarily due to growth in commercial term loans and commercial lines of credit.

Consumer loans decreased \$239,000, or 0.3 percent, to \$87.3 million at June 30, 2005 from \$87.5 million at December 31, 2004.

As of June 30, 2005, there were \$252.9 million of loans outstanding, or 10.41 percent of total gross loans outstanding, to borrowers who were involved in property leasing, primarily commercial real estate. There was no other concentration of loans to any one type of industry exceeding 10 percent of total gross loans.

**Non-Performing Assets**

Non-performing assets consist of loans on non-accrual status, loans 90 days or more past due and still accruing interest, loans restructured where the terms of repayment have been renegotiated resulting in a reduction or deferral of interest or principal, and other real estate owned (OREO). Loans are generally placed on non-accrual status when they become 90 days past due unless management believes the loan is adequately collateralized and in the process of collection. Loans may be restructured by management when a borrower has experienced some change in financial status, causing an inability to meet the original repayment terms, and where we believe the borrower eventually will overcome those circumstances and repay the loan in full. OREO consists of properties acquired by foreclosure or similar means that management intends to offer for sale.

Management's classification of a loan as non-accrual is an indication that there is reasonable doubt as to the full collectibility of principal or interest on the loan; at this point, we stop recognizing income from the interest on the loan and reverse any uncollected interest that had been accrued but unpaid. These loans may or may not be collateralized, but collection efforts are continuously pursued.

The table below shows the composition of non-performing assets as of the dates indicated.

|   | <b>June 30,</b> | <b>December</b>               | <b>Increase/(Decrease)</b> |                   |
|---|-----------------|-------------------------------|----------------------------|-------------------|
|   | <b>2005</b>     | <b>31,</b>                    | <b>Amount</b>              | <b>Percentage</b> |
|   |                 | <b>2004</b>                   |                            |                   |
|   |                 | <i>(Dollars in Thousands)</i> |                            |                   |
| Non-Accrual Loans                                 | \$5,688         | \$5,806                       | \$(118)                    | (2.0%)            |
| Loans 90 Days or More Past Due and Still Accruing | 409             | 208                           | 201                        | 96.6%             |
| Total Non-Performing Loans                        | 6,097           | 6,014                         | 83                         | 1.4%              |
| Other Real Estate Owned                           |                 |                               |                            |                   |
| <b>Total Non-Performing Assets</b>                | <b>\$6,097</b>  | <b>\$6,014</b>                | <b>\$ 83</b>               | <b>1.4%</b>       |

At June 30, 2005, accruing loans 90 days past due or more were \$409,000, an increase of \$201,000 from \$208,000 at December 31, 2004. Non-accrual loans were \$5.7 million at June 30, 2005, a decrease of \$118,000 compared to \$5.8 million at December 31, 2004. The decrease was due to \$177,000 of payments received on non-accrual loans and \$3.4 million of loans returned to performing status, partially offset by \$3.5 million of loans migrating to non-performing status.



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**Allowance for Loan Losses and Allowance for Off-Balance Sheet Items**

The allowance for loan losses and allowance for off-balance sheet items, such as unfunded loan commitments and letters of credit, are maintained at levels that management believes are adequate to absorb probable loan losses inherent in various financial instruments. The adequacy of both allowances is determined through periodic evaluations of the loan portfolio and other pertinent factors, which are inherently subjective as the process calls for various significant estimates and assumptions. Among other factors, the estimates involve the amounts and timing of expected future cash flows and fair value of collateral on impaired loans, estimated losses on loans based on historical loss experience, various qualitative factors, and uncertainties in estimating losses and inherent risks in the various credit portfolios, which may be subject to substantial change.

On a quarterly basis, we utilize a classification migration model and individual loan review analysis tools as starting points for determining the adequacy of the allowance for loan losses and allowance for off-balance sheet items. Our loss migration analysis tracks twelve quarters of loan losses to determine historical loss experience in every classification category (i.e., pass, special mention, substandard and doubtful ) for each loan type, except consumer loans (automobile, mortgage and credit cards), which are analyzed as homogeneous loan pools. The individual loan review analysis is the other part of the allowance allocation process, applying specific monitoring policies and procedures in analyzing the existing loan portfolios. Further assignments are made based on general and specific economic conditions, as well as performance trends within specific portfolio segments and individual concentrations of credit.

As of June 30, 2005, the allowance for loan losses was \$22.0 million, a decrease of \$653,000, or 2.9 percent, compared to \$22.7 million at December 31, 2004. The decrease in the allowance for loan losses was caused by the low level of net charge-offs in recent quarters, which caused historical loss percentages to decrease. As of June 30, 2005, the allowance for off-balance sheet items was \$1.9 million, an increase of \$136,000, or 7.6 percent, compared to \$1.8 million at December 31, 2004.

The loan loss estimation is based on historical losses, and specific allocations of the allowance are performed on a quarterly basis. Adjustments to allowance allocations for specific segments of the loan portfolio may be made as a result thereof, based on the accuracy of forecasted loss amounts and other loan-related or policy-related issues.

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We determine the appropriate overall allowance for loan losses and allowance for off-balance sheet items based on the foregoing analysis, taking into account management's judgment. This methodology is reviewed on a periodic basis and modified as appropriate. Based on this analysis, including the aforementioned factors, we believe that the allowance for loan losses and allowance for off-balance sheet items are adequate as of June 30, 2005.

|  | <b>As of and for the Three Months Ended</b> |                           |                              |
|--|---|---------------------------|------------------------------|
|  | <b>June 30,<br/>2005</b>                    | <b>March 31,<br/>2005</b> | <b>December 31,<br/>2004</b> |
|  | <i>(Dollars in<br/>Thousands)</i>           |                           |                              |
| <b>Allowance for Loan Losses:</b>                                  |   |                           |                              |
| Balance at Beginning of Period                                     | \$ 22,621                                   | \$ 22,702                 | \$ 22,150                    |
| Actual Charge-Offs   | (2,378)                                     | (603)                     | (1,040)                      |
| Recoveries on Loans Previously Charged Off                         | 1,356                                       | 522                       | 435                          |
| Net Loan Charge-Offs   | (1,022)                                     | (81)                      | (605)                        |
| Provision Charged to Operating Expenses                            | 450   |                           | 1,157                        |
| <b>Balance at End of Period</b>                                    | <b>\$ 22,049</b>                            | <b>\$ 22,621</b>          | <b>\$ 22,702</b>             |
| <b>Allowance for Off-Balance Sheet Items:</b>                      |   |                           |                              |
| Balance at Beginning of Period                                     | \$ 1,936                                    | \$ 1,800                  | \$ 1,800                     |
| Provision Charged to Operating Expenses                            |   | 136                       |                              |
| <b>Balance at End of Period</b>                                    | <b>\$ 1,936</b>                             | <b>\$ 1,936</b>           | <b>\$ 1,800</b>              |
| <b>Ratios:</b>   |   |                           |                              |
| Net Loan Charge-Offs to Average Total Gross Loans<br>(1)           | 0.18%                                       | 0.01%                     | 0.11%                        |
| Net Loan Charge-Offs to Total Gross Loans at End of<br>Period (1)  | 0.17%                                       | 0.01%                     | 0.11%                        |
| Allowance for Loan Losses to Average Total Gross<br>Loans          | 0.94%                                       | 1.01%                     | 1.00%                        |
| Allowance for Loan Losses to Total Gross Loans at<br>End of Period | 0.91%                                       | 1.00%                     | 1.00%                        |
| Net Loan Charge-Offs to Allowance for Loan Losses<br>(1)           | 18.59%                                      | 1.45%                     | 10.60%                       |
| Net Loan Charge-Offs to Provision Charged to<br>Operating Expenses | 227.11%                                     |                           | 52.29%                       |
| Allowance for Loan Losses to Non-Performing Loans                  | 361.64%                                     | 327.94%                   | 377.49%                      |
| <b>Balances:</b>   |   |                           |                              |
| Average Total Gross Loans Outstanding During<br>Period             | \$2,334,803                                 | \$ 2,239,174              | \$2,269,170                  |
| Total Gross Loans Outstanding at End of Period                     | \$2,430,544                                 | \$ 2,257,267              | \$2,262,641                  |
| Non-Performing Loans at End of Period                              | \$ 6,097                                    | \$ 6,898                  | \$ 6,014                     |

(1) *Net loan  
charge-offs  
annualized to  
calculate the  
ratios.*

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|   | <b>As of and for the<br/>Six Months Ended June 30,<br/>2005</b> |               | <b>2004</b> |               |
|---|---|---------------|-------------|---------------|
|   | <i>(Dollars in Thousands)</i>                                   |               |             |               |
| <b>Allowance for Loan Losses:</b>   |   |               |             |               |
| Balance at Beginning of Period  | \$  | 22,702        | \$          | 13,349        |
| Allowance for Loan Losses - PUB Acquisition                               |   |               |             | 10,566        |
| Actual Charge-Offs  |   | (2,981)       |             | (2,837)       |
| Recoveries on Loans Previously Charged Off                                |   | 1,878         |             | 1,195         |
| Net Loan Charge-Offs  |   | (1,103)       |             | (1,642)       |
| Provision Charged to Operating Expenses                                   |   | 450           |             | 1,335         |
| <b>Balance at End of Period</b>   | <b>\$</b>   | <b>22,049</b> | <b>\$</b>   | <b>23,608</b> |
| <b>Allowance for Off-Balance Sheet Items:</b>                             |   |               |             |               |
| Balance at Beginning of Period  | \$  | 1,800         | \$          | 1,385         |
| Provision Charged to Operating Expenses                                   |   | 136           |             | 415           |
| <b>Balance at End of Period</b>   | <b>\$</b>   | <b>1,936</b>  | <b>\$</b>   | <b>1,800</b>  |
| <b>Ratios:</b>  |   |               |             |               |
| Net Loan Charge-Offs to Average Total Gross Loans <sup>(1)</sup>          |   | 0.10%         |             | 0.21%         |
| Net Loan Charge-Offs to Total Gross Loans at End of Period <sup>(1)</sup> |   | 0.10%         |             | 0.15%         |
| Allowance for Loan Losses to Average Total Gross Loans                    |   | 0.96%         |             | 1.48%         |
| Allowance for Loan Losses to Total Gross Loans at End of Period           |   | 0.91%         |             | 1.06%         |
| Net Loan Charge-Offs to Allowance for Loan Losses <sup>(1)</sup>          |   | 10.09%        |             | 13.99%        |
| Net Loan Charge-Offs to Provision Charged to Operating Expenses           |   | 245.11%       |             | 123.00%       |
| Allowance for Loan Losses to Non-Performing Loans                         |   | 361.64%       |             | 281.35%       |
| <b>Balances:</b>  |   |               |             |               |
| Average Total Gross Loans Outstanding During Period                       |   | \$2,287,253   |             | \$1,592,785   |
| Total Gross Loans Outstanding at End of Period                            |   | \$2,430,544   |             | \$2,228,257   |
| Non-Performing Loans at End of Period                                     | \$  | 6,097         | \$          | 8,391         |

<sup>(1)</sup> Net loan charge-offs annualized to calculate the ratios.

We concentrate the majority of our interest-earning assets in loans. In all forms of lending, there are inherent risks. We concentrate the preponderance of our loan portfolio in either commercial loans or real estate loans. A small part of the portfolio is represented by installment loans, primarily for the purchase of automobiles.

While we believe that our underwriting criteria are prudent, outside factors can adversely impact credit quality. A portion of the portfolio is represented by loans guaranteed by the SBA, which further reduces the potential for loss. We also utilize credit review in an effort to maintain loan quality. Loans are reviewed throughout the year with special attention given to new loans and those loans that are classified as special mention and worse. In addition to our internal grading system, loans criticized by this credit review are downgraded with appropriate allowances added if required.

Although management believes the allowance is adequate to absorb losses as they arise, no assurance can be given that we will not sustain losses in any given period, which could be substantial in relation to the size of the allowance.

### Deposits

The following table shows the composition of deposits by type as of the dates indicated.

|                                    | <b>June 30,<br/>2005</b>      | <b>December 31,<br/>2004</b> | <b>Increase (Decrease)</b> |                   |
|------------------------------------|-------------------------------|------------------------------|----------------------------|-------------------|
|                                    |                               |                              | <b>Amount</b>              | <b>Percentage</b> |
|                                    | <i>(Dollars in Thousands)</i> |                              |                            |                   |
| Deposits:                          |                               |                              |                            |                   |
| Non-Interest-Bearing               | \$ 757,482                    | \$ 729,583                   | \$ 27,899                  | 3.8%              |
| Interest-Bearing:                  |                               |                              |                            |                   |
| Money Market Checking              | 518,893                       | 613,662                      | (94,769)                   | (15.4%)           |
| Savings                            | 141,440                       | 153,862                      | (12,422)                   | (8.1%)            |
| Time Deposits of \$100,000 or More | 916,212                       | 756,580                      | 159,632                    | 21.1%             |
| Other Time Deposits                | 225,950                       | 275,120                      | (49,170)                   | (17.9%)           |
| <b>Total Deposits</b>              | <b>\$2,559,977</b>            | <b>\$2,528,807</b>           | <b>\$ 31,170</b>           | <b>1.2%</b>       |

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Core deposits (defined as demand, money market checking and savings deposits) decreased \$79.3 million, or 5.3 percent, to \$1.42 billion at June 30, 2005 from \$1.50 billion at December 31, 2004. The \$27.9 million increase in non-interest-bearing deposits was due to continued efforts to increase the net interest margin by changing the deposit composition mix between interest-bearing and non-interest-bearing accounts.

**Borrowings**

Borrowings consist of advances from the Federal Home Loan Bank of San Francisco ( FHLB ), overnight federal funds and junior subordinated debentures associated with trust preferred securities.

At June 30, 2005 and December 31, 2004, advances from the FHLB were \$100.7 million and \$66.4 million, respectively. Junior subordinated debentures totaled \$82.4 million at June 30, 2005 and December 31, 2004. Among the total borrowings, as of June 30, 2005, short-term borrowings with a remaining maturity of less than one year were \$98.9 million, and the weighted-average interest rate thereon was 3.40 percent.

**LIQUIDITY AND CAPITAL RESOURCES**

Liquidity of the Bank is defined as the ability to supply cash as quickly as needed without causing a severe deterioration in its profitability. The Bank's major liquidity on the asset side stems from available cash positions, Federal funds sold and short-term investments categorized as trading and/or available for sale securities, which can be disposed of without significant capital losses in the ordinary course of business. Liquidity sources on the liability side come from borrowing capacities, which include Federal funds lines, repurchase agreements and FHLB advances. Thus, maintenance of high quality loans and securities that can be used for collateral in repurchase agreements or other secured borrowings is another important feature of liquidity management.

Liquidity risk may occur when the Bank has few short-duration securities available for sale and/or is not capable of raising funds as quickly as necessary at acceptable rates in the capital or money markets. Also, a heavy and sudden increase in cash demands for loans and/or deposits can tighten the liquidity position. Several ratios are reviewed on a daily, monthly and quarterly basis to manage the liquidity position and to preempt any liquidity crisis. Six specific statistics, which include the loans-to-assets ratio, off-balance sheet items and dependence on non-core deposits, foreign deposits, lines of credit and liquid assets, are reviewed regularly for liquidity management purposes.

The maintenance of a proper level of liquid assets is critical for both the liquidity and the profitability of the Bank. Since the primary objective of the investment portfolio is to ensure proper liquidity of the Bank, management maintains appropriate levels of liquid assets to avoid exposure to higher than necessary liquidity risk.

At June 30, 2005, short-term investments totaled 3.7 percent of total assets, compared to 4.8 percent at December 31, 2004. Core deposits, expressed as a percentage of total assets, decreased slightly to 38.5 percent at June 30, 2005 from 41.1 percent at December 31, 2004, while short-term non-core funding as a percentage of total assets increased to 37.6 percent at June 30, 2005 from 33.2 percent at December 31, 2004. The ratio of short-term investments to short-term non-core funding decreased slightly to 21.5 percent at June 30, 2005 from 22.6 percent at December 31, 2004. Off-balance sheet items, primarily unused credit lines, as a percentage of total assets increased to 16.8 percent at June 30, 2005 from 15.0 percent at December 31, 2004.

The Bank saw a drop-off in the demand for loans at the beginning of the first quarter of 2005, but the demand for loans increased toward the end of the first quarter and continued through the second quarter of 2005. Net loans as a percentage of total assets increased to 74.1 percent at June 30, 2005 from 71.9 percent at December 31, 2004.

In order to ensure adequate levels of capital, we conduct an ongoing assessment of projected sources and uses of capital in conjunction with projected increases in assets and levels of risk. Management considers, among other things, cash generated from operations, and access to capital from financial markets or the issuance of additional securities, including common stock or notes, to meet our capital needs. Total shareholders' equity was \$424.8 million at June 30, 2005, which represented an increase of \$24.9 million, or 6.2 percent, over total shareholders' equity of \$399.9 million at December 31, 2004.

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The regulatory agencies require a minimum ratio of qualifying total capital to risk-adjusted assets of 8.0 percent and a minimum ratio of Tier 1 capital to risk-adjusted assets of 4.0 percent. In addition to the risk-based guidelines, regulators require banking organizations to maintain a minimum amount of Tier 1 capital to total assets, referred to as the leverage ratio, of 4.0 percent. For a bank rated in the highest of the five categories used by regulators to rate banks, the minimum leverage ratio is 3.0 percent. In addition to these uniform risk-based capital guidelines 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.

At June 30, 2005, Hanmi Financial's Tier 1 capital (shareholders' equity plus junior subordinated debentures less intangible assets) was \$285.1 million. This represented an increase of \$28.0 million, or 10.9 percent, over Tier 1 capital of \$257.1 million at December 31, 2004. The capital ratios of Hanmi Financial and Hanmi Bank were as follows as of June 30, 2005:

|   | Actual    |        | Minimum Regulatory Requirement |       | Minimum to Be Categorized as Well Capitalized |        |
|---|-----------|--------|--------------------------------|-------|---|--------|
|   | Amount    | Ratio  | Amount                         | Ratio | Amount  | Ratio  |
|   |           |        | <i>(Dollars in Thousands)</i>  |       |   |        |
| Total Capital (to Risk-Weighted Assets):  |           |        |                                |       |   |        |
| Hanmi Financial                           | \$309,133 | 12.17% | \$203,238                      | 8.00% | N/A   | N/A    |
| Hanmi Bank                                | \$307,517 | 12.13% | \$202,819                      | 8.00% | \$253,524                                     | 10.00% |
| Tier 1 Capital (to Risk-Weighted Assets): |           |        |                                |       |   |        |
| Hanmi Financial                           | \$285,146 | 11.22% | \$101,619                      | 4.00% | N/A   | N/A    |
| Hanmi Bank                                | \$283,530 | 11.18% | \$101,410                      | 4.00% | \$152,114                                     | 6.00%  |
| Tier 1 Capital (to Average Total Assets): |           |        |                                |       |   |        |
| Hanmi Financial                           | \$285,146 | 9.65%  | \$118,220                      | 4.00% | N/A   | N/A    |
| Hanmi Bank                                | \$283,530 | 9.61%  | \$117,991                      | 4.00% | \$147,488                                     | 5.00%  |

**Dividends**

On June 17, 2005, we declared a quarterly cash dividend of \$0.05 per common share for the second quarter of 2005. The dividend was paid on July 19, 2005. Future dividend payments are subject to the future earnings and legal requirements and the discretion of the Board of Directors.

**OFF-BALANCE SHEET ARRANGEMENTS**

For a discussion of off-balance sheet arrangements, see Note 5 Off-Balance Sheet Arrangements of Notes to Consolidated Financial Statements and Item 1. Business Small Business Administration Guaranteed Loans and Item 1. Business Off-Balance Sheet Commitments in our Annual Report on Form 10-K for the year ended December 31, 2004.

**CONTRACTUAL OBLIGATIONS**

There were no material changes to the contractual obligations described in our Annual Report on Form 10-K for the year ended December 31, 2004.

**Table of Contents****ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK  
GENERAL**

Interest rate risk indicates our exposure to market interest rate fluctuations. The movement of interest rates directly and inversely affects the economic value of fixed-income assets, which is the present value of future cash flow discounted by the current interest rate. Under the same conditions, the higher the current interest rate, the higher the denominator of discounting. Interest rate risk management is intended to decrease or increase the level of our exposure to fluctuations in market interest rate. The level of interest rate risk can be managed through the changing of gap positions and the volume of fixed-income assets and so forth. For successful management of interest rate risk, we use various methods to measure existing and future interest rate risk exposures. In addition to regular reports used in business operations, repricing gap analysis, stress testing and simulation modeling are the main measurement techniques used to quantify interest rate risk exposure.

The following table shows the status of the gap position as of June 30, 2005:

|  | <b>Within<br/>Three<br/>Months</b> | <b>After<br/>Three<br/>Months<br/>But Within<br/>One Year</b> | <b>After One<br/>Year But<br/>Within<br/>Five<br/>Years</b> | <b>After<br/>Five<br/>Years</b> | <b>Non-<br/>Interest-<br/>Sensitive</b> | <b>Total</b>       |
|--|------------------------------------|---|---|---------------------------------|---|--------------------|
| <i>(Dollars in Thousands)</i>                          |                                    |   |   |                                 |   |                    |
| <b>Assets:</b>   |                                    |   |   |                                 |   |                    |
| Cash   |                                    |   |   |                                 |   |                    |
| (Non-Interest-Earning)                                 | \$                                 | \$  | \$  | \$                              | \$ 96,850                               | \$ 96,850          |
| Federal Funds Sold                                     | 7,000                              |   |   |                                 |   | 7,000              |
| FRB and FHLB Stock                                     |                                    |   |   | 24,130                          |   | 24,130             |
| <b>Securities:</b>                                     |                                    |   |   |                                 |   |                    |
| Fixed Rate   | 34,185                             | 69,111  | 137,904   | 113,235                         |   | 354,435            |
| Floating Rate  | 8,423                              |   | 40,341  | 8,642                           |   | 57,406             |
| <b>Loans:</b>  |                                    |   |   |                                 |   |                    |
| Fixed Rate   | 36,718                             | 40,171  | 121,999   | 71,475                          |   | 270,363            |
| Floating Rate  | 2,126,880                          | 7,873   | 19,740  |                                 |   | 2,154,493          |
| Non-Accrual  |                                    |   |   |                                 | 5,688                                   | 5,688              |
| Deferred Loan Fees and<br>Allowance for Loan<br>Losses |                                    |   |   |                                 | (26,508)                                | (26,508)           |
| Derivatives  | (70,000)                           |   | 70,000  |                                 |   |                    |
| Other Assets   |                                    | 22,283  |   | 5,967                           | 279,685                                 | 307,935            |
| <b>Total Assets</b>                                    | <b>\$2,143,206</b>                 | <b>\$ 139,438</b>   | <b>\$ 389,984</b>   | <b>\$223,449</b>                | <b>\$ 355,715</b>                       | <b>\$3,251,792</b> |
| <b>Liabilities</b>                                     |                                    |   |   |                                 |   |                    |
| <b>Deposits:</b>                                       |                                    |   |   |                                 |   |                    |
| Demand Deposits  | \$ 75,220                          | \$ 197,098  | \$ 416,938  | \$ 68,226                       | \$                                      | \$ 757,482         |
| Money Market Checking                                  | 68,937                             | 171,233   | 220,160   | 58,563                          |   | 518,893            |
| Savings  | 16,669                             | 45,165  | 69,655  | 9,951                           |   | 141,440            |
| Time Deposits of<br>\$100,000 or More                  | 480,924                            | 427,019   | 8,169   | 100                             |   | 916,212            |
| Other Time Deposits                                    | 92,743                             | 116,016   | 8,713   | 8,478                           |   | 225,950            |
| Other Borrowed Funds                                   | 98,918                             |   | 43,487  | 5,242                           |   | 147,647            |



|   |                   |                   |                   |                   |                   |                     |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|---------------------|
| Junior Subordinated<br>Debentures   | 82,406            |                   |                   |                   |                   | 82,406              |
| Fair Value Swaps  | 24,462            | (24,462)          |                   |                   |                   |                     |
| Other Liabilities   |                   |                   |                   |                   | 36,932            | 36,932              |
| Shareholders' Equity  |                   |                   |                   |                   | 424,830           | 424,830             |
| <b>Total Liabilities and<br/>Shareholders' Equity</b>                     | <b>\$ 940,279</b> | <b>\$ 932,069</b> | <b>\$ 767,122</b> | <b>\$ 150,560</b> | <b>\$ 461,762</b> | <b>\$ 3,251,792</b> |
| Repricing Gap   | \$1,202,927       | \$(792,631)       | \$(377,138)       | \$ 72,889         | \$(106,047)       |                     |
| Cumulative Repricing<br>Gap   | \$1,202,927       | \$ 410,296        | \$ 33,158         | \$106,047         | \$                |                     |
| Cumulative Repricing<br>Gap as a Percentage of<br>Total Assets            | 36.99%            | 12.62%            | 1.02%             | 3.26%             |                   |                     |
| Cumulative Repricing<br>Gap as a Percentage of<br>Interest-Earning Assets | 41.95%            | 14.31%            | 1.16%             | 3.70%             |                   |                     |

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The repricing gap analysis measures the static timing of repricing risk of assets and liabilities, i.e., a point-in-time analysis measuring the difference between assets maturing or repricing in a period and liabilities maturing or repricing within the same time period. Assets are assigned to maturity and repricing categories based on their expected repayment or repricing dates, and liabilities are assigned based on their repricing or maturity dates. Core deposits that have no maturity dates (demand deposits, savings and money market checking) are assigned to categories based on expected decay rates.

On June 30, 2005, the cumulative repricing gap as a percentage of interest-earning assets in the less-than-three month period was 41.95 percent. This was a decrease from the previous quarter's figure of 47.50 percent. The decrease was primarily caused by increases in time deposits of \$100,000 or more and other borrowings, which were partially offset by an increase in floating rate loans. The cumulative repricing gap as a percentage of interest-earning assets in the three to twelve-month period moved slightly lower, reaching 14.31 percent as compared to 16.53 percent in the previous quarter. In terms of fixed and floating gap positions, which are used internally to control repricing risk, the accumulated fixed gap position between assets and liabilities as a percentage of interest-earning assets was (18.03) percent. The floating gap position in the less-than-one year period was 17.45 percent.

The following table summarizes the status of the gap position as of the dates indicated:

|                                       | <b>Less than Three Months</b> |                           | <b>Three to Twelve Months</b> |                           |
|---------------------------------------|-------------------------------|---------------------------|-------------------------------|---------------------------|
|                                       | <b>June 30,<br/>2005</b>      | <b>March 31,<br/>2005</b> | <b>June 30,<br/>2005</b>      | <b>March 31,<br/>2005</b> |
|                                       | <i>(Dollars in Thousands)</i> |                           |                               |                           |
| Cumulative Repricing Gap              | \$1,202,927                   | \$1,318,006               | \$410,296                     | \$458,599                 |
| Percentage of Total Assets            | 36.99%                        | 41.98%                    | 12.62%                        | 14.61%                    |
| Percentage of Interest-Earning Assets | 41.95%                        | 47.50%                    | 14.31%                        | 16.53%                    |

The spread between interest income on interest-earning assets and interest expense on interest-bearing liabilities is the principal component of net interest income, and interest rate changes substantially affect our financial performance. We emphasize capital protection through stable earnings rather than maximizing yield. In order to achieve stable earnings, we prudently manage our assets and liabilities and closely monitor the percentage changes in net interest income and equity value in relation to limits established within our guidelines.

**ITEM 4. CONTROLS AND PROCEDURES****Disclosure Controls and Procedures**

The Chief Executive Officer and Principal Financial Officer directly supervised and participated in evaluating the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2005 and concluded that these controls and procedures were effective. There were no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 (the Exchange Act) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Principal Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

**Table of Contents****PART II OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

From time to time, Hanmi Financial or Hanmi Bank is a party to claims and legal proceedings arising in the ordinary course of business. After taking into consideration information furnished by counsel as to the current status of these claims or proceedings to which Hanmi Financial or Hanmi Bank is a party, management is of the opinion that the ultimate aggregate liability represented thereby, if any, will not have a material adverse effect on the financial condition or results of operations of Hanmi Financial or Hanmi Bank.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

On May 18, 2005, the Annual Meeting of Stockholders was called to vote on election of four nominees to serve as Class III Directors of Hanmi Financial for terms of three years each. The number of votes cast at the meeting as to each Director was as follows:

| <b>Class III Director Nominees</b> | <b>Votes<br/>For</b> | <b>Votes<br/>Withheld</b> | <b>Unvoted</b> |
|------------------------------------|----------------------|---------------------------|----------------|
| Ung Kyun Ahn                       | 40,410,186           | 1,164,722                 | 8,046,769      |
| Richard B. C. Lee                  | 40,389,884           | 1,185,024                 | 8,046,769      |
| Chang Kyu Park                     | 40,365,008           | 1,209,900                 | 8,046,769      |
| William J. Ruh                     | 41,270,327           | 304,581                   | 8,046,769      |

The other directors, whose term of office as a director continued after the meeting, were:

**Class I Directors Terms Expire in 2006**

I Joon Ahn

Joon Hyung Lee

Joseph K. Rho

Kraig A. Kupiec

**Class II Directors Terms Expire in 2007**

M. Christian Mitchell

Sung Won Sohn, Ph.D.

Won R. Yoon

**ITEM 5. OTHER INFORMATION**

None.

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**ITEM 6. EXHIBITS**

**Exhibit**

**Number**

**Document**

|      |   |
|------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended         |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended         |
| 32.1 | Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

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**SIGNATURES**

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

**HANMI FINANCIAL CORPORATION**

Date: August 9,  
2005

By: /s/ Sung Won Sohn, Ph.D.

Sung Won Sohn, Ph.D.  
President and Chief Executive Officer

Date: August 9,  
2005

By: /s/ Michael J. Winiarski

Michael J. Winiarski  
Senior Vice President and Chief Financial Officer

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