2008

ANNUAL

FARMERS & MERCHANTS BANK OF LONG BEACH

REPORT

Cover Artwork Features: The decorative window eve on the Main Office building, 302 Pine Ave, Long Beach, CA; and the new Customer Care Center, fondly noted as C3 or the Cube, located at 1695 Adolfo Lopez Drive, Seal Beach, CA.   The Customer Care Center is the site of our 2009 Annual Shareholder Meeting.

Dear Fellow Shareholders:

At a time when the performance of banks was duly tested by an extraordinary series of events in the credit and financial markets, Farmers & Merchants Bank of Long Beach achieved solid loan and deposit growth in 2008.

Net loans increased 27% and deposits grew 33% in 2008, reaffirming Farmers & Merchants Bank's position as one of the safest and soundest institutions in California and underscoring the value that we provide to our customers and communities. The year also demonstrated our adherence to conservative banking disciplines that helped us avert the subprime mortgage debacle.

At the same time, the overriding macroeconomic factors had an impact on our financial results. Interest income for the year ended December 31, 2008 was down slightly to $182.3 million from $183.3 million for the year ended December 31, 2007, mainly due to a significantly lower interest rate environment. Interest expense, on the other hand, declined to $35.5 million in 2008 from $47.8 million in 2007.

Reflecting a deteriorating economic environment, our provision for loan losses totaled $53.0 million in 2008, versus $6.4 million for 2007. The Bank's allowance for loan losses as a percentage of loans outstanding was 2.69% at December 31, 2008, compared with 1.75% at December 31, 2007.

These are unprecedented times, and we continue to monitor our non-performing loans closely and work proactively with our clients to address potential issues before they become problems. Additionally, the investments in our securities portfolio remain conservative and strong.

Net income for 2008 was $29.7 million, or $218.97 per diluted share, compared with $51.2 million, or $337.97 per diluted share, for 2007. The decrease in net income primarily reflected the increased levels of provision for loan losses.

Despite the economy's effect on our performance, we are confident in our ability to successfully navigate through this recessionary period with more than a century of experience and a strong and dedicated management team.

Among the most noteworthy accomplishments in 2008 was the strength of our balance sheet.

Strong Balance Sheet

Net loans increased to $1.95 billion as of December 31, 2008 from $1.53 billion at December 31, 2007. The Bank's deposits grew to $2.68 billion at the end of 2008, versus $2.01 billion at December 31, 2007. Total assets increased to $3.64 billion at the close of 2008 from $3.20 billion at December 31, 2007.

At year end, our capital ratios stood well above the industry average. We remained "well-capitalized" under all regulatory standards at December 31, 2008, with a total risk-based capital ratio of 26.04%, a Tier 1 risk-based capital ratio of 24.78%, and a Tier 1 leverage ratio of 16.18%. The minimum ratios for capital adequacy for a well-capitalized bank are 10.00%, 6.00% and 5.00%, respectively.

We understand that our depositors, borrowers and shareholders look to the strength of our balance sheet, especially in this challenging economy, and we are focused on maintaining its vigor.

Staying the Course

In November 2008, we opened the doors to our new customer care center in Seal Beach, Calif., a 60,000 square-foot complex that combined 150 employees in previously separate facilities. This new centralized location allows our Bank to streamline procedures and communications while instituting advanced and environmentally-conscious technology.

Meanwhile, after a careful review of the U.S. Treasury Department's Capital Purchase Program's terms, our board and management team determined that participation in the program would not enhance the interests of the Bank, our customers, or our shareholders.

Farmers & Merchants Bank is strongly capitalized, and we believe that employing our own time-tested strategies will further enhance our organization.

Moving Forward

We will continue our efforts to maximize the breadth of Farmers & Merchants' brand and encourage customers to bank with us at a time when strength, soundness and stability are well defined by our 102-year-old heritage. We believe the growth prospects for our Bank in Southern California remain robust, and we will continue to explore opportunities as they become available.

The strength and experience of our management team is receiving recognition throughout the region. We applaud John Hinrichs, our executive vice president and chief financial officer, who was presented with a lifetime achievement award in January at the CFO of the Year Awards hosted by the Orange County Business Journal and the California Society of Certified Public Accountants.

As we move forward, the economic challenges our country faces will not be easy. However, the discipline, commitment and integrity that have propelled our Bank for more than a century are steadfast, and we are prepared for the road ahead.

On behalf of our board of directors and management team, we would like to thank you for your continued dedication to Farmers & Merchants Bank of Long Beach.

Daniel K. Walker

Daniel Walker
Chairman of the Board and President

W. Henry Walker

W. Henry Walker
Chief Executive Officer

FARMERS & MERCHANTS BANK OF LONG BEACH
2008 ANNUAL REPORT

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KPMG LLP
Suite 2000
355 South Grand Avenue
Los Angeles, CA 90071-1568

Independent Auditors' Report

The Board of Directors
Farmers & Merchants Bank of Long Beach:

We have audited the accompanying balance sheets of Farmers & Merchants Bank of Long Beach (the Bank) as of December 31, 2008 and 2007, and the related statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Farmers & Merchants Bank of Long Beach as of December 31, 2008 and 2007, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

Los Angeles, California
March 31, 2009

FARMERS & MERCHANTS BANK OF LONG BEACH
BALANCE SHEETS

	December 31, 2008	December 31, 2007
Assets		
Cash and due from banks	$ 209,696,893	$ 112,983,325
Federal funds sold	-	18,000,000
Total cash and cash equivalents	209,696,893	130,983,325
Securities held-to-maturity (fair value of $991,583,907 and $1,024,055,217)	965,166,197	1,018,982,056
Securities available-for-sale (amortized cost of $404,653,584 and $446,238,896)	421,192,391	453,899,382
Loans, net	1,947,156,909	1,529,898,523
Bank premises and equipment, net	55,531,620	34,945,602
Accrued interest receivable	14,853,715	16,994,591
Other assets	23,674,204	19,262,817
Total assets	**$ 3,637,271,929**	**$ 3,204,966,296**
Liabilities & Stockholders' Equity		
Liabilities:		
Deposits:		
Demand, non-interest bearing	$ 809,671,161	$ 705,005,305
Demand, interest bearing	225,485,095	211,061,618
Savings and money market savings	507,521,371	423,259,630
Time deposits	1,133,141,414	672,674,495
Total deposits	2,675,819,041	2,012,001,048
Securities sold under agreements to repurchase	393,201,735	495,545,303
Accrued interest payable and other liabilities	7,329,241	6,792,260
Total liabilities	3,076,350,017	2,514,338,611
Commitments and Contingencies		
Stockholders' equity:		
Common stock, par value $20; authorized 250,000 shares; issued and outstanding 130,928 and 151,475 shares	2,618,560	3,029,500
Surplus	12,043,783	12,043,783
Retained earnings	536,674,669	671,114,844
Accumulated other comprehensive income	9,584,900	4,439,558
Total stockholders' equity	560,921,912	690,627,685
Total liabilities and stockholders' equity	**$ 3,637,271,929**	**$ 3,204,966,296**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF INCOME

	Years Ended December 31, 2008	Years Ended December 31, 2007
Interest income:		
Loans	$ 115,050,129	$ 108,938,112
Securities held-to-maturity	44,439,550	45,507,671
Securities available-for-sale	20,722,296	24,500,454
Federal funds sold	1,848,476	4,366,744
Deposits with banks	205,923	-
Total interest income	182,266,374	183,312,981
Interest expense:		
Deposits	27,605,714	29,317,673
Securities sold under agreements to repurchase	7,849,337	18,471,470
Total interest expense	35,455,051	47,789,143
Net interest income	146,811,323	135,523,838
Provision for loan losses	52,989,722	6,364,997
Net interest income after provision for loan losses	93,821,601	129,158,841
Non-interest income:		
Service charges on deposit accounts	6,031,132	4,738,864
Merchant bankcard fees	1,368,093	1,790,768
Escrow fees	1,183,167	952,832
Other	5,699,319	4,820,702
Total non-interest income	14,281,711	12,303,166
Non-interest expense:		
Salaries and employee benefits	38,590,068	36,861,304
FDIC and other insurance expense	1,612,793	551,189
Occupancy expense	5,747,933	5,187,343
Equipment expense	4,351,144	3,776,278
Legal and professional fees	2,409,215	3,763,161
Marketing and promotional expense	2,475,774	2,395,599
Printing and supplies	1,052,658	1,244,949
Postage and delivery	1,356,813	1,224,690
Other	3,950,746	3,051,527
Total non-interest expense	61,547,144	58,056,040
Income before income tax expense	46,556,168	83,405,967
Income tax expense	16,833,911	32,223,816
Net income	**$ 29,722,257**	**$ 51,182,151**
Basic earnings per common share	$ 218.97	$ 338.03
Diluted earnings per common share	$ 218.97	$ 337.97

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31, 2008	2007
Net income	$ 29,722,257	$ 51,182,151
Other comprehensive income, net of tax:		
Unrealized gains on securities:		
Unrealized holding gains arising during period	5,145,342	4,910,898
Other comprehensive income	5,145,342	4,910,898
Comprehensive income	**$ 34,867,599**	**$ 56,093,049**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

		Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)		Total Stock-holders' Equity
Balance, December 31, 2006	**$**	**3,021,800**	**11,269,983**	**635,837,568**	**(471,340)**	**$**	**649,658,011**
Issuance of common stock upon exercise of employee stock options		7,700	723,800	-	-		731,500
Stock option compensation expense		-	50,000	-	-		50,000
Net income		-	-	51,182,151	-		51,182,151
Cash dividends		-	-	(15,904,875)	-		(15,904,875)
Other comprehensive income, net of tax expense		-	-	-	4,910,898		4,910,898
Balance, December 31, 2007	**$**	**3,029,500**	**12,043,783**	**671,114,844**	**4,439,558**	**$**	**690,627,685**
Repurchase and retirement of common stock		(410,940)	-	(149,582,160)	-		(149,993,100)
Net income		-	-	29,722,257	-		29,722,257
Cash dividends		-	-	(14,580,272)	-		(14,580,272)
Other comprehensive income, net of tax expense		-	-	-	5,145,342		5,145,342
Balance, December 31, 2008	**$**	**2,618,560**	**12,043,783**	**536,674,669**	**9,584,900**	**$**	**560,921,912**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CASH FLOWS

	Years Ended December 31, 2008	Years Ended December 31, 2007
Cash flows from operating activities:		
Net income	$ 29,722,257	$ 51,182,151
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,919,893	2,420,601
Net amortization on securities	2,778,086	3,731,672
Provision for loan losses	52,989,722	6,364,997
(Reduction of) provision for losses on unfunded commitments	(549,356)	124,559
Deferred income tax benefit	(7,170,597)	(1,497,758)
Stock compensation expense	-	50,000
Decrease in accrued interest receivable	2,140,876	27,741
Increase in other assets	(973,769)	(2,167,947)
Increase (decrease) in accrued interest payable and other liabilities	1,086,337	(902,254)
Total adjustments	53,221,192	8,151,611
Net cash provided by operating activities	82,943,449	59,333,762
Cash flows from investing activities:		
Proceeds from maturities of securities held-to-maturity	275,957,127	245,859,597
Purchases of securities held-to-maturity	(203,576,533)	(254,467,562)
Proceeds from maturities of securities available-for-sale	212,688,777	326,384,892
Purchases of securities available-for-sale	(192,446,286)	(315,734,479)
Net increase in loans	(470,248,108)	(183,958,860)
Purchases of bank premises and equipment	(23,505,911)	(13,224,139)
Net cash used in investing activities	(401,130,935)	(195,140,551)

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CASH FLOWS

	Years Ended December 31,	
	2008	2007
Cash flows from financing activities:		
Net increase (decrease) in deposits	$ 663,817,993	$ (53,586,973)
Net (decrease) increase in securities sold under agreements to repurchase	(102,343,568)	144,739,263
Issuance of common stock	-	731,500
Repurchase and retirement of common stock	(149,993,100)	-
Dividends paid	(14,580,272)	(15,904,875)
Net cash provided by financing activities	396,901,053	75,978,915
Net increase (decrease) in cash and cash equivalents	78,713,568	(59,827,874)
Cash and cash equivalents at beginning of year	130,983,325	190,811,199
Cash and cash equivalents at end of year	**$ 209,696,893**	**$ 130,983,325**
Supplemental disclosures of cash flow information:		
Interest paid (including interest credited during the year)	$ 35,613,129	$ 47,721,104
Cash paid during the year for income taxes	25,030,000	36,380,351

See accompanying notes to financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Farmers & Merchants Bank of Long Beach (the “Bank”) is an FDIC-insured community bank engaged primarily in commercial lending with a loan portfolio comprised primarily of commercial, real estate and construction loans, most of which are secured. The Bank operates primarily in California’s South Los Angeles County and Orange County.

The Bank’s operations, like those of other financial institutions operating in Southern California, are significantly influenced by economic conditions in Southern California, including local economies, the strength of the real estate market, and the fiscal and regulatory policies of the federal and state government and the regulatory authorities that govern financial institutions. No individual or single group of related accounts is considered material in relation to the total assets or deposits of the Bank. However, approximately 91% of the loan portfolio at December 31, 2008 consisted of real estate related loans, including commercial loans and construction loans secured by real estate. There has been a slow-down in the real estate market due to negative economic trends and credit market disruptions, the impact of which are not yet completely known or quantified. The Bank has observed tighter credit underwriting and higher premiums on liquidity, both of which may continue to place downward pressure on real estate values. Any further downturn in the real estate market could materially and adversely affect the business because a significant portion of the loan portfolio is secured by real estate. The ability to recover on defaulted loans by selling the real estate collateral would then be diminished and the Bank would be more likely to suffer losses on defaulted loans. Substantially all of the Bank’s real property collateral is located in Southern California. Consequently, the results of operations and financial condition are dependent upon the general trends in the Southern California economies and, in particular, the commercial and residential real estate markets. If there is a further decline in real estate values, especially in Southern California, the collateral of the loans would provide less security. Real estate values could be affected by, among other things, a worsening of the economic conditions, an increase in foreclosures, a decline in home sale volumes, an increase in interest rates, earthquakes and other natural disasters particular to California. Further, the Bank may experience an increase in the number of borrowers who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to the Bank given a sustained weakness or weakening in business and economic conditions generally in the principal markets in which the Bank does business. An increase in number of delinquencies, bankruptcies or defaults could result in higher level of nonperforming assets, net charge-offs and provision for loan losses.

The accounting and reporting policies of Farmers & Merchants Bank of Long Beach are in accordance with accounting principles generally accepted in the United States of America and conform to general practice within the banking industry.

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and income statement for the year. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses and the valuation of real estate owned. Management believes that the allowances established on loans and real estate owned are adequate. While management uses available information to recognize losses on loans and real estate owned, future additions to the allowances may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank’s allowance for losses on loans and real estate owned. Such agencies may require the Bank to recognize changes to the allowances based on their judgments about information available to them at the time of their examination.

NOTE 1 - Summary of Significant Accounting Policies, continued

The Bank is required to carry its available-for-sale securities at fair value and real estate acquired in settlement of loans at the lower of cost or fair value, less estimated selling costs. Fair value estimates are made at a specific point in time based upon relevant market information and other information about the asset. Such estimates related to the investment securities portfolios include published bid prices or bid quotations received from securities dealers. Fair value estimates for real estate acquired in settlement of loans is determined by current appraisals and, where no active market exists for a particular property, discounting a forecast of expected cash flows at the rate commensurate with the risk involved.

Securities Held-to-maturity and Securities Available-for-sale

Securities at December 31, 2008 consist of U.S. Government agency obligations, State and Municipal bonds and mortgage-backed securities. In accordance with Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debts and Equity Securities* (SFAS No. 115), the Bank classifies its securities into one of two categories: held-to-maturity and available-for-sale. Securities held-to-maturity are those for which the Bank has the ability and positive intent to hold until maturity. All other securities are classified as available-for-sale.

Securities held-to-maturity are recorded at cost, adjusted for the amortization of premiums and accretion of discounts on a level-yield basis. Securities available-for-sale are carried at fair value. Unrealized holding gains and losses, net of the related tax effect, on securities available-for-sale are excluded from income and reported as a separate component of stockholders' equity, identified as accumulated other comprehensive income, until realized. Transfers of securities between categories, if any, are recorded at fair value at the date of the transfer. Unrealized holding gains or losses included in the separate component of equity for securities transferred from available-for-sale to held-to-maturity would be maintained and amortized into income over the remaining life of the security as an adjustment to the yield in a manner consistent with the amortization of premium or accretion of discount on the associated security.

A decline in market value of any held-to-maturity or available-for-sale security below cost that is deemed other than temporary is charged to income as realized loss, resulting in the establishment of a new cost basis for the security. In estimating other-than-temporary impairment losses, management considers, among other things, (i) the length of time and the extent of which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer and (iii) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The new cost basis is not changed for subsequent recoveries in fair value.

Premiums and discounts are amortized and accreted over the life of the related securities available-for-sale and securities held-to-maturity as an adjustment to yield using the interest method. Realized gains and losses on securities available-for-sale and securities held-to-maturity are included in income and are derived using the specific-identification method for determining the cost of securities sold.

Loans and Allowance for Loan Losses

Loans are reported at amounts advanced, net of unearned discounts and undisbursed loan funds, less principal payments collected. Unearned interest on discounted loans is accreted into interest income over the lives of the related loans in a manner approximating the interest method.

NOTE 1 – Summary of Significant Accounting Policies, continued

Loans and Allowance for Loan Losses, continued

Interest on loans is accrued as earned. It is the Bank's general practice for interest accruals on loans to be discontinued whenever the payment of interest or principal is 90 days past due. Whenever the accrual of interest is discontinued, previously accrued but uncollected interest income is reversed. Accrual of interest is resumed only when principal and interest are brought fully current and when in management's judgment such loans are deemed fully collectible as to both principal and interest. The accrual of interest on loans that are more than 90 days past due may continue if the loans are well secured, in the process of collection, and management deems it appropriate.

The Bank considers a loan impaired when it is probable that the Bank will be unable to collect all amounts due according to its contractual terms. The amount of an impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or measured against the value of the loan's underlying collateral, if the loan is collateral dependent. Impairment losses are included in the allowance for loan losses through the provision for loan losses. In determining impairment for a specific loan, management evaluates the impairment on an individual loan basis, including an analysis of the credit worthiness, cash flows and financial status of the borrower and the condition and the estimated value of the collateral. The Bank reviews consumer loans by analyzing their performance as a whole because of the relatively homogenous nature of the portfolio. The Bank also includes as impaired loans, all loans on which the accrual of interest has been discontinued and loans which have been restructured. Cash receipts on impaired loans receivable are applied to reduce the principal amount of such loans until the principal has been recovered and are recognized as income thereafter.

Loans are charged against the allowance for loan losses when management believes that the collectibility of the principal is unlikely, and recoveries are credited to the allowance. The provision for loan losses is established by a charge to expense and added to the allowance to maintain it at a level that management believes, based upon its evaluation of the collectibility and prior loss experience of the portfolio, is adequate to absorb losses inherent in existing loans and commitments to extend credit. That evaluation takes into consideration such factors as changes in the nature and volume of the portfolio, overall problem loans, commitments, and economic conditions that may affect the borrower's ability to pay. Subsequent changes in these factors and related assumptions may warrant adjustments in the level of the allowance for loan losses, based on conditions prevailing at the time.

Other Real Estate Owned

Real estate and other assets acquired in satisfaction of indebtedness are carried at fair value less estimated selling costs. Prior to foreclosure, related loan amounts are written down to the fair value of the assets to be acquired by a charge to the allowance for loan losses. Declines in value from the periodic valuation of foreclosed properties are charged against operating expenses and included in the allowance for other real estate owned in the period in which they are identified. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other income or expense as appropriate.

NOTE 1 – Summary of Significant Accounting Policies, continued

Bank Premises and Equipment

Bank premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed on straight-line method based on the estimated useful lives of the assets:

Type	Estimated Useful Life
Buildings	20 to 30 years
Building improvements	20 to 30 years
Furniture, fixtures and equipment	3 to 7 years

Leasehold improvements are capitalized and amortized on a straight-line basis over the term of the lease or the estimated useful lives of the improvements, whichever is shorter. Construction in process is carried at cost and includes land acquisition, architectural fees, general contractor fees, capitalized interest and other costs related directly to the construction of a property. Maintenance and repairs are charged to expense. Gains or losses on sale or retirement of assets are reported in other income or expense.

Income Taxes

The Bank is subject to Federal and California State income taxes. Income taxes are recorded using the asset and liability method. Under this method, the deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents consist of cash and due from banks and federal funds sold.

Stock Option Plan

In December 2004, the FASB issued SFAS No. 123R (Revised 2004), Share-Based Payment: an amendment of FASB Statements No. 123 and 95 (SFAS 123R). SFAS 123R requires companies to recognize in the income statement the grant-date fair value of stock options and other equity-based compensation issued to employees. Compensation costs should be recognized over the requisite service period. The amount accrued each period until the vesting date is based on the estimated number of awards that are expected to vest, adjusted periodically to reflect the current estimate of forfeitures. SFAS 123R does not express a preference for a type of valuation model to be used in measuring the grant-date fair value that is accrued over the service period. The Bank adopted SFAS 123R on January 1, 2006 and employed the modified prospective method of transition upon implementation.

NOTE 1 – Summary of Significant Accounting Policies, continued

Comprehensive Income

SFAS No. 130, *Reporting Comprehensive Income* (SFAS No. 130), established standards for reporting and presentation of comprehensive income and its components in a full set of financial statements. Comprehensive income consists of net income and net unrealized gains (losses) on securities available-for-sale arising or reclassified during the period, and is presented in the statements of comprehensive income. SFAS No. 130 only requires additional disclosures in the financial statements; it does not affect the Bank's financial position or results of operations.

Earning Per Share (EPS) Data

The table below is a reconciliation of the numerators and denominators used in the calculation of basic and diluted EPS for the years ended December 31, 2008 and 2007. Basic EPS 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 that then would share the earnings of the Bank.

	2008	2007
Basic earnings per share:		
Net income available to common stockholders	$ 29,722,257	$ 51,182,151
Weighted average number of common shares outstanding	135,737	151,413
Weighted basic earnings per common share	$ 218.97	$ 338.03
Diluted earnings per share:		
Net income available to common stockholders	$ 29,722,257	$ 51,182,151
Weighted average number of common shares outstanding	135,737	151,413
Impact of stock options	-	27
Average diluted number of common shares outstanding	135,737	151,440
Diluted earnings per common share	$ 218.97	$ 337.97

Recent Accounting Pronouncements

Business Combinations

FASB Statement No. 141R, which is a revision to SFAS No. 141, *Business Combinations* (SFAS No. 141), was issued in December 2007. This Statement established principles in which the acquirer in a business combination is required to recognize and measure in its financial statements all identifiable assets acquired, liabilities assumed and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date. As such, contingent consideration will need to be recognized based on estimated fair value at the date of acquisition. In addition, the costs related to the acquisition are to be recognized as incurred rather than allocated to the individual assets and liabilities. Also, if applicable, where the fair value of the assets acquired exceeded the acquisition cost, the excess asset value will be recognized as income. This statement makes significant amendments to other statements and other authoritative guidance. The provisions of this statement apply prospectively to business combinations with acquisition dates on or after January 1, 2009. We are currently evaluating the potential impact this statement will have on the Bank's financial results.

NOTE 1 – Summary of Significant Accounting Policies, continued

Recent Accounting Pronouncements, continued

Fair Value Measurements

FASB Statement No. 157, *Fair Value Measurements* (SFAS No. 157), defines fair value, establishes a framework for measuring fair value in GAAP, and requires enhanced disclosures about fair value measurements. This Statement applies when other accounting pronouncements require or permit fair value measurements; it does not require new fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those years. In February 2008, the FASB issued Staff Position (FSP) 157-2, *Effective Date of FASB Statement No. 157.* This FSP delays the effective date of SFAS No. 157 for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. In October 2008, the FASB issued Staff Position (FSP) 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active.* This FSP clarifies the application of SFAS No. 157 in a market that is not active. FSP 157-3 was effective upon issuance. The adoption of SFAS No. 157 did not have a material impact on the Bank's consolidated financial statements.

Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans

FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (SFAS No. 158), requires an employer to recognize in its statement of financial position the overfunded or underfunded status of a defined benefit postretirement plan measured as the difference between the fair value of plan assets and the benefit obligation. This Statement is effective for nonpublic entities for fiscal years ending after June 15, 2007. Implementation of this Statement did not have an impact on the Bank's financial results.

The Fair Value Option for Financial Assets and Financial Liabilities

FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment to FASB Statement No. 115* (SFAS No. 159), was issued in February 2007. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value to mitigate volatility in reported earnings caused by measuring financial instruments differently without having to apply complex hedge accounting provisions. The fair value option may be applied instrument by instrument, is irrevocable and is applied only to the entire instrument. Following the initial fair value measurement date, a business entity shall report unrealized gains and losses on financial instruments for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption of this Statement is required for the fiscal year that begins after November 15, 2007. The Bank did not elect the fair value option on any financial assets or liabilities on the Bank's financial statements at the date of the adoption of SFAS No. 159.

Noncontrolling Interests in Consolidated Financial Statements

FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements* (SFAS No. 160), was issued in December 2007. This Statement amends Accounting Research Bulletin No. 51, *Consolidated Financial Statements* (ARB No. 51). This statement clarifies that a noncontrolling interest (minority interest) in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. Sufficient disclosure should be provided to identify and distinguish between the interests of the parents and the interest of the noncontrolling owners. This statement also establishes that purchases or sales of equity securities that do not result in a change in control will be accounted for as equity transactions. Upon loss of control, the interest sold, as well as any interest retained, will be measured at fair value with any gain or loss recognized in earnings. This statement is effective for the Bank on January 1, 2009, and is not expected to have a significant impact on the Bank's financial statements.

NOTE 2 - FAIR VALUE MEASUREMENTS

SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. The Bank adopted SFAS No. 157 on January 1, 2008, and determined the fair values of our financial instruments based on the three-level fair value hierarchy established in SFAS No. 157. The three-level inputs to measure the fair value of assets and liabilities are as follows:

Level 1 - Quoted prices in active markets for identical assets or liabilities.
Level 2 - Observable prices in active markets for similar assets or liabilities; prices for identical or similar assets or liabilities in markets that are not active; directly observable market inputs for substantially the full term of the asset and liability; market inputs that are not directly observable but are derived from or corroborated by observable market data.
Level 3 - Unobservable inputs based on the Bank's own judgments about the assumptions that a market participant would use.

The Bank uses the following methodologies to measure the fair value of its financial assets on a recurring basis:

Securities available-for-sale - The Bank measures all securities by using quoted market prices for similar securities or dealer quotes, a Level 2 measurement. This category generally includes U.S. Government agency securities, state and municipal securities, mortgage-backed securities, asset-backed securities and corporate bonds.

Impaired loans - The Bank does not record loans at fair value on a recurring basis. However, from time to time, nonrecurring fair value adjustments to collateral dependent impaired loans are recorded based on either current appraised value of the collateral, a Level 2 measurement, or management's judgment and estimation of value reported on old appraisals which are then adjusted based on recent market trends, a Level 3 measurement.

The following table presents the Bank's hierarchy for its assets and liabilities measured at fair value on a recurring and non-recurring basis at December 31, 2008:

	Fair Value Measurements Using			Table at
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Assets				
On a recurring basis:				
Securities available-for-sale	$ -	$ 421,192,391	$ -	$ 421,192,391
On a non-recurring basis:				
Impaired loans	-	18,597,888	42,994,343	61,592,231
Total assets	$ -	$ 439,790,279	$ 42,994,343	$ 482,784,622

NOTE 3 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial instruments are defined under SFAS No. 107, *Disclosures About Fair Value of Financial Instruments* (SFAS No. 107), as cash, evidence of an ownership in an entity or a contract that conveys or imposes on an entity the contractual right or obligation to either receive or deliver cash or another financial instrument. A significant portion of the Bank's assets and liabilities are financial instruments as defined under SFAS No. 107.

The following presents a description of the Bank's financial instruments and the methodologies and assumptions used to estimate their fair value. Much of the information used to determine fair value is highly subjective. When applicable, readily available market information has been utilized. However, for a significant portion of the Bank's financial instruments, active markets do not exist. Therefore, considerable judgments were required in estimating fair value of certain items. The subjective factors include, among other things, the estimated timing and amount of cash flows, risk characteristics, credit quality and interest rates, all of which are subject to change. Since the fair value is estimated as of December 31, 2008 and 2007, the amounts that will actually be realized could be significantly different.

Cash and Cash Equivalents

The carrying value of cash and cash equivalents approximates the fair value because of the short maturity of such assets.

Securities Held-to-maturity and Securities Available-for-sale

The Bank used market quotes for similar or identical securities in an actively traded market to determine the fair values of securities held-to-maturity and securities available-for-sale as disclosed in Notes 4 and 5, respectively.

Loans

Fair values were estimated for portfolios of loans with similar financial characteristics. Each loan category was further segmented into fixed and adjustable rate interest terms and by performing and non-performing categories. The fair value of performing loans was calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. The entire allowance for loan losses was applied to classified loans, including non-accruals. Accordingly, they are considered to be carried at fair value as the allowance for loan losses represents the estimated discount for credit risk for the applicable loans.

Deposits

The fair value of demand deposits, savings and money market saving accounts was determined to approximate the carrying value as they are immediately withdrawable. For fixed maturity time deposits, the fair value was estimated by discounting expected cash flows by the current offering rates of term deposits with similar maturities. In accordance with SFAS No. 107, no value has been assigned to the Bank's long-term relationship with its deposit customers (core deposit intangibles) since it is not a financial instrument as defined under SFAS No. 107.

NOTE 3 – Fair Value Of Financial Instruments, continued

Securities Sold Under Agreements to Repurchase

The fair value of securities sold under agreements to repurchase approximates their carrying value due to the terms and nature of the obligations.

Off-Balance Sheet Financial Instruments

As the standby letters of credit and commitments to lend have terms that are consistent with current market terms, the Bank estimates the fair value of the fees charged to enter into such agreements to be nominal.

The following table presents estimated fair value information for the Bank's loans and deposits at December 31:

	2008	
	Carrying Value	**Estimated Fair Value**
Loans, net of allowance for loan losses	$ 1,947,156,909	$ 2,401,288,156
Deposits:		
Demand, non-interest bearing	$ 809,671,161	$ 809,671,161
Demand, interest bearing	225,485,095	225,485,095
Savings and money market savings	507,521,371	507,521,371
Time deposits	1,133,141,414	1,134,931,438
	$ 2,675,819,041	$ 2,677,609,065

	2007	
	Carrying Value	**Estimated Fair Value**
Loans, net of allowance for loan losses	$ 1,529,898,523	$ 1,323,026,087
Deposits:		
Demand, non-interest bearing	$ 705,005,305	$ 705,005,305
Demand, interest bearing	211,061,618	211,061,618
Savings and money market savings	423,259,630	423,259,630
Time deposits	672,674,495	672,004,129
	$ 2,012,001,048	$ 2,011,330,682

NOTE 4 – SECURITIES HELD-TO-MATURITY

The following is a summary of securities held-to-maturity:

	December 31, 2008	December 31, 2007
Carrying Value:		
U.S. Treasury securities	$ -	$ 9,976,201
U.S. Government agency obligations	24,342,791	54,154,386
State and Municipal securities	139,089,960	140,104,931
Mortgage-backed securities	801,733,446	814,746,538
	$ 965,166,197	$ 1,018,982,056
Approximate Fair Value:		
U.S. Treasury securities	$ -	$ 9,973,400
U.S. Government agency obligations	25,368,216	54,787,540
State and Municipal securities	140,479,984	141,412,979
Mortgage-backed securities	825,735,707	817,881,298
	$ 991,583,907	$ 1,024,055,217

	December 31, 2008	December 31, 2007
Gross Unrealized Gains:		
U.S. Government agency obligations	$ 1,025,425	$ 667,738
State and Municipal securities	1,774,353	1,406,870
Mortgage-backed securities	24,006,521	4,814,993
	26,806,299	6,889,601
Gross Unrealized Losses:		
U.S. Treasury securities	-	2,801
U.S. Government agency obligations	-	34,584
State and Municipal securities	384,329	98,822
Mortgage-backed securities	4,260	1,680,233
	388,589	1,816,440
Net Unrealized Gains	$ 26,417,710	$ 5,073,161

Maturities at December 31, 2008:	**Carrying Value**	**Estimated Fair Value**
Due in 1 year or less	$ 12,494,067	$ 12,586,173
Due after 1 year through 5 years	80,317,302	82,324,082
Due after 5 years through 10 years	60,110,549	60,314,187
Due after 10 years	10,510,833	10,623,758
Mortgage-backed securities	801,733,446	825,735,707
	$ 965,166,197	$ 991,583,907

NOTE 4 - Securities Held-to-Maturity, continued

There were no sales of securities held-to-maturity in 2008 or 2007. There were no transfers of securities from held-to-maturity to available-for-sale in 2008 or 2007.

Gross unrealized losses on held-to-maturity securities and the fair value of the related held-to-maturity securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2008 were as follows:

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
State and Municipal securities	$ 23,170,146	$ 381,252	$ 321,690	$ 3,077	$ 23,491,836	$ 384,329
Mortgage-backed securities	11,752,675	4,260	-	-	11,752,675	4,260
Total temporarily impaired securities	$ 34,922,821	$ 385,512	$ 321,690	$ 3,077	$ 35,245,511	$ 388,589

The Bank's held-to-maturity portfolio is primarily comprised of mortgage-backed securities issued or guaranteed by FNMA (Fannie Mae) or GNMA (Ginnie Mae). The unrealized losses on mortgage-backed securities are primarily attributable to declining market prices caused by accelerated prepayments on the mortgages resulting from a lower interest rate environment. At December 31, 2008, there were 64 and 1 held-to-maturity securities with unrealized losses less than 12 months and 12 months or longer, respectively.

At December 31, 2008, management believes that held-to-maturity securities in an unrealized loss position were temporary in nature, and therefore no impairment losses were recognized in the statement of income. Because the Bank has the ability and intent to hold these investments until a market price recovery or maturity, these held-to-maturity securities are not considered other-than-temporarily impaired.

Total securities with a carrying value of approximately $695,464,944 and $566,629,316 at December 31, 2008 and December 31, 2007, respectively, were pledged to secure public deposits and for other purposes required by law.

Interest income on tax-exempt securities was $5,696,594 for the year ended December 31, 2008, and $5,338,944 for the year ended December 31, 2007.

NOTE 5 – SECURITIES AVAILABLE-FOR-SALE

The following is a summary of securities available-for-sale:

	December 31, 2008	December 31, 2007
Amortized Cost:		
U.S. Government agency obligations	$ 153,115,436	$ 220,888,970
State and municipal securities	37,717,608	37,169,269
Mortgage-backed securities	213,820,540	188,180,657
	$ 404,653,584	$ 446,238,896
Approximate Fair Value:		
U.S. Government agency obligations	$ 161,062,685	$ 224,910,468
State and municipal securities	38,369,786	37,722,901
Mortgage-backed securities	221,759,920	191,266,013
	$ 421,192,391	$ 453,899,382
Gross Unrealized Gains:		
U.S. Government agency obligations	$ 7,947,249	$ 4,037,131
State and municipal securities	700,394	553,632
Mortgage-backed securities	7,939,380	3,175,959
	16,587,023	7,766,722
Gross Unrealized Losses:		
U.S. Government agency obligations	-	15,633
State and municipal securities	48,216	-
Mortgage-backed securities	-	90,603
	48,216	106,236
Net Unrealized Gains	$ 16,538,807	$ 7,660,486

Maturities at December 31, 2008:

	Amortized Cost	Estimated Fair Value
Due in 1 year or less	$ 40,398,058	$ 40,736,244
Due after 1 year through 5 years	89,390,540	95,157,436
Due after 5 years through 10 years	37,139,115	38,604,874
Due after 10 years	23,905,331	24,933,917
Mortgage-backed securities	213,820,540	221,759,920
	$ 404,653,584	$ 421,192,391

NOTE 5 - Securities Available-for-Sale, continued

There were no sales of securities in 2008 or 2007.

Gross unrealized losses on available-for-sale securities and the fair value of the related available-for-sale securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2008 were as follows:

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
State and Municipal securities	$ 4,831,343	$ 48,216	$ -	$ -	$ 4,831,343	$ 48,216
Total temporarily impaired securities	$ 4,831,343	$ 48,216	$ -	$ -	$ 4,831,343	$ 48,216

The unrealized losses on mortgage-backed securities are primarily attributable to declining market prices caused by accelerated prepayments on the mortgages resulting from a lower interest rate environment. At December 31, 2008, there were 7 available-for-sale securities with unrealized losses less than 12 months and no available-for-sale securities with unrealized losses 12 months or longer. Whenever the cost of an investment security exceeds its fair value, management evaluates, among other factors, general market conditions, the duration and extent to which cost is more than fair value.

At December 31, 2008, management believes that available-for-sale securities in an unrealized loss position were temporary in nature, and therefore no impairment losses were recognized in the income statement. Because the Bank has the ability and intent to hold these investments until a market price recovery or maturity, these available-for-sale securities are not considered other-than-temporarily impaired.

The following represents the related tax effect allocated to each component of other comprehensive income for the year ended December 31, 2008:

	Before-Tax Amount	Tax Expense	Net-of-Tax Amount
Unrealized gains on securities:			
Unrealized holding gains arising during period	$ 8,878,321	$ (3,732,979)	$ 5,145,342
Other comprehensive income	$ 8,878,321	$ (3,732,979)	$ 5,145,342

NOTE 5 - Securities Available-for-Sale, continued

The following represents the related tax effect allocated to each component of other comprehensive income for the year ended December 31, 2007:

	Before-Tax Amount	Tax Expense	Net-of-Tax Amount
Unrealized gains on securities:			
Unrealized holding gains arising during period	$ 8,473,786	$ (3,562,888)	$ 4,910,898
Other comprehensive gains	$ 8,473,786	$ (3,562,888)	$ 4,910,898

NOTE 6 – LOANS AND ALLOWANCE FOR LOAN LOSSES

The following is a summary of the major categories of loans:

	December 31,	
	2008	2007
Commercial	$ 135,113,415	$ 170,218,803
Real estate	1,515,229,002	1,095,261,895
Construction	308,856,536	272,475,343
Consumer	41,752,300	19,172,364
	2,000,951,253	1,557,128,405
Less: Allowance for loan losses	(53,794,344)	(27,229,882)
Loans, net	$ 1,947,156,909	$ 1,529,898,523

Activities in the allowance for loan losses for the years ended December 31, 2008 and 2007 were as follows:

	2008	2007
Balance, beginning of year	$ 27,229,882	$ 23,678,558
Provision for loan losses	52,989,722	6,364,997
Charge-offs	(26,480,673)	(3,007,896)
Recoveries	55,413	194,223
Balance, end of year	$ 53,794,344	$ 27,229,882

The loan portfolio is composed mainly of credit extended to borrowers in Southern California with the majority of loans secured by real estate, even though a substantial amount of the Bank's loans are intended for business purposes. There is no concentration of loans to borrowers in a specific industry within the commercial loan portfolio.

NOTE 6 – Loans and Allowance for Loan Losses, continued

Loans on which the accrual of interest has been discontinued amounted to $85,383,313 at December 31, 2008, and $4,845,762 at December 31, 2007. If interest on these loans had been accrued, interest income would have been increased by approximately $3,402,349 in 2008, and $458,073 in 2007.

During 2008 and 2007, the Bank recorded $17,008 and $131,211, respectively, in interest income recoveries on loans that had previously been on non-accrual.

Loans 90 days or more past due as to interest and/or principal which remain on accrual status approximated $9,321,774 at December 31, 2008 and $15,964,241 at December 31, 2007.

Included in the Bank's loan portfolio are restructured loans, which are those loans whose terms have been modified because of a deterioration in the financial condition of the borrower. The total amount of restructured loans was $1,973,339 at December 31, 2008. There were no restructured loans at December 31, 2007.

At December 31, 2008 and 2007, the recorded investment in loans for which an impairment has been recognized was $54,321,922 and $39,659, respectively, and the related specific allowance for loan losses was $17,587,912 and $39,659, respectively. The recorded investment in loans considered impaired and for which no specific allowance has been recorded was $24,858,221 at December 31, 2008 and $3,932,961 at December 31, 2007. The average recorded investment in impaired loans during 2008 and 2007 was $49,979,425 and $1,832,565, respectively. Interest income recognized on impaired loans was $11,684 during 2008 and $473,297 during 2007.

The Bank had outstanding loan commitments of $407,880,260 and $411,711,469 at December 31, 2008 and 2007, respectively. Substantially, all of the Bank's loan commitments are on a variable rate basis and are comprised of real estate loan commitments. Activities in the reserve for unfunded commitments included in other liabilities in the accompanying balance sheet for the years ended December 31, 2008 and 2007 were as follows:

	2008	2007
Balance, beginning of year	$ 3,317,189	$ 3,192,630
Provision for (reduction of) losses on unfunded commitments	(549,356)	124,559
Charge-offs	-	-
Recoveries	-	-
Balance, end of year	$ 2,767,833	$ 3,317,189

NOTE 7 - BANK PREMISES AND EQUIPMENT

The following is a summary of bank premises and equipment at December 31:

	2008	2007
Land	$ 19,067,560	$ 9,952,616
Buildings	36,092,672	27,883,200
Furniture, fixtures and equipment	23,576,929	17,344,907
Leasehold improvements	3,518,336	3,640,456
	82,255,497	58,821,179
Less accumulated depreciation and amortization	(26,723,877)	(23,875,577)
	$ 55,531,620	$ 34,945,602

Depreciation and amortization expense was $2,919,893 in 2008 and $2,420,601 in 2007.

The Bank is committed under operating leases on certain premises and equipment. Certain leases require the Bank to pay property taxes and insurance. Rental expense was $1,780,369 in 2008 and $1,636,704 in 2007, net of sublease income of $326,374 and $320,259, respectively. Annual minimum lease commitments at December 31, 2008 were:

2009	$ 1,430,942
2010	1,446,217
2011	1,235,521
2012	962,516
2013	915,339
Thereafter	3,367,613

Management expects that in the normal course of business, leases that expire will be renewed or replaced by other leases.

NOTE 8 – TIME DEPOSITS

The following is a summary of time deposits:

	December 31,	
	2008	2007
Time deposits less than $100,000	$ 338,428,568	$ 232,506,904
Time deposits of $100,000 and over	794,712,846	440,167,591
	$ 1,113,141,414	$ 672,674,495

Interest expense on time deposits of $100,000 and over totaled $16,500,579 and $16,183,096 for the years ended December 31, 2008 and 2007, respectively.

NOTE 8 – Time Deposits, continued

At December 31, 2008, the maturity distribution of the Bank's time deposits was as follows:

2009	$ 1,091,896,930
2010	22,584,137
2011	18,166,452
2012	493,895
	$ 1,133,141,414

NOTE 9 – SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

At December 31, 2008 and 2007, securities sold under agreements to repurchase totaled $393,201,735 and $495,545,303 and carried weighted average interest rates of 0.68% and 3.71%, respectively. The securities underlying these agreements were U.S. Treasury securities, U.S. Government agency obligations and mortgage-backed securities with carrying values of $407,792,509 and $531,443,733 and fair values of $422,572,386 and $536,391,941, at December 31, 2008 and 2007, respectively. The securities underlying these agreements are held by a custodian bank until the maturity of the agreement. The identical securities will be repurchased by the Bank.

The average outstanding amounts of securities sold under agreements to repurchase (based upon daily balances) were $466,870,029 in 2008 and $447,917,219 in 2007. The weighted average interest rates were 1.68% in 2008 and 4.12% in 2007, and the maximum amounts outstanding during the periods were $545,603,418 and $564,573,825, respectively. All agreements in 2008 and 2007 are short term with maturities in a range of 6 to 8 weeks.

NOTE 10 – INCOME TAXES

The provision for income taxes for the years ended December 31, 2008 and 2007, is comprised of the following:

	2008	2007
Current:		
Federal	$ 17,497,239	$ 25,491,213
State	6,507,269	8,230,361
Total	24,004,508	33,721,574
Deferred:		
Federal	(4,993,541)	(1,173,374)
State	(2,237,146)	(324,384)
Total	(7,170,597)	(1,497,758)
Total income tax expense	$ 16,833,911	$ 32,223,816

NOTE 10 – Income Taxes, continued

Significant temporary differences that give rise to the deferred tax assets and liabilities as of December 31, 2008 are as follows:

		Assets		Liabilities
Allowance for loan losses	$	23,664,569	$	-
Discount accretion income		-		34,641
State income taxes		73,831		-
Depreciation and amortization		981,175		-
Fair value adjustments on securities available-for-sale		-		6,953,906
Other, net		215,035		-
Total deferred taxes	$	24,934,610	$	6,988,547

Based on management's review of the recoverability of the net deferred tax asset above, no valuation allowance was considered necessary as of December 31, 2008. The net deferred tax asset is included in other assets in the accompanying balance sheets.

Significant temporary differences that give rise to the deferred tax assets and liabilities as of December 31, 2007 are as follows:

		Assets		Liabilities
Allowance for loan losses	$	13,998,042	$	-
Discount accretion income		-		35,323
State income taxes		1,435,034		-
Depreciation and amortization		2,264,938		-
Fair value adjustments on securities available-for-sale		-		3,220,927
Other, net		247,473		188,200
Total deferred taxes	$	17,945,487	$	3,444,450

Based on management's review of the recoverability of the net deferred tax asset above, no valuation allowance was considered necessary as of December 31, 2007.

The Federal tax rate was 35% for 2008 and 2007. A reconciliation of income tax expense and the amount computed by applying the "expected" Federal income tax rate to income before income taxes follows:

	2008	2007
Federal income tax rate	35.0%	35.0%
State income taxes, net of Federal benefit	6.0%	6.3%
Tax exempt income	(4.0%)	(2.0%)
Other, primarily tax credits	(0.8%)	(0.7%)
	36.2%	38.6%

NOTE 11 - COMMITMENTS, CONTINGENCIES AND OFF-BALANCE SHEET RISK

In the normal course of business, there are various outstanding commitments and contingencies, such as financial instruments with off balance sheet risk, which are not reflected in the accompanying financial statements. These financial instruments primarily consist of commitments to extend credit and standby letters of credit issued to meet the financing needs of the Bank's customers. Management does not anticipate any material losses as a result of these transactions.

Commitments to extend credit and standby letters of credit represent exposure to risk only in the event the contract is drawn upon and the other party to the contract defaults. The actual credit risk of these transactions depends upon the credit worthiness of the customer and on the value of any related collateral. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

The Bank had outstanding loan commitments of $407,880,260 and $411,711,469 at December 31, 2008 and 2007, respectively. Substantially, all of the Bank's loan commitments are on a variable rate basis and are comprised of real estate loan commitments.

Standby letters of credit amounting to $49,549,574 and $51,986,436 were outstanding at December 31, 2008 and 2007, respectively. Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Where appropriate, cash or other security support is held as collateral.

From time to time, the Bank is a defendant or plaintiff in various legal proceedings, including litigation arising in the ordinary course of its business. To date, none of these types of litigation has had a material effect on the Bank and, as of December 31, 2008, the Bank is not a party to any material litigation.

NOTE 12 – STOCKHOLDERS' EQUITY AND STOCK OPTION PLAN

In 2007, the Board of Directors and the shareholders approved and authorized the Bank to repurchase up to $150,000,000 of its common stock. As of December 31, 2008, the Bank repurchased 20,547 shares for a total price of $149,993,100 and thereafter retired the shares. There were no shares repurchased as of December 31, 2007.

In 1997, the Bank adopted a stock option plan (the "Plan"), pursuant to which the Board of Directors may grant stock options to officers and key employees. The Plan authorizes grants of options to purchase up to 15,000 shares of authorized but unissued common stock. The Board granted 4,550 options in 1997 and another 1,250 options during 2000. Stock options are granted with an exercise price equal to the stock's fair value at the date of the grant. Stock options have 5 to 10-year terms and vest and become fully exercisable after 5 to 10 years from the date of grant. No options were granted during 2008 and 2007. During 2007, 385 options became exercisable and were exercised during the year. The Plan expired in 2007 in accordance with its terms.

There were no outstanding options at December 31, 2008 and 2007.

NOTE 12 – Stockholders' Equity and Stock Option Plan, continued

Stock option activity during the periods indicated is as follows:

	Number of Shares	Weighted-Average Exercise Price
Balance at December 31, 2006	385	$ 1,900
Granted	-	-
Exercised	(385)	$ 1,900
Forfeited	-	-
Expired	-	-
Balance at December 31, 2007	-	$ -

A summary of the status of the Bank's nonvested shares as of December 31, 2007, and changes during the year ended December 31, 2007, is presented below:

Nonvested Shares	Number of Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2007	385	$ 425.18
Granted	-	-
Vested	(385)	$ 425.18
Forfeited	-	$ -
Nonvested at December 31, 2007	-	$ -

As of December 31, 2008 and 2007, there were no unrecognized compensation costs related to nonvested options granted under the Plan. The average fair value of shares vested during the year ended December 31, 2007 was $6,594.

NOTE 13 - RELATED PARTY TRANSACTIONS

At December 31, 2008 and 2007, there was one loan, with remaining outstanding balance of $438,672, and $447,815, respectively, that the Bank extended to an affiliated party. In the opinion of management, the terms of this loan were the same that would be offered to any other borrower of similar financial strength and collateral.

NOTE 13 – Related Party Transactions, continued

The Bank and Farmers & Merchants Trust Company of Long Beach (Trust Co.) are affiliated parties as a substantial percentage of the outstanding shares of the Bank and the parent company of the Trust Co. are held by common shareholders, who include Richard Darling, William Hayter, Lawrence McLaughlin, Daniel K. Walker, Kenneth G. Walker and W. Henry Walker, each of whom is either a director and/or an officer of the Bank. In addition, certain officers and/or directors of the Bank are also officers and/or directors of the parent company of the Trust Co. and its subsidiaries, including the Trust Co. The Bank provides administrative, accounting and data processing services as well as office space to the Trust Co. The Trust Co. provides trustee and financial management services to the Bank and maintains deposits with the Bank. The Bank and the Trust Co. have entered into an agreement for the exchange of services, which will result in a periodic settlement of amounts owed. This agreement was unanimously approved by their respective audit committee and Board of Directors. The Trust Co. paid the Bank $78,097 and $34,983, respectively, pursuant to the agreement for the exchange of services for each of the years ended December 31, 2008 and 2007.

The Bank leases a branch location from the Trust Co.'s parent corporation. The Bank paid $267,954 and $267,954, respectively, in rent pursuant to this lease for each of the years ended December 31, 2008 and 2007.

NOTE 14 – PROFIT-SHARING PLAN

The Bank has a noncontributory profit-sharing plan in which employees are eligible to participate at year-end if they have been employed for at least 1,000 hours during the year. The Bank contributed $3,191,908 and $3,662,585 to the profit-sharing plan in 2008 and 2007, respectively. At December 31, 2008 and December 31, 2007, no shares of the Bank's stock are held by the trust created by the plan.

NOTE 15 – REGULATORY MATTERS

The Bank is subject to various regulatory capital requirements administered by the Federal and State banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly, additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2008, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2008, the most recent notification from the Federal Reserve Bank categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the institution's category.

NOTE 15 – Regulatory Matters, continued

The Bank's actual regulatory capital amounts and ratios are also presented in the table.

	Actual		For Capital Adequacy Purposes:		To Be Well Capitalized Under Prompt Corrective Action Provisions:	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2008:						
Total Capital (to Risk-Weighted Assets)	$579,506,990	26.04%	≥$178,016,485	≥8.0%	≥$222,520,607	≥10.0%
Tier 1 Capital (to Risk-Weighted Assets)	$551,337,012	24.78%	≥$ 89,008,243	≥4.0%	≥$133,512,364	≥ 6.0%
Tier 1 Capital (to Average Assets)	$551,337,012	16.18%	≥$136,281,773	≥4.0%	≥$170,352,216	≥ 5.0%

	Actual		For Capital Adequacy Purposes:		To Be Well Capitalized Under Prompt Corrective Action Provisions:	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2007:						
Total Capital (to Risk-Weighted Assets)	$709,776,047	37.75%	≥$150,405,956	≥8.0%	≥$188,007,445	≥10.0%
Tier 1 Capital (to Risk-Weighted Assets)	$686,188,127	36.50%	≥$ 75,202,978	≥4.0%	≥$112,804,467	≥ 6.0%
Tier 1 Capital (to Average Assets)	$686,188,127	21.71%	≥$126,408,118	≥4.0%	≥$158,010,148	≥ 5.0%

Farmers & Merchants Bank of Long Beach
2008 Annual Report: Corporate Information

Board of Directors

Daniel K. Walker, Chairman of the Board
Richard W. Darling
Walter M. Florie
William G. Hayter
Timothy W. Jackert
Lawrence J. McLaughlin
Timothy M. Wilson

Principal Officers

Daniel K. Walker, Chairman of the Board and President
W. Henry Walker, Chief Executive Officer
Kenneth G. Walker, President, Main Office
John Hinrichs, Chief Financial Officer

Independent Auditor

KPMG LLP
600 Anton Boulevard, Suite 700
Costa Mesa, CA 92626-7651

Legal Counsel

Paul, Hastings, Janofsky & Walker LLP
695 Town Center Drive, 17th Floor
Costa Mesa, CA 92626

Investor Relations

PondelWilkinson Inc.
1880 Century Park East, Suite 700
Los Angeles, CA 90067

Transfer Agent

Farmers & Merchants Trust Company
302 Pine Avenue
Long Beach, CA 90802

Security Listing

Farmers & Merchants Bank's common stock is traded on the OTC Bulletin Board under the symbol FMBL.

Corporate Headquarters

302 Pine Avenue
Long Beach, CA 90802

Certain statements in the annual report may be forward-looking statements. Readers of this annual report should understand that all such forward-looking statements are inherently subject to risk and uncertainties, some of which cannot be predicted or quantified. Future events and actual results could differ materially from those set forth in, contemplated by or underlying such forward-looking statements and the Bank's actual results or outcomes could differ materially from those anticipated.