HANMI FINANCIAL

2005 ANNUAL REPORT

you're on our mind

Hanmi Bank is a wholly owned subsidiary of Hanmi Financial Corporation (Nasdaq: HAFC). A leading multi-ethnic bank headquartered in Los Angeles, Hanmi Bank provides high quality individual, corporate and institutional financial services in regional markets. Throughout its history, Hanmi has produced long-term profitable growth while adapting to changing market conditions.

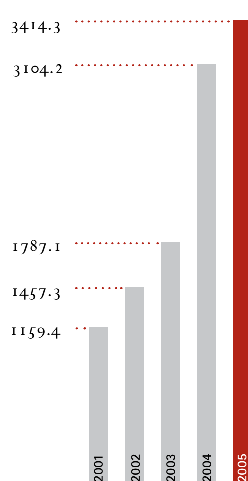
We credit this success to practicing sound and prudent risk management techniques and to nurturing enduring relationships with you — our shareholders, customers and employees. By always keeping you in mind, we are continually building a better bank.

At year-end 2005, your bank had total assets of $3.4 billion and 22 full-service offices in Los Angeles, Orange, San Francisco, Santa Clara and San Diego counties.

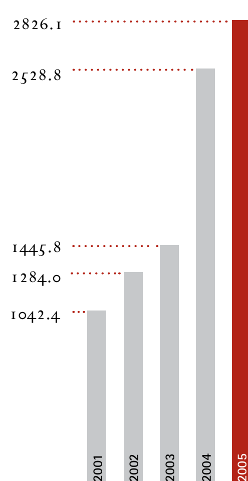
Financial Highlights

(Amounts in thousands, except per share amounts)	2005	2004	2003	2002	2001
For the Year					
Net interest income	$ 136,996	$ 101,749	$ 56,621	$ 47,971	$ 43,688
Service charges and fee income	$ 24,669	$ 21,624	$ 15,397	$ 13,485	$ 12,799
Other operating income	$ 7,547	$ 5,775	$ 4,625	$ 7,719	$ 4,454
Noninterest expenses	$ 69,133	$ 66,566	$ 39,325	$ 38,333	$ 32,028
Net income	$ 58,229	$ 36,700	$ 19,213	$ 17,030	$ 16,810
At Year End					
Total assets	$3,414,252	$3,104,188	$1,787,139	$1,457,313	$1,159,416
Net loans	$2,469,080	$2,234,842	$1,248,399	$ 975,154	$ 781,718
Total deposits	$2,826,114	$2,528,807	$1,445,835	$1,283,979	$1,042,353
Shareholders' equity	$ 426,777	$ 399,910	$ 139,467	$ 124,468	$ 104,873
Per Common Share					
Net income (diluted)	$ 1.17	$ 0.84	$ 0.67	$ 0.60	$ 0.60
Cash dividends declared	$ 0.20	$ 0.20	$ 0.20	$ —	$ —
Book value	$ 8.77	$ 8.11	$ 4.92	$ 4.47	$ 3.83
Financial Ratios					
Net interest margin	4.77%	4.26%	3.68%	3.93%	4.25%
Nonperforming loans to total gross loans	0.41%	0.27%	0.68%	0.65%	0.63%
Allowance for loan losses to total gross loans	1.00%	1.00%	1.06%	1.14%	1.19%
Efficiency ratio	40.86%	51.54%	51.31%	55.41%	52.40%
Tier 1 capital to average total assets*	9.06%	8.78%	7.75%	8.34%	8.76%
Total risk-based capital*	11.80%	11.80%	11.09%	11.94%	12.75%
Return on average assets	1.79%	1.37%	1.18%	1.30%	1.53%
Return on average equity	13.94%	12.51%	14.51%	15.08%	17.56%

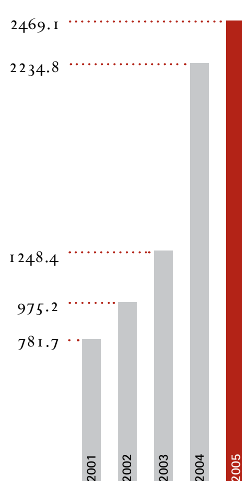
* *Hanmi Bank ratio*



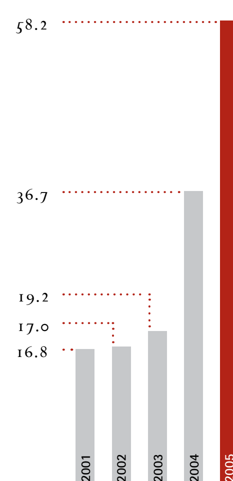
Total Assets
(dollars in millions)



Total Deposits
(dollars in millions)



Net Loans
(dollars in millions)



Net Income
(dollars in millions)

To Our Shareholders

Last year was by far the most successful in Hanmi's history. It also marked a crucial turning point in Hanmi's development. To best explain how the year's accomplishments and challenges fit within our strategic plan, this letter will recap 2005's highlights, summarize our expectations for 2006 and outline our aspirations for the next five to ten years.

2005 Highlights

Hanmi again posted a record-breaking year. At December 31, 2005, assets were an unprecedented $3.41 billion, compared to $3.10 billion at the end of 2004. Net income for the year was a record $58.2 million, up from $36.7 million the year prior. We saw a year-over-year improvement in net interest margin, to 4.77 percent in 2005 from 4.26 percent for 2004. And earnings per share were $1.17 (diluted) as compared to $0.84 (diluted) in 2004.

These results demonstrate the core strengths of our operations and are credited, in good part, to our timely and efficient integration of Hanmi Bank and Pacific Union Bank following our April 2004 merger. We believe we have fully realized the operating efficiencies afforded by our merger and that the combined strengths of our operations will continue to serve us well in the future.

During 2005 we assembled a management team that has the experience, energy and ability to achieve our defined milestones. We introduced an Incentive Compensation Plan (ICP) for our branch managers and senior management that rewards performance and excellence. In addition to institutionalizing best-practices performance throughout our organization, the ICP is designed to promote stronger growth in loan originations and the gathering of less costly deposits. We expanded our loan production capabilities with the opening of three new loan production offices out of state.

We tackled challenges during 2005 specific to our market. These included growing competition, which increased pricing pressures on both loans and deposits and created a greater demand for experienced employees. We have taken steps to counteract these market forces and enter 2006 with considerable optimism.

2006 Outlook

Our confidence stems from the fundamental and systemic adjustments we have made at Hanmi over the past 18 months – and our planned extension of those programs deeper into the organization. For example, the ICP and training programs now apply to loan officers as well as senior management. We are rolling out sales and service training, and continue to make staff retention a priority. The marketing and product development team we recruited in 2005 is spearheading vital new programs for us. And we plan to open additional out-of-state loan production offices this year.

We continue to make significant improvements in our operations as well. In January we reorganized our structure into six districts. Each is headed by a proven leader, and all support our more sales-focused culture. Hanmi will benefit from the competition among the districts, and the structure enables us to incorporate greater budget accountability.

As for market trends, we anticipate that interest rates will continue to inch up over the coming year. We could see growing stress on the real estate market and a deceleration in economic growth. These are normal and predictable market trends, and we have positioned ourselves well to manage their effects on our operations.

Future Growth

Hanmi is becoming a leading regional commercial bank and, as such, we are growing our products and services to meet our customers' financial needs. They require more sophisticated banking services, and instead of turning to major banks, they should find those services at Hanmi. We are increasing our middle-market lending and offering additional lending products.

To make our current and potential customers aware of our broader range of products and services, we will increase our sales and marketing efforts. We are implementing a Customer Relationship Management system to increase and measure our success. And we are training employees at all levels to advise customers on the banking products that will best meet their objectives. To make sure our customers continue to turn to Hanmi for their commercial banking needs, we will focus on providing excellent customer service. Through every contact with the bank, our customers will know that they are being served by the best in the business.

Hanmi is becoming a leading regional commercial bank and, as such, we are growing our products and services to meet our customers' financial needs. They require more sophisticated banking services, and instead of turning to major banks, they should find those services at Hanmi.

Our accomplishments, our abilities and our aspirations in 2005, 2006 and beyond are geared toward building value in the organization. All we do is undertaken with you – our shareholders, our customers and our employees – in mind. We thank you for your continued support and look forward to sharing our future accomplishments with you.

Sincerely,

Joon Hyung Lee
Chairman of the Board

Sung Won Sohn
President and Chief Executive Officer

you're on our mind

Our customers are the foundation for all we do

Jung Hak Son
District Leader

Hassan M. Bouayad
Chief Lending Officer

Suki Murayama
District Leader

entrepreneurial spirit

From our inception, we have focused on serving the Korean-American community. Beyond being a natural fit for our founders, the Korean-American demographic has long demonstrated attributes attractive to bankers. Among all U.S. ethnic groups, Korean-Americans boast the highest rate of entrepreneurship: One of every eight owns his or her own business. They also sustain a savings rate that is one of the highest among all U.S. residents.

Over the past five years, the Korean-American market has delivered a 29 percent compounded annual growth rate (CAGR) in loans and a 23 percent CAGR in deposits. As the business ownership and savings rates within our community generate increased wealth, our customers demand more sophisticated products and services.

extensive reach

Of the 2.2 million Korean-Americans in the United States, 40 percent reside in California. Hanmi Bank has the most extensive branch network in the region to serve them. Moreover, we have leveraged our expertise to reach out to other ethnic groups, including those of Iranian and Indian descent. Currently more than 40 percent of our loans are from the non-Korean-American market. We will continue this trend by adding more loan production offices in ethnic communities.

Our resources and infrastructure – specifically $3.41 billion in assets, a network of 22 branch offices and command of the highest share of the Korean-American market – give us a significant competitive advantage over our peers.

established relationships

Our infrastructure also is impressive in that it is so well established. We, as the marriage of Hanmi Bank and Pacific Union Bank, are the oldest bank serving our community. Our branch managers and other staff members have forged long-lasting, personal relationships with our customers. That connectedness with our community is invaluable.

proven leadership

Hanmi Financial is honored and proud to have leaders at all levels of the organization. These professionals include our CEO, Dr. Sung Won Sohn. Our senior management team possesses many years of experience in Korean-American and major U.S. banks, and the vision to accomplish our strategic goals. We have branch managers who have served us well for 20 years or more, and among our newer employees are individuals whose ideas and energy are inspirational to all.

We believe that rewarding excellence multiplies excellence. Nurturing and recognizing our employees' performance opens up channels for new ideas, innovative products and services, and opportunities for growth that our customers clearly count as a differentiating factor between us and our competitors.

reinforced excellence

Employee capabilities go far toward establishing us as the bank of choice among our current and targeted customers. To sustain, expand and encourage those capabilities, we introduced two new programs in 2005. One is our Incentive Compensation Plan, which rewards strong performance and productivity. The other is internal training to arm our staff with the tools they need to excel in their jobs. Courses range from fundamental skills such as using computer software to cross-selling and team selling.

incomparable talent

We believe we have the best talent in the market. To recruit, improve and retain such highly qualified people, we continue to develop career paths and to tailor opportunities that will help our employees attain their professional and personal goals.

you're on our mind

Our people make all the difference

Greg Kim
Chief of Operations

J. Han Park
District Leader

you're on our mind

Let's get together to discuss the CRA Service hours and share ideas on how to achieve our goals.

Invite Mr. Lee to lunch to express Hanmi's deep appreciation for his long and loyal patronage.

◦ Payroll card SVC - issue CK Card to non-account holders of customers business

Our service will be our trademark

SM Meeting
- DFI/FRB joint exam to begin 3/13
- Send loan file list to branches
- File review by SCOs

◦ Image statement for individual customers

Helen Kim	Steve Choe	Ae Cha Kim
District Leader	*Chief of Banking Services*	*District Leader*

customer-driven approach

Hanmi Financial's vision is "Meeting all of our customers' financial needs and growing with them." Our commitment to that vision mandates that we provide the best possible customer service. We are dedicated to ensuring that our products and services are tailored to the needs and sensibilities of the people we serve.

We operate in a fiercely competitive marketplace. We believe our success depends on delivering the best possible service to our customers. While intangible, our trademark service will ensure that we build long-term and sustainable value for our shareholders, customers and employees.

To set new standards, we pay close attention to each and every customer who visits our branches. We are training our branch managers, loan officers and tellers on how to best address their customers' needs. Earlier this year, we reorganized our branching groups into six districts, headed by executives who have proven their excellence through more than 70 combined years of service to the bank.

streamlined operations

We have centralized our back-office support functions so that district and branch managers have more time to build relationships with their customers, market our products and services, and increase our employees' skills. To measure and enhance the effectiveness of our services, we soon will implement a Customer Relationship Management (CRM) system.

At Hanmi, we believe the success of our business rests fundamentally on loyalty, confidence and trust – and that those qualities must exist between our customers and all of us and across the levels of our organization.

diversified portfolio

Hanmi Bank began as a community commercial bank and has built core competencies around serving ethnic markets' financial needs. The recent years of record low interest rates and exponentially growing property values have enabled us to grow and prosper in real estate lending. We expect growth in the sector to slow as interest rates rise and property value appreciation decelerates. To ensure continued success for our business, and sustained shareholder value, we are working to expand the commercial and industrial lending portion of the business, emphasizing cash flow. Changing the mix of our lending portfolio will add balance and diversify risk.

We operate in a fiercely competitive marketplace for customers. We are committed to making decisions that ensure robust business today while simultaneously building value for tomorrow and beyond.

balanced approach

"Balanced" is a word we use to describe our operating philosophy as well as our portfolio. We continue to closely monitor and manage our credit quality. As a result, we have a reputation in our community for having high-quality assets. We are known among our peers for management tenets that ensure long-term quality and returns.

insightful management

Our management team knows first-hand the cycles that the economy follows. They are vigilant in monitoring the signs of coming change. While market risks cannot be fully mitigated, would-be surprises can be anticipated and diffused. Given our balanced approach and insightful team, we look forward to the challenges and opportunities of our ever-changing marketplace.

you're on our mind

View of Role -- Joint Effort
① Underwriting
② Credit Fundamentals
③ Won't always agree

9 Underwriting:
centralization
10 Discuss w/ SCO's
• Loan Type
11 • Region
• Servicing
12 noon

Our **asset quality** remains superior

3 ALCO committee
Discuss our Gap
4 position & fixed rate
loans.
5

Plans
① Streamline approval – Slow now – leaving HR
② Writing format
③ Visit Branches
④ Provide Guidance – Any Basis → Good Credit
⑤ Training

10 Loan Committee
11 1 case to FFC.

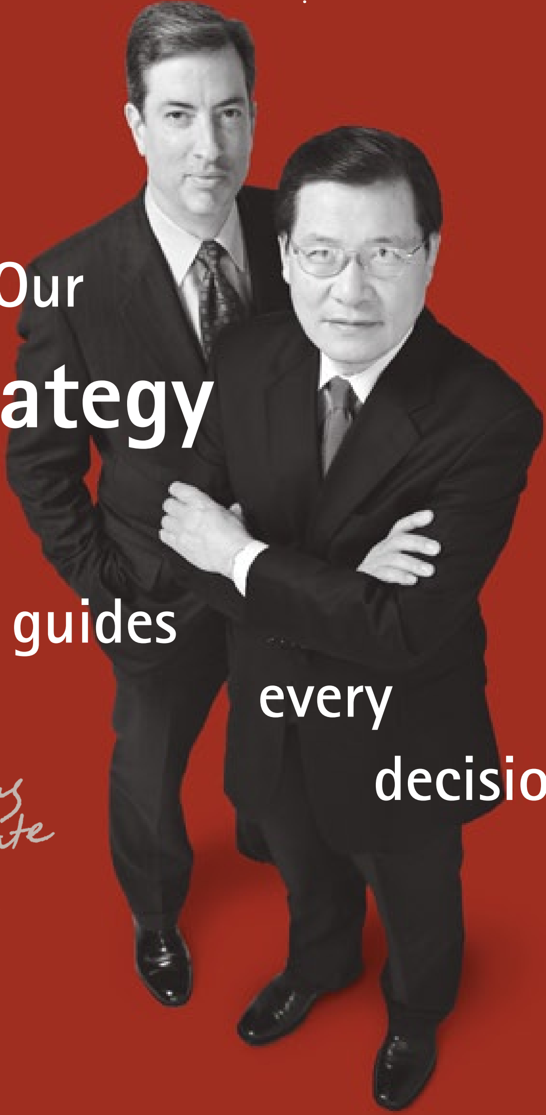
Kurt M. Wegleitner
Chief Credit Officer

Eunice U. Lim
Deputy Chief Credit Officer

you're on our mind

Can we increase the fixed rate loan up to the point of flat Gap position?

Get input from Branch Managers on incentive comp. plan



Our strategy guides every decision

Meet with road trip investors on Tuesday

Special ALCO meeting to discuss flat rate strategy Tuesday

Muni Bonds still have positive market value because of the term and tax exempt provision,
long term

Michael J. Winiarski
Chief Financial Officer

Sung Won Sohn
President & Chief Executive Officer

forward looking

From our inception through 2003, we focused on growth. We grew steadily and were the largest Korean-American bank before we acquired Pacific Union Bank, our market's oldest bank. Our first years of growth gave us infrastructure, momentum and recognition. Those assets will serve us well as we have added profitability to our growth focus.

Ethnic banks in Southern California have traditionally focused on serving their customers' real estate needs. When those customers wanted more sophisticated services, they often moved to major U.S. banks. We want to be the "go-to" bank for the ethnic groups we serve.

pragmatic process

We are the market leader because we have made changes. Yet making changes is not necessarily the same thing as taking risks. We have carefully weighed our options along the way, and our decisions have followed a carefully conceived business strategy, a strategy that guides us today.

In 2005, we completed the integration of Pacific Union Bank and realized significant economies of scale. We solidified our management team. We made keeping the industry's best talent one of our priorities, and stabilized our workforce. And we have worked diligently to instill cultural changes throughout our organization that will ensure continuous compliance with government regulations.

The pieces are in place. Hanmi Financial is poised to execute on a number of plans designed to definitively differentiate our bank from our competition; to complete our transformation into a regional commercial bank; and to realize the upside potential we have worked for a quarter of a century to create.

next steps on our strategic path

All of us at Hanmi Financial are excited about the future of our organization, our bank and our business. We believe we have solidified the requisite components for success – a strong customer base, incomparable employees, customer-driven services, excellent asset quality and a strategic business model. We are now leveraging their collective strengths to make Hanmi Bank the "go-to" regional commercial bank for ethnic groups in California. Our broad plans include the operating philosophies outlined below.

We have a well thought-out strategic plan. However, new opportunities and innovative developments will determine our actual course. We remain flexible, so we can quickly adapt to changes, and proactive, so that we can manage challenges before they arise. At the same time, we will remain disciplined, persistently pursuing our vision.

future growth will be both organic and external

We have the necessary critical mass to grow our business from within, which is an incredible strength. Our strong balance sheet gives us the capacity to fund the development of new products and new internal systems necessary to support continuing growth. At the same time, we command the resources to enable us to make acquisitions given the perfect opportunity. We are conservative, yet growth oriented, and will make the decisions that add the most value to our business as we move forward.

we will upgrade existing products and introduce new ones

Our stated vision is to meet all of our customers' financial needs and grow with them. To do so, we will expand our product offerings and be more proactive in counseling our customers in their financial matters. While we will be stretching our boundaries in this endeavor, we will be offering tried-and-true products.

we will emphasize sales and service

We are the oldest and largest bank in our market. Our connections with our community run deep, and we are in a position now to expand those relationships.

we will explore expansion into other markets

We plan to open additional new loan production offices in 2006. We will add more branches to our already extensive network in California and potentially in other large multi-ethnic communities across the country. And we have the option of becoming a larger player in facilitating investments and other banking activities between customers in the United States and Korea. Hanmi Financial possesses numerous options for expanding its business – options we will keep open.

One difference between us and our competitors is that we are willing – indeed, eager – to position ourselves to clear even higher bars in the future. In fact, we are raising those bars ourselves. We are implementing strategies to diversify our portfolio when others are not. We are basing compensation on performance measures even in the face of a talent shortage in our marketplace. Our approach is different than our competitors', but we believe rewarding excellence is the right way to do business. We are examining operations and procedures throughout our organization and institutionalizing best practices. That, too, is the right way to do business.

We are doing all of these things because when you conduct business in the most impeccable and service-oriented manner, your customers are satisfied. They refer additional customers. Your employees are proud of their work and their contribution to their community. They recruit like-minded professionals. Your shareholders realize a favorable return on their investments, and they continue to support your endeavors. We are pursuing the best business practices because all of you – shareholders, customers and employees – are on our mind.

Corporate Information

Independent Public Accountants

KPMG, LLP
Los Angeles, California

Registrar and Transfer Agent

U.S. Stock Transfer Corporation
Glendale, California

Website

www.hanmifinancial.com

Stock Listing

Nasdaq

Ticker symbol for common stock "HAFC"

Left to right:
Joseph K. Rho
Dr. Chang Kyu Park
M. Christian Mitchell
Dr. Sung Won Sohn
Kraig Kupiec
Joon Hyung Lee
I Joon Ahn
Dr. Won R. Yoon
Richard B. C. Lee

Officers

Dr. Sung Won Sohn
President and
Chief Executive Officer

Michael J. Winiarski
Senior Vice President and
Chief Financial Officer

Kurt M. Wegleitner
Executive Vice President and
Chief Credit Officer

Board of Directors

Joon Hyung Lee
Chairman of the Board
President
Root-3 Corporation

Richard B.C. Lee
Vice Chairman of the Board
President
B.C. Textiles, Inc.

I Joon Ahn
Former Chairman of the Board

Kraig Kupiec
Managing Member
Shoreline Trading Group

M. Christian Mitchell
Former Partner
Deloitte & Touche

Dr. Chang Kyu Park
Former Chairman of the Board
Principal Pharmacist
Serrano Medical Center
Pharmacy

Joseph K. Rho
Former Chairman of the Board
Principal
J & S Investment

William J. Ruh
Executive Vice President
Castle Creek Capital LLC

Dr. Sung Won Sohn
President and
Chief Executive Officer

Dr. Won R. Yoon
Former Chairman of the Board
Chief Surgeon
Olympic Medical Center

In memoriam

We note with regret the passing of our colleague, Ung Kyun Ahn, distinguished member and former Chairman of Hanmi's Board of Directors.

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Selected Financial Data

The following table presents selected historical financial information, including per share information as adjusted for the stock dividends and stock splits declared by us. This selected historical financial data should be read in conjunction with our consolidated financial statements and the notes thereto appearing elsewhere in this Report and the information contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations." The selected historical financial data as of and for each of the years in the five years ended December 31, 2005 is derived from our audited financial statements. In the opinion of management, the information presented reflects all adjustments, including normal and recurring accruals, considered necessary for a fair presentation of the results of such periods.

	As of and for the Year Ended December 31,				
(Dollars in Thousands, Except for Per Share Data)	*2005*	*2004*	*2003*	*2002*	*2001*
Summary Statement of Income Data:					
Interest income	$ 199,107	$ 134,366	$ 77,417	$ 69,316	$ 76,678
Interest expense	62,111	32,617	20,796	21,345	32,990
Net interest income before provision for credit losses	136,996	101,749	56,621	47,971	43,688
Provision for credit losses	5,395	2,907	5,680	4,800	1,400
Non-interest income	32,216	27,399	20,022	21,204	17,253
Non-interest expenses	69,133	66,566	39,325	38,333	32,028
Income before income taxes	94,684	59,675	31,638	26,042	27,513
Income taxes	36,455	22,975	12,425	9,012	10,703
Net income	$ 58,229	$ 36,700	$ 19,213	$ 17,030	$ 16,810
Summary Statement of Financial Condition Data:					
Cash and cash equivalents	$ 163,477	$ 127,164	$ 62,595	$ 122,772	$ 81,205
Total securities	443,912	418,973	414,616	279,548	213,179
Loans receivable, net [1]	2,469,080	2,234,842	1,248,399	975,154	781,718
Total assets	3,414,252	3,104,188	1,787,139	1,457,313	1,159,416
Total deposits	2,826,114	2,528,807	1,445,835	1,283,979	1,042,353
Total liabilities	2,987,475	2,704,278	1,647,672	1,332,845	1,054,543
Total shareholders' equity	426,777	399,910	139,467	124,468	104,873
Tangible equity	209,028	178,791	137,424	122,304	102,689
Average net loans	2,359,439	1,912,534	1,103,765	882,625	701,714
Average securities	418,964	425,537	379,635	244,675	235,034
Average interest-earning assets	2,871,564	2,387,412	1,538,820	1,222,050	1,029,046
Average total assets	3,249,190	2,670,701	1,623,214	1,308,885	1,100,182
Average deposits	2,632,254	2,129,724	1,416,564	1,164,562	988,392
Average interest-bearing liabilities	2,046,227	1,687,688	1,057,249	854,858	736,947
Average shareholders' equity	417,813	293,313	132,369	112,927	95,740
Average tangible equity	198,527	143,262	130,252	110,762	93,427
Per Share Data:					
Earnings per share – basic	$ 1.18	$ 0.87	$ 0.68	$ 0.62	$ 0.61
Earnings per share – diluted	$ 1.17	$ 0.84	$ 0.67	$ 0.60	$ 0.60
Book value per share [2]	$ 8.77	$ 8.11	$ 4.92	$ 4.47	$ 3.83
Tangible book value per share [3]	$ 4.30	$ 3.62	$ 4.85	$ 4.39	$ 3.75
Cash dividends per share	$ 0.20	$ 0.20	$ 0.20	$ —	$ —
Common shares outstanding	48,658,798	49,330,704	28,326,820	27,830,866	27,385,660

(Dollars in Thousands, Except for Per Share Data)	As of and for the Year Ended December 31,				
	2005	2004	2003	2002	2001
Selected Performance Ratios:					
Return on average assets [4]	1.79%	1.37%	1.18%	1.30%	1.53%
Return on average shareholders' equity [5]	13.94%	12.51%	14.51%	15.08%	17.56%
Return on average tangible equity [6]	29.33%	25.62%	14.75%	15.38%	17.99%
Net interest spread [7]	3.89%	3.70%	3.06%	3.17%	2.97%
Net interest margin [8]	4.77%	4.26%	3.68%	3.93%	4.25%
Efficiency ratio [9]	40.86%	51.54%	51.31%	55.41%	52.40%
Dividend payout ratio [10]	16.95%	22.99%	29.41%	—	—
Average shareholders' equity to average total assets	12.86%	10.98%	8.15%	8.63%	8.70%
Selected Capital Ratios:					
Tier 1 capital to average total assets:					
Hanmi Financial	9.11%	8.93%	7.80%	8.50%	8.86%
Hanmi Bank	9.06%	8.78%	7.75%	8.34%	8.76%
Tier 1 capital to total risk-weighted assets:					
Hanmi Financial	11.03%	10.93%	10.05%	11.01%	11.71%
Hanmi Bank	10.96%	10.75%	10.00%	10.81%	11.59%
Total capital to total risk-weighted assets:					
Hanmi Financial	12.04%	11.98%	11.13%	12.14%	12.87%
Hanmi Bank	11.98%	11.80%	11.09%	11.94%	12.75%
Selected Asset Quality Ratios:					
Non-performing loans to total gross loans [11]	0.41%	0.27%	0.68%	0.65%	0.63%
Non-performing assets to total assets [12]	0.30%	0.19%	0.48%	0.44%	0.43%
Net loan charge-offs to average total gross loans	0.12%	0.19%	0.29%	0.28%	0.45%
Allowance for loan losses to total gross loans	1.00%	1.00%	1.06%	1.14%	1.19%
Allowance for loan losses to non-performing loans	246.40%	377.49%	154.13%	173.81%	188.12%

(1) Loans are net of deferred fees and related direct costs.

(2) Total shareholders' equity divided by common shares outstanding.

(3) Tangible equity divided by common shares outstanding.

(4) Net income divided by average total assets.

(5) Net income divided by average shareholders' equity.

(6) Net income divided by average tangible equity.

(7) Average yield earned on interest-earning assets less average rate paid on interest-bearing liabilities.

(8) Net interest income before provision for credit losses divided by average interest-earning assets.

(9) Total non-interest expenses divided by the sum of net interest income before provision for credit losses and total non-interest income.

(10) Dividends declared per share divided by basic earnings per share.

(11) Non-performing loans consist of non-accrual loans, loans past due 90 days or more and restructured loans.

(12) Non-performing assets consist of non-performing loans (see footnote (11) above) and other real estate owned.

Non-GAAP Financial Measures

Return on Average Tangible Equity

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:

	Years Ended December 31,				
(Dollars in Thousands)	*2005*	*2004*	*2003*	*2002*	*2001*
Average shareholders' equity	$417,813	$293,313	$132,369	$112,927	$95,740
Less average goodwill and core deposit intangible assets	(219,286)	(150,051)	(2,117)	(2,165)	(2,313)
Average tangible equity	$198,527	$143,262	$130,252	$110,762	$93,427
Return on average shareholders' equity	13.94%	12.51%	14.51%	15.08%	17.56%
Effect of average goodwill and core deposit intangible assets	15.39%	13.11%	0.24%	0.30%	0.43%
Return on average tangible equity	29.33%	25.62%	14.75%	15.38%	17.99%

Tangible Book Value Per Share

Tangible book value per share is supplemental financial information determined by a method other than in accordance with GAAP. This non-GAAP measure is used by management in the analysis of Hanmi Financial's performance. Tangible book value per share is calculated by subtracting goodwill and core deposit intangible assets from total shareholders' equity and dividing the difference by the number of shares of common stock outstanding. 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:

	Years Ended December 31,				
(Dollars in Thousands)	*2005*	*2004*	*2003*	*2002*	*2001*
Total shareholders' equity	$426,777	$399,910	$139,467	$124,468	$104,873
Less average goodwill and core deposit intangible assets	(217,749)	(221,119)	(2,043)	(2,164)	(2,184)
Tangible equity	$209,028	$178,791	$137,424	$122,304	$102,689
Book value per share	$8.77	$8.11	$4.92	$4.47	$3.83
Effect of goodwill and core deposit intangible assets	(4.47)	(4.49)	(0.07)	(0.08)	(0.08)
Tangible book value per share	$4.30	$3.62	$4.85	$4.39	$3.75

This discussion presents management's analysis of the financial condition and results of operations as of and for the years ended December 31, 2005, 2004 and 2003. This discussion should be read in conjunction with our consolidated financial statements and the notes related thereto presented elsewhere in this report.

This discussion and analysis contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in such forward-looking statements because of certain factors discussed elsewhere 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 the "Notes to Consolidated Financial Statements." 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 critical accounting policies. We use estimates and assumptions based on historical experience and other factors that we believe to be reasonable under the circumstances. Actual results could differ significantly from these estimates and assumptions, which 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 Hanmi Financial's Board of Directors.

During the year ended December 31, 2004, in accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, *"Business Combinations"* ("SFAS No. 141"), 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 Bank used market data regarding securities market prices and interest rates to estimate the fair values of financial assets, including the securities portfolio, deposits and borrowings. 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.

We believe the allowance for loan losses and allowance for off-balance sheet items 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 "Financial Condition – Allowance for Loan Losses and Allowance for Off-Balance Sheet Items," "Results of Operations – Provision for Credit Losses" and "Notes to Consolidated Financial Statements, Note 1 – Summary of Significant Accounting Policies" for a description of the methodology used to determine the allowance for loan losses and allowance for off-balance sheet items.

Overview

On April 30, 2004, we completed the merger with PUB. Therefore, operating results for the year ended December 31, 2004 include eight months of operations of the combined entity and reflect an increase in average total assets from $2.67 billion for the year ended December 31, 2004 to $3.25 billion for the year ended December 31, 2005.

Over the last two years, we have experienced significant growth in assets and deposits. Total assets increased to $3,414.3 million at December 31, 2005 from $3,104.2 million and $1,787.1 million at December 31, 2004 and 2003, respectively. Net loans increased to $2,469.1 million at December 31, 2005 from $2,234.8 million and $1,248.4 million at December 31, 2004 and 2003, respectively. Total deposits increased to $2,826.1 million at December 31, 2005 from $2,528.8 million and $1,445.8 million at December 31, 2004 and 2003, respectively. Our asset growth was mainly due to the acquisition of PUB, which had assets of $1.2 billion, and also was attributable to loan production during the period.

For the year ended December 31, 2005, net income was $58.2 million, representing an increase of $21.5 million, or 58.7 percent, from $36.7 million for the year ended December 31, 2004. This resulted in basic earnings per share of $1.18 and $0.87 for the years ended December 31, 2005 and 2004, respectively, and diluted earnings per share of $1.17 and $0.84 for the same years. Our primary source of revenue is net interest income, which is the difference between interest and fees derived from earning assets and interest paid on liabilities incurred to fund those assets. Net interest income is affected by changes in the volume of interest-earning assets and interest-bearing liabilities. It also is affected by changes in yields earned on interest-earning assets and rates paid on interest-bearing liabilities. The increase in net income for 2005 was attributable to increases in net interest margin and average interest-earning assets. Net interest income increased due to a 23.2 percent increase in volume of gross loans. The average interest rate paid on interest-bearing liabilities increased by 111 basis points while the average interest rate earned on interest-earning assets increased by 130 basis points. As a result, net interest spread increased by 19 basis points from 3.70 percent in 2004 to 3.89 percent in 2005.

For the year ended December 31, 2004, net income was $36.7 million, representing an increase of $17.5 million, or 91.0 percent, from $19.2 million for the year ended December 31, 2003. This resulted in basic earnings per share of $0.87 and $0.68 for the years ended December 31, 2004 and 2003, respectively, and diluted earnings per share of $0.84 and $0.67 for the same years. The increase in net income for 2004 was attributable to increases in net interest margin and average interest-earning assets. Net interest income increased due to a 73.1 percent increase in volume of gross loans. The average interest rate paid on interest-bearing liabilities decreased by four basis points while the average interest rate earned increased by 60 basis points. As a result, net interest spread increased by 64 basis points from 3.06 percent in 2003 to 3.70 percent in 2004.

Our results of operations are significantly affected by the provision for credit losses. The provision for credit losses was $5.4 million, $2.9 million and $5.7 million in 2005, 2004 and 2003, respectively, reflecting changes in the balance and credit quality of the loan portfolio.

We also generated substantial non-interest income from service charges on deposit accounts, charges and fees from international trade finance, and gains on sales of loans. For the year ended December 31, 2005, non-interest income was $32.2 million, an increase of $4.8 million, or 17.6 percent, over 2004 non-interest income of $27.4 million. For the year ended December 31, 2004, non-interest income was $27.4 million, an increase of $7.4 million, or 36.8 percent, over 2003 non-interest income of $20.0 million. The increases in both years resulted primarily from the merger with PUB and expansion in the Bank's loan and deposit portfolios.

Non-interest expenses consist primarily of employee compensation and benefits, occupancy and equipment expenses and data processing expenses. For the year ended December 31, 2005, non-interest expenses were $69.1 million, an increase of $2.6 million, or 3.9 percent, over 2004 non-interest expenses of $66.6 million. For the year ended December 31, 2004, non-interest expenses were $66.6 million, an increase of $27.3 million, or 69.3 percent, over 2003 non-interest expenses of $39.3 million. In both years, the increases were primarily the result of the merger with PUB. The efficiency ratio improved to 40.86 percent in 2005 compared to 51.54 percent in 2004 as the Bank achieved greater operating efficiencies after completing the integration of PUB's operations into the Bank's, whereas 2004 non-interest expenses included the cost of parallel operations and non-recurring expenses associated with the merger. In 2004, the efficiency ratio increased slightly to 51.54 percent compared to 51.31 percent in 2003 because of non-recurring expenses associated with the merger.

Results of Operations

Net Interest Income and Net Interest Margin

Our earnings depend largely upon the difference between the interest income received from our loan portfolio and other interest-earning assets and the interest paid on deposits and borrowings. The difference is "net interest income." The difference between the yield earned on interest-earning assets and the cost of interest-bearing liabilities is "net interest spread." 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. Our net interest income also is 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 FRS.

For the years ended December 31, 2005 and 2004, net interest income was $137.0 million and $101.7 million, respectively. The net interest spread and net interest margin for the year ended December 31, 2005 were 3.89 percent and 4.77 percent, respectively, compared to 3.70 percent and 4.26 percent, respectively, for the year ended December 31, 2004.

For the years ended December 31, 2004 and 2003, net interest income was $101.7 million and $56.6 million, respectively. The net interest spread and net interest margin for the year ended December 31, 2004 were 3.70 percent and 4.26 percent, respectively, compared to 3.06 percent and 3.68 percent, respectively, for the year ended December 31, 2003.

Average interest-earning assets increased 20.3 percent to $2,871.6 million in 2005 from $2,387.4 million in 2004. Average gross loans increased 23.2 percent to $2,382.2 million in 2005 from $1,933.8 million in 2004, and average investment securities decreased 1.5 percent to $419.0 million in 2005 from $425.5 million in 2004. Total loan interest income increased by 53.2 percent in 2005 on an annual basis due to the increase in average gross loans outstanding and the increase in the average yield on loans from 6.04 percent in 2004 to 7.51 percent in 2005. The average interest rate charged on loans increased 147 basis points, reflecting the

increase in the WSJ Prime Rate of 185 basis points from 4.34 percent in 2004 to 6.19 percent in 2005. The yield on average interest-earning assets increased from 5.63 percent in 2004 to 6.93 percent in 2005, an increase of 130 basis points, reflecting a shift in the mix of interest-earning assets from 81.0 percent loans, 17.8 percent securities and 1.2 percent other interest-earning assets in 2004 to 83.0 percent loans, 14.6 percent securities and 2.4 percent other interest-earning assets in 2005.

The majority of interest-earning assets growth was funded by a $502.5 million, or 23.6 percent, increase in average total deposits. Total average interest-bearing liabilities grew by 21.2 percent to $2,046.2 million in 2005 compared to $1,687.7 million in 2004. The average interest rate paid for interest-bearing liabilities increased by 111 basis points from 1.93 percent in 2004 to 3.04 percent in 2005 due to competitive pricing. As a result of the increases in the yield on interest-earning assets and cost of interest-bearing liabilities, the net interest spread increased to 3.89 percent in 2005 compared to 3.70 percent in 2004.

The 2005 net interest spread reflects the increase in the average balance of Federal funds sold, which are highly liquid but have a relatively low yield, from $12.8 million in 2004 to $46.8 million in 2005. The average yield on Federal funds sold was 3.40 percent and 1.43 percent in 2005 and 2004, respectively. In the second half of 2005, the Bank increased its rates on certificates of deposit to maintain relationships with valued customers and fund loan growth. In 2005, loan production increased 32.2 percent over 2004 levels. This trend was particularly evident in the second quarter of 2005 and continued throughout the second half of the year, during which production was 37.4 percent higher than 2004 levels. However, because of the flat yield curve (long-term interest rates were unusually low relative to short-term rates, approaching an briefly falling below short-term rates) and strong competition, the Bank experienced a high level of loan payoffs because management was unwilling to match the aggressive pricing on five- to seven-year fixed-rate loans offered to our customers by certain competitors.

Average interest-earning assets increased 55.1 percent to $2,387.4 million in 2004 from $1,538.8 million in 2003. Average gross loans increased 73.1 percent to $1,933.8 million in 2004 from $1,117.0 million in 2003 and average investment securities increased 12.1 percent to $425.5 million in 2004 from $379.6 million in 2003. Total loan interest income increased by 81.1 percent in 2004 on an annual basis due to the increase in average gross loans outstanding and the increase in average yield on loans from 5.78 percent in 2003 to 6.04 percent in 2004. The average interest rate charged on loans increased 26 basis points, reflecting the average WSJ Prime Rate increase of 22 basis points from 4.12 percent in 2003 to 4.34 percent in 2004. The yield on average interest-earning assets increased from 5.03 percent in 2003 to 5.63 percent in 2004, an increase of 60 basis points, reflecting a shift in the mix of interest-earning assets from 72.3 percent loans, 24.9 percent securities and 2.8 percent other interest-earning assets in 2003 to 81.0 percent loans, 17.8 percent securities and 1.2 percent other interest-earning assets in 2004.

The majority of interest-earning assets growth was funded by a $713.2 million, or 50.3 percent, increase in average total deposits. Total average interest-bearing liabilities grew by 59.6 percent to $1,687.7 million in 2004 compared to $1,057.2 million in 2003. The average interest rate paid for interest-bearing liabilities decreased by four basis points from 1.97 percent in 2003 to 1.93 percent in 2004. As a result of the increases in the yield on interest-earning assets and cost of interest-bearing liabilities, the net interest spread increased to 3.74 percent in 2004 compared to 3.09 percent in 2003.

The following tables show 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.

	For the Year Ended December 31,								
	2005			2004			2003		
(Dollars in Thousands)	Average Balance	Interest Income / Expense	Average Yield / Rate	Average Balance	Interest Income / Expense	Average Yield / Rate	Average Balance	Interest Income / Expense	Average Yield / Rate
Assets									
Interest-earning assets:									
Gross loans, net [1]	$ 2,382,230	$ 179,011	7.51%	$ 1,933,761	$ 116,811	6.04%	$ 1,116,952	$ 64,505	5.78%
Municipal securities [2]	74,166	3,122	6.48%	70,372	3,015	6.59%	33,596	1,421	6.97%
Obligations of other U.S. Government agencies	102,703	4,002	3.90%	90,336	3,374	3.73%	70,465	2,395	3.40%
Other debt securities	241,881	10,271	4.25%	264,829	10,261	3.87%	275,574	8,321	3.02%
Equity securities	23,571	1,107	4.70%	15,041	716	4.76%	6,003	273	4.55%
Federal funds sold	46,799	1,589	3.40%	12,772	183	1.43%	21,844	277	1.27%
Term Federal funds sold	—	—	—	—	—	—	14,370	225	1.57%
Interest-earning deposits	214	5	2.34%	301	6	1.99%	16	—	—
Total interest-earning assets	2,871,564	199,107	6.93%	2,387,412	134,366	5.63%	1,538,820	77,417	5.03%
Non-interest-earning assets:									
Cash and cash equivalents	92,245			76,064			52,067		
Allowance for loan losses	(22,791)			(21,227)			(13,187)		
Other assets	308,172			228,452			45,514		
Total non-interest-earning assets	377,626			283,289			84,394		
Total assets	$ 3,249,190			$ 2,670,701			$ 1,623,214		
Liabilities and Shareholders' Equity									
Interest-bearing liabilities:									
Deposits:									
Money market checking	$ 539,678	12,964	2.40%	$ 466,880	8,098	1.73%	$ 207,689	2,584	1.24%
Savings	138,167	2,130	1.54%	131,589	1,790	1.36%	97,070	1,894	1.95%
Time deposits of $100,000 or more	959,904	31,984	3.33%	611,555	10,966	1.79%	386,701	7,415	1.92%
Other time deposits	242,996	7,114	2.93%	253,884	5,414	2.13%	302,651	7,354	2.43%
Other borrowed funds	165,482	7,919	4.79%	223,780	6,349	2.84%	63,138	1,549	2.45%
Total interest-bearing liabilities	2,046,227	62,111	3.04%	1,687,688	32,617	1.93%	1,057,249	20,796	1.97%
Non-interest-bearing liabilities:									
Demand deposits	751,509			665,816			422,453		
Other liabilities	33,641			23,884			11,143		
Total non-interest-bearing liabilities	785,150			689,700			433,596		
Total liabilities	2,831,377			2,377,388			1,490,845		
Shareholders' equity	417,813			293,313			132,369		
Total liabilities and shareholders' equity	$ 3,249,190			$ 2,670,701			$ 1,623,214		
Net interest income		$ 136,996			$ 101,749			$ 56,621	
Net interest spread [3]			3.89%			3.70%			3.06%
Net interest margin [4]			4.77%			4.26%			3.68%

(1) Loans are net of deferred fees and related direct costs. Loan fees have been included in the calculation of interest income. Loan fees were $5.6 million, $6.0 million and $3.2 million for the years ended December 31, 2005, 2004 and 2003, respectively.

(2) Yields on tax-exempt income have been computed on a tax-equivalent basis, using a tax rate of 35 percent.

(3) Represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.

(4) Represents net interest income as a percentage of average interest-earning assets.

The following table sets forth, for the periods indicated, the dollar amount of changes in interest earned and paid for interest-earning assets and interest-bearing liabilities and the amount of change attributable to changes in average daily balances (volume) or changes in average daily interest rates (rate). The variances attributable to both the volume and rate changes have been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amount of the changes in each:

	For the Year Ended December 31,					
	2005 vs. 2004			2004 vs. 2003		
	Increases (Decreases) Due to Change in			Increases (Decreases) Due to Change in		
(In Thousands)	Volume	Rate	Total	Volume	Rate	Total
Interest Income:						
Gross loans, net	$ 30,311	$ 31,889	$ 62,200	$ 49,212	$ 3,094	$ 52,306
Municipal securities	161	(54)	107	1,576	18	1,594
Obligations of other U.S. Government agencies	477	151	628	725	254	979
Other debt securities	(929)	939	10	(335)	2,275	1,940
Equity securities	401	(10)	391	429	14	443
Federal funds sold	930	476	1,406	(126)	32	(94)
Term Federal funds sold	–	–	–	(112)	(113)	(225)
Interest-earning deposits	(2)	1	(1)	6	–	6
Total interest income	31,349	33,392	64,741	51,375	5,574	56,949
Interest Expense:						
Money market checking	1,403	3,463	4,866	4,191	1,323	5,514
Savings	92	248	340	564	(668)	(104)
Time deposits of $100,000 or more	8,385	12,633	21,018	4,060	(509)	3,551
Other time deposits	(241)	1,941	1,700	(1,103)	(837)	(1,940)
Other borrowed funds	(1,966)	3,536	1,570	4,522	278	4,800
Total interest expense	7,673	21,821	29,494	12,234	(413)	11,821
Change in net interest income	$ 23,676	$ 11,571	$ 35,247	$ 39,141	$ 5,987	$ 45,128

Provision for Credit Losses

For the year ended December 31, 2005, the provision for credit losses was $5.4 million, compared to $2.9 million for the year ended December 31, 2004, an increase of 85.6 percent. The allowance for loan losses remained at 1.00 percent of total gross loans at December 31, 2005 and 2004, with the increase in the dollar amount allowed for credit losses due to an increase in loan volume. This was primarily due to the overall decrease in historical loss factors on pass grade loans, while non-performing assets increased from $6.1 million, or 0.27 percent of gross loans, to $10.1 million, or 0.41% of gross loans, as of December 31, 2004. The $235.2 million, or 10.4 percent, increase in the loan portfolio and the $4.1 million, or 68.5 percent, increase in non-performing assets required the provision to increase to $5.4 million in 2005 from $2.9 million in 2004 to maintain the necessary allowance level. Since 2001, we have refined our credit management process and instituted a more comprehensive risk rating system. For the year ended December 31, 2004, the provision for credit losses was $2.9 million, compared to $5.7 million for the year ended December 31, 2003, a decrease of 48.8 percent.

Non-Interest Income

The following table sets forth the various components of non-interest income for the years indicated:

	For the Year Ended December 31,		
(In Thousands)	2005	2004	2003
Service charges on deposit accounts	$ 15,782	$ 14,441	$ 10,339
Trade finance fees	4,269	4,044	2,887
Remittance fees	2,122	1,653	952
Other service charges and fees	2,496	1,486	1,219
Bank-owned life insurance income	845	731	499
Increase in fair value of derivatives	1,105	232	35
Other income	2,459	1,681	840
Gain on sales of loans	3,021	2,997	2,157
Gain on sales of securities available for sale	117	134	1,094
Total non-interest income	$ 32,216	$ 27,399	$ 20,022

We earn non-interest income from three major sources: service charges on deposit accounts, fees generated from international trade finance and gain on sales of loans. Non-interest income has become a significant part of revenue in the past several years. For the year ended December 31, 2005, non-interest income was $32.2 million, an increase of 17.6 percent from $27.4 million for the year ended December 31, 2004. The increase was primarily a result of the merger with PUB and expansion in the Bank's loan and deposit portfolios.

Service charges on deposit accounts increased $1.3 million, or 9.3 percent, in 2005 compared to 2004 and increased $4.1 million, or 39.7 percent, in 2004 compared to 2003. Service charge income on deposit accounts increased with the higher deposit volume and number of accounts as a result of the PUB merger and expansion in the Bank's deposit portfolio. Average demand deposits increased by 12.9 percent to $751.5 million in 2005 from $665.8 million in 2004 and increased by 57.6 percent to $665.8 million in 2004 from $422.5 million in 2003. Service charges are constantly reviewed to maximize service charge income while still maintaining a competitive position.

Fees generated from international trade finance increased by 5.6 percent from $4.0 million in 2004 to $4.3 million in 2005 and increased 40.1 percent from $2.9 million in 2003 to $4.0 million in 2004. The increase was primarily due to the PUB merger. Trade finance fees relate primarily to import and export letters of credit.

Remittance fees increased 28.4 percent and 73.6 percent in 2005 and 2004, respectively, to $2.1 million in 2005 from $1.7 million in 2004 and $952,000 in 2003. The 2005 increase reflects increased volume derived from Hanmi Bank's close relationship with Korea Exchange Bank, a stockholder of Hanmi Financial, and the 2004 increase reflects increased volume resulting from the merger with PUB.

Other charges and fees increased $1.0 million, or 68.0 percent, in 2005, from $1.5 million in the prior year to $2.5 million, and increased $270,000, or 22.2 percent, in 2004, from $1.2 million in the prior year to $1.5 million. The increase in 2005 was caused by higher loan prepayment fees as prepayment activity increased in response to increasing interest rates and the flat yield curve environment. The increase in 2004 was caused primarily by increased activity associated with the merger with PUB.

The changes in the fair value of derivatives are caused primarily by movements in the indexes to which interest rates on certain certificates of deposit are tied. In 2005 and 2004, the Bank offered certificates of deposit tied to either of the Standard & Poor's 500 Index and a basket of Asian currencies. As explained in "Notes to Consolidated Financial Statements, Note 15 – Derivatives," the Bank entered into swap transactions to hedge the market risk associated with such certificates of deposit. The swaps and the related derivatives embedded in the certificates of deposit are accounted for at fair value. The increase in the fair value of the swaps of $1.1 million and $232,000 recorded in non-interest income in 2005 and 2004, respectively, are partially offset by changes in the fair value of the embedded derivatives recorded in non-interest expenses.

Other income increased $778,000, or 46.3 percent, to $2.5 million in 2005 from $1.7 million in 2004, compared to an increase of $841,000, or 100.1 percent, to $1.7 million in 2004 from $840,000 in 2003. The increase in other income over these years is mainly due to an increase in sales commissions from mutual funds and insurance products and, in 2004, an increase in credit card fee income. As a part of our continuing effort to expand non-interest income, we introduced non-depository products, such as life insurance, mutual funds and annuities, to customers in December 2001. During 2005, we generated income of $749,000 from this activity, which represented a 61.4 percent increase from $464,000 earned in 2004.

Gain on sales of loans was $3.0 million in 2005, compared to $3.0 million and $2.2 million in 2004 and 2003, respectively, representing increases of 0.8 percent and 38.9 percent for the years ended December 31, 2005 and 2004, respectively. The increase in gain on sales of loans resulted from increased sales activity in SBA loans, which was primarily due to the acquisition of PUB. The guaranteed portion of a substantial percentage of SBA loans is sold in the secondary markets, and servicing rights are retained. During 2005, there were $50.6 million of SBA loans sold, compared to $51.3 million in 2004 and $32.9 in 2003. The lower premiums earned in 2005 reflect a greater use of brokers to refer loan applications, which causes a higher cost to originate loans, compared to retail originations through the branch network.

Gain on sales of securities available for sale decreased by 87.8 percent from $1.1 million in 2003 to $134,000 in 2004. Gain on sales of securities was $117,000 in 2005. In 2003, we sold $45.1 million of securities, recognizing premiums of 2.43 percent over their carrying value. In 2004, we sold $53.1 million of securities, primarily securities from PUB's portfolio, in order to reposition the balance sheet. Securities sales activity was limited to $11.4 million in 2005, and gains on sales of securities were nominal in amount in 2004 and 2005.

Non-Interest Expenses

The following table sets forth the breakdown of non-interest expenses for the years indicated:

	For the Year Ended December 31,		
(In Thousands)	2005	2004	2003
Salaries and employee benefits	$ 36,839	$ 33,540	$ 21,214
Occupancy and equipment	8,978	8,098	5,198
Data processing	4,844	4,540	3,080
Advertising and promotion	2,913	3,001	1,635
Supplies and communications	2,556	2,433	1,496
Professional fees	2,201	2,068	1,167
Amortization of core deposit intangible	2,785	1,872	121
Decrease in fair value of embedded option	748	–	–
Other operating expense	7,778	8,961	5,414
Merger-related expenses	(509)	2,053	–
Total non-interest expenses	$ 69,133	$ 66,566	$ 39,325

For the year ended December 31, 2005, non-interest expenses were $69.1 million, an increase of $2.6 million, or 3.9 percent, from $66.6 million for the year ended December 31, 2004. For the year ended December 31, 2004, non-interest expenses were $66.6 million, an increase of $27.2 million, or 69.3 percent, from $39.3 million for the year ended December 31, 2003. The increases in both years were primarily due to the PUB merger, which closed on April 30, 2004.

Salaries and employee benefits expenses for 2005 increased $3.3 million, or 9.8 percent, to $36.8 million from $33.5 million for 2004 and, for 2004, increased $12.3 million, or 58.1 percent, to $33.5 million from $21.2 million for 2003. These increases were due primarily to increases in the average number of employees following the acquisition of PUB. Average headcount was 535 and 503 in 2005 and 2004, respectively, representing increases of 6.4 percent and 36.5 percent, respectively, over the prior years. Assets per employee were $6.2 million at December 31, 2005, compared to $5.8 million at December 31, 2004, an increase of 6.2 percent, which reflects the greater operating efficiencies achieved following the merger with PUB.

Occupancy and equipment expenses for 2005 increased $880,000, or 10.9 percent, to $9.0 million compared to $8.1 million for 2004 and, for 2004, increased $2.9 million, or 55.8 percent, to $8.1 million compared to $5.2 million for 2003. These increases were mainly due to the acquisition of twelve former PUB branches in April 2004, which increased the branch network to 27 facilities. Following the closure of four branches in October 2004 and an additional branch closure in January 2005, the Bank now operates 22 branches, the same as the average number of branches for the year ended December 31, 2004.

Data processing expense for 2005 increased $304,000, or 6.7 percent, to $4.8 million from $4.5 million for 2004 as a result of a 12.9 percent increase in average demand deposits, a 28.5 percent increase in average deposits, and a 23.2 percent increase in average loans outstanding. Data processing expense for 2004 increased $1.5 million, or 47.4 percent, to $4.5 million from $3.1 million for 2003. In 2004, average demand deposits increased 57.6 percent, average deposits increased 47.3 percent, and average loans outstanding increased 73.1 percent compared to 2003. In 2004, additional expense was incurred because of the need to operate parallel systems until the conversion of the Bank's core data processing systems.

Advertising and promotion expense decreased from $3.0 million for 2004 to $2.9 million for 2005, a decrease of $88,000, or 2.9 percent. In 2004, Hanmi Bank conducted print, radio and television campaigns and distributed various promotional items to publicize its merger with PUB and attract and retain customers, and advertising and promotion expense increased $1.4 million, or 83.5 percent, to $3.0 million from $1.6 million in 2003.

Supplies and communication expenses increased $123,000, or 5.1 percent, to $2.6 million in 2005 from $2.4 million in 2004. Supplies and communication expenses increased $937,000, or 62.6 percent, to $2.4 million in 2004 from $1.5 million in 2003 because of the merger with PUB.

Professional fees were $2.2 million in 2005, representing an increase of $133,000, or 6.4 percent, compared to $2.1 million in 2004. The increase was caused primarily by increased regulatory compliance consulting fees. Professional fees were $2.1 million in 2004, representing an increase of $901,000, or 62.6 percent, compared to $1.2 million for 2003. The increase was caused primarily by consulting fees related to the integration with PUB and data processing system conversions.

Core deposit premium amortization increased to $2.8 million in 2005 compared to $1.9 million in 2004 and $121,000 in 2003. The increase is attributable to the acquisition of PUB.

Other operating expenses were $7.8 million for 2005, compared to $9.0 million for 2004, representing a decrease of $1.2 million, or 13.2 percent. The decreases are primarily attributable to a $1.2 million decrease in loan referral fees from 2004 to 2005. Other operating expenses were $9.0 million for 2004, compared to $5.4 million for 2003, representing an increase of $3.5 million, or 65.5 percent. The increases are primarily attributable to additional operating expenses associated with the acquisition of PUB.

During the year ended December 31, 2004, restructuring charges totaling $2.1 million were recorded in connection with the acquisition of PUB, consisting of employee severance and retention bonuses, leasehold termination costs, and fixed asset impairment charges associated with planned branch closures. In 2004, $975,000 of restructuring costs was recognized related to retention bonuses paid to former PUB employees. Such costs are treated as period costs and are recognized in the period services are rendered. In 2005, $509,000 of restructuring charges was reversed, as severance payments were lower than anticipated.

Income Taxes

For the year ended December 31, 2005, income taxes of $36.5 million were recognized on pre-tax income of $94.7 million, representing an effective tax rate of 38.5 percent, compared to income taxes of $23.0 million recognized on pre-tax income of $59.7 million, representing an effective tax rate of 38.5 percent, for 2004, and income taxes of $12.4 million recognized on pre-tax income of $31.6 million, representing an effective tax rate of 39.3 percent, for 2003.

We have made investments in various tax credit funds totaling $6.9 million as of December 31, 2005 and recognized $673,000 of income tax credits earned from qualified low-income housing investments in 2005. We recognized an income tax credit of $723,000 for the tax year 2004 from $5.3 million in such investments. We intend to continue to make such investments as part of an effort to lower the effective tax rate and to meet our community reinvestment obligations under the CRA.

As indicated in "Notes to Consolidated Financial Statements, Note 10 – Income Taxes," income taxes are the sum of two components: current tax expense and deferred tax expense (benefit). Current tax expense is the result of applying the current tax rate to taxable income. The deferred portion is intended to account for the fact that income on which taxes are paid differs from financial statement pretax income because certain items of income and expense are recognized in different years for income tax purposes than in the financial statements. These differences in the years that income and expenses are recognized cause "temporary differences."

Most of our temporary differences involve recognizing more expenses in our financial statements than we have been allowed to deduct for taxes, and therefore we normally have a net deferred tax asset. At December 31, 2005, we had net deferred tax assets of $9.7 million.

Financial Condition

Loan Portfolio

Total gross loans increased by $235.2 million, or 10.4 percent, in 2005. Total gross loans represented 73.2 percent of total assets at December 31, 2005 compared with 72.9 percent and 70.8 percent at December 31, 2004 and 2003, respectively.

Commercial and industrial loans were $1,431.5 million and $1,218.3 million at December 31, 2005 and 2004, respectively, representing 57.3 percent and 53.8 percent, respectively, of the total loan portfolio. Commercial loans include term loans and revolving lines of credit. Term loans typically have a maturity of three to five years and are extended to finance the purchase of business entities, owner-occupied commercial property, business equipment, leasehold improvements or for permanent working capital. SBA guaranteed loans usually have a longer maturity (5 to 20 years). Lines of credit, in general, are extended on an annual basis to businesses that need temporary working capital and/or import/export financing. These borrowers are well diversified as to industry, location and their current and target markets. We manage the portfolio to avoid concentration in any of the areas mentioned.

Real estate loans were $974.2 million and $956.8 million at December 31, 2005 and 2004, respectively, representing 39.0 percent and 42.3 percent, respectively, of the total loan portfolio. Real estate loans are extended to finance the purchase and/or improvement of commercial real estate and residential property. The properties generally are investor-owned, but may be for user-owned purposes. Underwriting guidelines include, among other things, review of appraised value, limitations on loan-to-value ratios, and minimum cash flow requirements to service debt. The majority of the properties taken as collateral are located in Southern California.

Overall, loan production increased 32.2 percent in 2005 compared to 2004, as the Bank's customer base continued to expand and collateral values continued to increase, although at a slower pace than in past years. However, loan portfolio growth was restricted by a high level of loan payoffs caused by the flat yield curve that obtained throughout much of 2005 and aggressive pricing of five- to seven-year fixed-rate commercial real estate loans by certain competitors, which eroded the Bank's portfolio of commercial real estate loans tied to the prime rate.

The shift in the mix of the loan portfolio in 2005 reflects management's intent to emphasize commercial and industrial lending, while continuing to grow the commercial real estate portfolio at a prudent pace commensurate with the Bank's rigorous underwriting standards and asset/liability management and profitability objectives.

The following table sets forth the amount of total loans outstanding in each category as of the dates indicated:

	Amount Outstanding as of December 31,				
(In Thousands)	2005	2004	2003	2002	2001
Real Estate Loans:					
Commercial property	$ 733,650	$ 783,539	$ 397,853	$ 284,465	$ 198,529
Construction	152,080	92,521	43,047	39,237	33,618
Residential property [1]	88,442	80,786	58,477	47,891	49,333
Total real estate loans	974,172	956,846	499,377	371,593	281,480
Commercial and Industrial Loans:					
Commercial term loans	945,210	754,108	433,398	346,522	280,057
Commercial lines of credit	224,271	201,940	120,856	117,304	98,304
SBA loans [2]	155,491	166,285	91,717	66,443	60,053
International loans	106,520	95,936	65,040	42,641	34,506
Total commercial and industrial loans	1,431,492	1,218,269	711,011	572,910	472,920
Consumer Loans	92,154	87,526	54,878	44,416	38,645
Total gross loans	$ 2,497,818	$ 2,262,641	$ 1,265,266	$ 988,919	$ 793,045

(1) As of December 31, 2005, loans held for sale totaling $1.1 million were included at the lower of cost or market.

(2) As of December 31, 2004, loans held for sale totaling $3.9 million were included at the lower of cost or market.

The following table sets forth the percentage distribution of loans in each category as of the dates indicated:

	Percentage Distribution of Loans as of December 31,				
	2005	2004	2003	2002	2001
Real Estate Loans:					
Commercial property	29.37%	34.63%	31.44%	28.77%	25.03%
Construction	6.09%	4.09%	3.40%	3.97%	4.24%
Residential property	3.54%	3.57%	4.63%	4.84%	6.22%
Total real estate loans	39.00%	42.29%	39.47%	37.58%	35.49%
Commercial and Industrial Loans:					
Commercial term loans	37.84%	33.33%	34.25%	35.04%	35.31%
Commercial lines of credit	8.98%	8.92%	9.55%	11.86%	12.40%
SBA loans	6.23%	7.35%	7.25%	6.72%	7.57%
International loans	4.26%	4.24%	5.14%	4.31%	4.35%
Total commercial and industrial loans	57.31%	53.84%	56.19%	57.93%	59.63%
Consumer Loans	3.69%	3.87%	4.34%	4.49%	4.88%
Total gross loans	100.00%	100.00%	100.00%	100.00%	100.00%

The following table shows the distribution of undisbursed loan commitments as of the dates indicated:

	December 31,	
(In Thousands)	2005	2004
Commitments to extend credit	$ 555,736	$ 367,708
Commercial letters of credit	58,036	49,699
Standby letters of credit	42,768	47,901
Unused credit card lines	14,892	14,324
Total undisbursed loan commitments	$ 671,432	$ 479,632

The table below shows the maturity distribution and repricing intervals of outstanding loans as of December 31, 2005. In addition, the table shows the distribution of such loans between those with variable or floating interest rates and those with fixed or predetermined interest rates. The table includes non-accrual loans of $10.1 million.

(In Thousands)	*Within One Year*	*After One But Within Five Years*	*After Five Years*	*Total*
Real Estate Loans:				
Commercial property	$ 589,647	$ 67,705	$ 76,298	$ 733,650
Construction	152,080	–	–	152,080
Residential property	36,785	2,195	49,462	88,442
Total real estate loans	778,512	69,900	125,760	974,172
Commercial and Industrial Loans:				
Commercial term loans	825,209	34,764	85,237	945,210
Commercial lines of credit	224,271	–	–	224,271
SBA loans	155,491	–	–	155,491
International loans	106,520	–	–	106,520
Total commercial and industrial loans	1,311,491	34,764	85,237	1,431,492
Consumer Loans	37,291	53,941	922	92,154
Total gross loans	$ 2,127,294	$ 158,605	$ 211,919	$ 2,497,818
Loans with predetermined interest rates	$ 115,215	$ 158,605	$ 200,849	$ 474,669
Loans with variable interest rates	$ 2,012,079	$ –	$ 11,070	$ 2,023,149

As of December 31, 2005, there were $258.3 million of loans outstanding, or 10.34 percent of total gross loans outstanding, to borrowers who were involved in the accommodation/hospitality industry. 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.

Non-performing loans, which made up all non-performing assets, were $10.1 million at December 31, 2005, compared to $6.0 million and $8.7 million at December 31, 2004 and 2003, respectively, representing a 68.5 percent increase in 2005 and a 30.6 percent decrease in 2004. Total gross loans increased by 10.5 percent in 2005 over 2004 and 78.8 percent in 2004 over 2003. As a result, the ratio of non-performing assets to total gross loans increased to 0.41 percent at December 31, 2005 from 0.27 percent at December 31, 2004, and decreased to 0.27 percent at December 31, 2004 from 0.68 percent at December 31, 2003. As of December 31, 2005 and 2004, we had no OREO.

Except for non-performing loans set forth below and loans disclosed as impaired, our management is not aware of any loans as of December 31, 2005 for which known credit problems of the borrower would cause serious doubts as to the ability of such borrowers to comply with their present loan repayment terms, or any known events that would result in the loan being designated as non-performing at some future date. Our management cannot, however, predict the extent to which a deterioration in general economic conditions, real estate values, increases in general rates of interest, or changes in the financial condition or business of borrower may adversely affect a borrower's ability to pay.

The following table provides information with respect to the components of non-performing assets as of December 31 for the years indicated:

(Dollars in Thousands)	2005	2004	2003	2002	2001
Non-Accrual Loans:					
Real estate loans:					
Commercial property	$ —	$ —	$ 527	$ —	$ 1,183
Residential property	474	112	1,126	287	730
Commercial and industrial loans	9,574	5,510	6,398	5,522	2,275
Consumer loans	74	184	53	49	94
Total non-accrual loans	10,122	5,806	8,104	5,858	4,282
Loans 90 Days or More Past Due and Still Accruing (As to Principal or Interest):					
Real estate loans:					
Commercial property	—	—	557	356	602
Residential property	—	—	—	261	117
Commercial and industrial loans	—	169	—	—	—
Consumer loans	9	39	—	—	—
Total loans 90 days or more past due and still accruing (as to principal or interest)	9	208	557	617	719
Total non-performing loans	10,131	6,014	8,661	6,475	5,001
Other real estate owned	—	—	—	—	—
Total non-performing assets	$ 10,131	$ 6,014	$ 8,661	$ 6,475	$ 5,001
Troubled debt restructurings	$ 642	$ 1,227	$ 491	$ —	$ —
Non-performing loans as a percentage of total gross loans	0.41%	0.27%	0.68%	0.65%	0.63%
Non-performing assets as a percentage of total assets	0.30%	0.19%	0.48%	0.44%	0.43%

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

Provisions to the allowance for loan losses are made quarterly to recognize probable loan losses. The quarterly provision is based on the allowance need, which is calculated using a formula designed to provide adequate allowances for anticipated losses. The formula is composed of various components. The allowance is determined by assigning specific allowances for all classified loans. All loans that are not classified are then given certain allocations according to type with larger percentages applied to loans deemed to be of a higher risk. These percentages are determined based on the prior loss history by type of loan, adjusted for current economic factors.

	December 31,									
(Dollars in Thousands)	2005		2004		2003		2002		2001	
Allowance for Loan Losses Applicable To	*Allowance Amount*	*Total Loans*	*Allowance Amount*	*Total Loans*	*Allowance Amount*	*Total Loans*	*Allowance Amount*	*Total Loans*	*Allowance Amount*	*Total Loans*
Real Estate Loans:										
Commercial property	$ 2,043	$ 733,650	$ 1,854	$ 783,539	$ 374	$ 397,853	$ 337	$ 284,465	$ 1,108	$ 198,336
Construction	475	152,080	349	92,521	427	43,047	267	39,237	163	33,618
Residential property [1]	19	87,377	155	80,786	191	58,477	149	47,891	258	49,526
Total real estate loans	2,537	973,107	2,358	956,846	992	499,377	753	371,593	1,529	281,480
Commercial and industrial loans	21,035	1,431,492	19,051	1,214,419	11,376	685,557	9,773	560,370	7,072	457,973
Consumer loans	1,391	92,154	1,293	87,526	846	54,878	652	44,416	738	38,645
Unallocated	—	—	—	—	135	—	76	—	69	—
Total	$ 24,963	$ 2,496,753	$22,702	$ 2,258,791	$ 13,349	$ 1,239,812	$ 11,254	$ 976,379	$ 9,408	$ 778,098

(1) Loans held for sale excluded.

The allowance is based on estimates, and ultimate future losses may vary from current estimates. Underlying trends in the economic cycle, particularly in Southern California, which management cannot completely predict, will influence credit quality. It is always possible that future economic or other factors may adversely affect Hanmi Bank's borrowers. As a result, we may sustain loan losses in any particular period that are sizable in relation to the allowance, or exceed the allowance. In addition, our asset quality may deteriorate through a number of possible factors, including:

- rapid growth;
- failure to maintain or enforce appropriate underwriting standards;
- failure to maintain an adequate number of qualified loan personnel; and
- failure to identify and monitor potential problem loans.

The allowance for loan losses and allowance for off-balance sheet items are maintained at levels that are believed to be adequate by management to absorb estimated probable loan losses inherent in the loan portfolio. The adequacy of the allowance and the reserve 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 others, 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 allowance for loan loss and reserve for credit loss adequacy. 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 (auto, mortgage and credit cards), which are analyzed as homogeneous loan pools. These calculated loss factors are then applied to outstanding loan balances, unused commitments and off-balance sheet exposures, such as letters of credit. 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 allowance assignments are made based on general and specific economic conditions, as well as performance trends within specific portfolio segments and individual concentrations of credit.

The allowance for loan losses was $25.0 million at December 31, 2005, compared to $22.7 million at December 31, 2004. The increase in the allowance for loan losses in 2005 was due primarily to increased specific reserves for impaired loans and an increase in the qualitative adjustments due to changes in the qualitative factors. The ratio of the allowance for loan losses to total gross loans was 1.00 percent at December 31, 2005 and 2004, primarily due to the overall decrease of historical loss factors on pass grade loans. The loan loss estimation, based on historical losses, and specific allocations of the allowance are performed on a quarterly basis. The allowance for off-balance sheet items was $2.1 million at December 31, 2005, compared to $1.8 million at December 31, 2004.

The loan loss estimation, 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- or policy-related issues.

We determine the appropriate overall allowance for loan losses and allowance for off-balance sheet items based on the analysis described above, taking into account management's judgment. The allowance 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 December 31, 2005.

	As of and for the Year Ended December 31,				
(Dollars in Thousands)	*2005*	*2004*	*2003*	*2002*	*2001*
Allowance for Loan Losses:					
Balance at beginning of year	$ 22,702	$ 13,349	$ 11,254	$ 9,408	$ 11,276
Allowance for loan losses – PUB acquisition	–	10,566	–	–	–
Actual charge-offs:					
Real estate loans:					
Commercial property	–	–	198	–	–
Commercial and industrial loans	4,371	5,004	3,687	3,213	3,782
Consumer loans	827	481	538	358	324
Total charge-offs	5,198	5,485	4,423	3,571	4,106
Recoveries on loans previously charged off:					
Real estate loans:					
Commercial property	–	–	21	–	273
Residential property	–	–	6	–	–
Commercial and industrial loans	2,193	1,702	859	871	307
Consumer loans	201	78	322	105	214
Total recoveries	2,394	1,780	1,208	976	794
Net loan charge-offs	2,804	3,705	3,215	2,595	3,312
Provision charged to operating expenses	5,065	2,492	5,310	4,441	1,444
Balance at end of year	$ 24,963	$ 22,702	$ 13,349	$ 11,254	$ 9,408
Allowance for Off-Balance Sheet Items:					
Balance at beginning of year	$ 1,800	$ 1,385	$ 1,015	$ 656	$ 700
Provision charged to operating expenses	330	415	370	359	(44)
Balance at end of year	$ 2,130	$ 1,800	$ 1,385	$ 1,015	$ 656
Ratios:					
Net loan charge-offs to average total gross loans	0.12%	0.19%	0.29%	0.29%	0.46%
Net loan charge-offs to total gross loans at end of period	0.11%	0.16%	0.25%	0.26%	0.42%
Allowance for loan losses to average total gross loans	1.05%	1.17%	1.19%	1.26%	1.32%
Allowance for loan losses to total gross loans at end of period	1.00%	1.00%	1.06%	1.14%	1.19%
Net loan charge-offs to allowance for loan losses	11.23%	16.32%	24.08%	23.06%	35.20%
Net loan charge-offs to provision charged to operating expenses	55.36%	148.68%	60.55%	58.43%	229.36%
Allowance for loan losses to non-performing loans	246.40%	377.55%	154.13%	173.81%	188.12%
Balances:					
Average total gross loans outstanding during period	$ 2,382,230	$ 1,933,761	$ 1,116,952	$ 893,122	$ 713,338
Total gross loans outstanding at end of period	$ 2,497,818	$ 2,262,641	$ 1,265,266	$ 988,919	$ 793,045
Non-performing loans at end of period	$ 10,131	$ 6,014	$ 8,661	$ 6,475	$ 5,001

We concentrate the majority of our 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 that are classified special mention and worse. In addition to our internal grading system, loans criticized by this credit review are downgraded with appropriate allowance added if required.

As indicated above, we formally assess the adequacy of the allowance on a quarterly basis by:

- reviewing the adversely graded, delinquent or otherwise questionable loans;
- generating an estimate of the loss potential in each such loan;
- adding a risk factor for industry, economic or other external factors; and
- evaluating the present status of each loan.

Although management believes the allowance is adequate to absorb probable losses, 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.

Investment Portfolio

As of December 31, 2005, the investment portfolio was composed primarily of mortgage-backed securities, U.S. Government agency securities ("Agencies"), collateralized mortgage obligations, municipal bonds and corporate bonds.

Investment securities available for sale were 99.8 percent and 99.7 percent of the total investment portfolio as of December 31, 2005 and 2004, respectively. Most of the securities held by us carried fixed interest rates. Other than holdings of Agencies, there were no investments in securities of any one issuer exceeding 10 percent of shareholders' equity as of December 31, 2005, 2004 or 2003.

We maintain an investment portfolio primarily for liquidity purposes. As of December 31, 2005, the investment portfolio balance was $446.7 million, or 13.1 percent of total assets, compared to $415.8 million, or 13.4 percent of total assets as of December 31, 2004. During 2005, we purchased $132.7 million of securities, primarily mortgage-backed and Agencies, to replenish the portfolio for principal repayments in the form of calls, prepayments and scheduled amortization and to maintain an asset mix consistent with our strategic direction.

The following table summarizes the amortized cost, fair value and distribution of investment securities as of the dates indicated:

Investment Portfolio as of December 31,

(In Thousands)	2005 Amortized Cost	2005 Fair Value	2004 Amortized Cost	2004 Fair Value	2003 Amortized Cost	2003 Fair Value
Held to Maturity:						
Municipal bonds	$ 692	$ 692	$ 691	$ 691	$ 690	$ 689
Mortgage-backed securities	357	359	399	402	638	645
Total held to maturity	$ 1,049	$ 1,051	$ 1,090	$ 1,093	$ 1,328	$ 1,334
Available for Sale:						
Mortgage-backed securities	$ 149,311	$ 147,268	$ 148,706	$ 149,174	$ 117,139	$ 117,484
U.S. Government agency securities	129,589	127,813	89,345	89,677	80,845	81,426
Collateralized mortgage obligations	83,068	81,456	93,172	92,539	125,491	124,096
Municipal bonds	71,536	73,220	71,771	73,616	60,741	61,403
Corporate bonds	8,235	8,053	8,380	8,444	13,641	13,903
Other securities	4,999	5,053	4,437	4,433	15,055	14,976
Total available for sale	$ 446,738	$ 442,863	$ 415,811	$ 417,883	$ 412,912	$ 413,288

The following table summarizes the maturity and/or repricing schedule for investment securities and their weighted-average yield as of December 31, 2005:

	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years	
(Dollars in Thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Mortgage-backed securities (1)	$ 55,507	3.94%	$ 45,238	4.56%	$ 41,224	4.73%	$ 5,656	5.15%
U.S. Government agency securities	14,882	3.20%	112,931	4.32%	–	–	–	–
Collateralized mortgage obligations (1)	15,915	3.70%	57,895	4.25%	7,646	4.64%	–	–
Municipal bonds (2)	270	7.82%	1,408	4.94%	8,089	6.19%	64,145	6.30%
Corporate bonds	–	–	8,053	4.36%	–	–	–	–
Other securities	5,053	6.51%	–	–	–	–	–	–
	$ 91,627	3.93%	$ 225,525	4.36%	$ 56,959	4.93%	$ 69,801	6.21%

(1) Mortgage-backed securities and collateralized mortgage obligations have contractual maturities through 2035. The above table is based on the expected prepayment schedule.

(2) The yield on municipal bonds has been computed on a tax-equivalent basis, using an effective marginal rate of 35 percent.

Deposits

Total deposits at December 31, 2005, 2004 and 2003 were $2,826.1 million, $2,528.8 million and $1,445.8 million, respectively, representing an increase of $297.3 million, or 11.8 percent, in 2005 and $1,083.0 million, or 74.9 percent, in 2004. At December 31, 2005, 2004 and 2003, total time deposits outstanding were $1,439.8 million, $1,031.7 million and $667.8 million, respectively, representing 50.9 percent, 40.8 percent and 46.2 percent, respectively, of total deposits. This growth reflects the shift away from low-yielding accounts that normally occurs as interest rates rise and depositors take advantage of the greater interest rate differentials available in the market.

Demand deposits and money market accounts decreased by $78.5 million, or 5.8 percent, in 2005 and increased by $662.1 million, or 97.2 percent, in 2004. Core deposits (defined as demand, money market and savings deposits) decreased $110.7 million, or 7.4 percent, to $1,386.4 million as of December 31, 2005 from $1,497.1 million as of December 31, 2004, as depositors shifted funds into higher yielding certificates of deposit. At December 31, 2005, non-interest-bearing demand deposits represented 26.1 percent of total deposits compared to 28.9 percent at December 31, 2004.

Average deposits for the years ended December 31, 2005, 2004 and 2003 were $2,632.3 million, $2,129.7 million and $1,416.6 million, respectively. Average deposits grew by 23.6 percent in 2005 and 50.3 percent in 2004.

We accept brokered deposits on a selective basis at prudent interest rates to augment deposit growth. There were $7.4 million and $40.0 million of brokered deposits as of December 31, 2005 and 2004, respectively. We also had $200.0 million of state time deposits over $100,000 with a weighted-average interest rate of 3.87 percent and 2.08 percent as of December 31, 2005 and 2004, respectively.

The table below summarizes the distribution of average deposits and the average rates paid for the periods indicated:

	For the Year Ended December 31,					
	2005		*2004*		*2003*	
(Dollars In Thousands)	*Average Balance*	*Average Rate*	*Average Balance*	*Average Rate*	*Average Balance*	*Average Rate*
Demand, non-interest-bearing	$ 751,509		$ 665,816		$ 422,453	
Money market checking	539,678	2.40%	466,880	1.73%	207,689	1.24%
Savings	138,167	1.54%	131,589	1.36%	97,070	1.95%
Time deposits of $100,000 or more	959,904	3.33%	611,555	1.79%	386,701	1.92%
Other time deposits	242,996	2.93%	253,884	2.13%	302,651	2.43%
Total deposits	$ 2,632,254		$ 2,129,724		$ 1,416,564	

The table below summarizes the maturity of time deposits in denominations of $100,000 or greater at December 31 of the years indicated:

	December 31,		
(Dollars in Thousands)	*2005*	*2004*	*2003*
Three months or less	$ 587,251	$ 378,205	$ 261,274
Over three months through six months	248,338	232,231	57,034
Over six months through twelve months	321,714	131,775	52,815
Over twelve months	4,647	14,369	17,821
	$ 1,161,950	$ 756,580	$ 388,944

Borrowings

Our borrowings mostly take the form of advances from the Federal Home Loan Bank of San Francisco ("FHLB"), overnight Federal funds, and junior subordinated debt associated with trust preferred securities.

At December 31, 2005, advances from the FHLB were $43.5 million, a decrease of $22.8 million, or 34.4 percent, from the December 31, 2004 balance of $66.4 million. In 2005, we used liquidity available from the growth of the portfolio of certificates of deposit to pay down borrowings to the extent it was cost-effective to do so.

During the first half of 2004, we issued two junior subordinated notes bearing interest at three-month London InterBank Offered Rate ("LIBOR") plus 2.90 percent totaling $61.8 million and one junior subordinated note bearing interest at three-month LIBOR plus 2.63 percent totaling $20.6 million. Our outstanding subordinated debentures related to these offerings, the proceeds of which were used to finance the purchase of PUB, totaled $82.4 million at December 31, 2005.

Interest Rate Risk Management

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 market interest rates. The level of interest rate risk can be managed through such means as the changing of gap positions and the volume of fixed-income assets. 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 most recent status of our gap position.

(Dollars In Thousands)	*Less Than Three Months*	*After Three But Within One Year*	*After One Year But Within Five Years*	*After Five Years*	*Non-Interest-Sensitive*	*Total*
Assets						
Cash	$ –	$ –	$ –	$ –	$ 103,477	$ 103,477
Federal funds sold	40,000	–	–	–	–	40,000
Securities purchased under agreements to resell	20,000	–	–	–	–	20,000
FRB and FHLB stock	–	–	–	24,587	–	24,587
Securities:						
Fixed rate	11,238	29,339	225,521	126,762	–	392,860
Floating rate	6,718	–	36,261	8,073	–	51,052
Loans:						
Fixed rate	35,775	41,169	175,691	163,986	–	416,621
Floating rate	1,952,655	13,028	104,878	–	–	2,070,561
Non-accrual	–	–	–	–	10,122	10,122
Deferred loan fees and allowance for loan losses	–	–	–	–	(28,224)	(28,224)
Other assets	–	22,713	–	6,944	283,539	313,196
Total assets	$ 2,066,386	$ 106,249	$ 542,351	$ 330,352	$ 368,914	$ 3,414,252
Liabilities and Shareholders' Equity						
Liabilities						
Deposits:						
Demand deposits	$ 72,459	$ 192,446	$ 407,097	$ 66,616	$ –	$ 738,618
Savings	16,483	39,913	57,453	7,725	–	121,574
Money market checking	70,270	174,274	223,155	58,472	–	526,171
Time deposits:						
Fixed rate	700,402	572,925	17,332	137	–	1,290,796
Floating rate	148,955	–	–	–	–	148,955
Other borrowed funds	2,803	5,000	33,411	5,117	–	46,331
Junior subordinated debentures	82,406	–	–	–	–	82,406
Other liabilities	–	–	–	–	32,624	32,624
Shareholders' equity	–	–	–	–	426,777	426,777
Total liabilities and shareholders' equity	$ 1,093,778	$ 984,558	$ 738,448	$ 138,067	$ 459,401	$ 3,414,252
Repricing gap	$ 972,608	$ (878,309)	$ (196,097)	$ 192,285	$ (90,487)	
Cumulative repricing gap	$ 972,608	$ 94,299	$ (101,798)	$ 90,487	$ –	
Cumulative repricing gap as a percentage of total assets	28.49%	2.76%	(2.98%)	2.65%	–	
Cumulative repricing gap as a percentage of interest-earning assets	32.25%	3.13%	(3.38%)	3.00%	–	

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 December 31, 2005, the cumulative repricing gap as a percentage of interest-earning assets in the less-than-three month period was 32.25 percent. This was a large decrease from the previous year's figure of 46.00 percent. The decrease

was primarily caused by a shift in the mix of the loan portfolio into fixed-rate loans, funded primarily by certificates of deposit, as the mix of the deposits portfolio shifted away from core deposits and the balance of loans linked to the prime rate decreased $48.6 million. The cumulative repricing percentage in the three-to-twelve month period also moved significantly lower, reaching 3.13 percent. 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 (10.30) percent. The floating gap position in the less-than-one year period was 7.00 percent.

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

	Less Than Three Months December 31,		*Less Than Twelve Months December 31,*	
(Dollars in Thousands)	*2005*	*2004*	*2005*	*2004*
Cumulative repricing gap	$ 972,608	$ 1,274,507	$ 94,299	$451,176
Percentage of total assets	28.49%	41.06%	2.76%	14.53%
Percentage of interest-earning assets	32.25%	46.00%	3.13%	16.29%

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.

To supplement traditional gap analysis, we perform simulation modeling to estimate the potential effects of interest rate changes. The following table summarizes one of the stress simulations performed to forecast the impact of changing interest rates on net interest income and the market value of interest-earning assets and interest-bearing liabilities reflected on our balance sheet. This sensitivity analysis is compared to policy limits, which specify the maximum tolerance level for net interest income exposure over a one-year horizon, given the basis point adjustment in interest rates reflected below.

Rate Shock Table

(Dollars in Thousands)	*Percentage Changes*		*Change in Amount*	
Change in Interest Rate	*Net Interest Income*	*Economic Value of Equity*	*Net Interest Income*	*Economic Value of Equity*
200%	14.78%	(8.78%)	$ 22,688	$ (38,522)
100%	7.37%	(4.66%)	$ 11,311	$ (20,438)
(100%)	(7.42%)	5.14%	$ (11,394)	$ 22,565
(200%)	(14.91%)	10.54%	$ (22,896)	$ 46,234

In the above stress simulation, for a 100 basis point decline in interest rates, we may be exposed to a 7.42 percent decline in net interest income and a 5.14 percent increase in the economic value of equity. For a 100 basis point increase in interest rates, net interest income may increase by 7.37 percent, but the economic value of equity may decrease by 4.66 percent. For a 200 basis point increase in interest rates, net interest income may increase by 14.78 percent, but the economic value of equity may decrease by 8.78 percent. For a 200 basis point decrease in interest rates, net interest income may decrease by 14.91 percent, but the economic value of equity may increase by 10.54 percent. All projected changes remained well within internal policy guidelines at December 31, 2005.

The estimated sensitivity does not necessarily represent our forecast and the results may not be indicative of actual change to our net interest income. These estimates are based upon a number of assumptions including: the nature and timing of interest rate levels including yield curve shape, prepayments on loans and securities, pricing strategies on loans and deposits, and replacement of asset and liability cash flows. While the assumptions used are based on current economic and local market conditions, there is no assurance as to the predictive nature of these conditions, including how customer preferences or competitor influences might change.

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 profitability. The Bank's major liquidity on the asset side stems from available cash positions, Federal funds sold and short-term investments categorized as available for sale securities, which can be disposed of without significant capital losses in the ordinary business cycle. Liquidity sources on the liability side come from borrowing capacities, which include Federal funds lines, repurchase agreements, and Federal Home Loan Bank 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. In addition, 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. In 2005, the mix of the deposits portfolio shifted towards time deposits, and strong growth in certificates of deposit offset a decline in core deposits.

	December 31,		
	2005	2004	2003
Liquidity Ratios:			
Short-term investments/ total assets	3%	5%	6%
Core deposits/ total assets	35%	41%	40%
Short-term non-core funding/total assets	42%	33%	45%
Short-term investments/ short-term non-core funding dependence	18%	23%	20%
Net loans/total assets	72%	72%	70%
Investments/deposits	19%	20%	30%
Loans and investments/ deposits	106%	109%	116%
Off-balance sheet items/ total assets	18%	15%	18%

The net loans to total assets ratio remained at 72 percent as of December 31, 2005. Despite fluctuations during the year, net loans grew at approximately the same rate as assets. During the year, the ratio of net loans to total assets generally was in the range of 71 percent to 74 percent. The investments to deposits ratio decreased to 19 percent as of December 31, 2005, while the ratio of loans and investments to deposits decreased to 106 percent. Off-balance sheet items as a percentage of total assets increased at December 31, 2005 to 18 percent from 15 percent at December 31, 2004, and the total amount increased to $671.4 million at December 31, 2005 from $479.6 million at December 31, 2004. The increase was primarily due to a $188.0 million increase in unused loan commitments. During the year, the percentage of off-balance sheet items to total assets generally ranged from 15 percent to 18 percent. The ratios of short-term non-core funding to total assets and short-term investments to short-term non-core funding dependence were 42 percent and 18 percent, respectively, at December 31, 2005, compared to 33 percent and 23 percent, respectively, at December 31, 2004.

Foreign deposit risk deals with dependency on foreign deposits that could adversely affect the Bank's liquidity. These liabilities are assumed to be volatile in accordance with the variability of social, political and environmental conditions in foreign countries. On a quarterly basis, the Bank monitors foreign deposits and Brazilian deposits separately, and exposures to both categories remained well within the Bank's internal guidelines.

There were increases to the lines of credit secured by us to meet our liquidity needs. As of December 31, 2005, we maintained a total of $154.0 million in credit lines. In addition, we maintained eight master repurchase agreements, all of which can furnish liquidity to us in consideration of bond collateral. We also can meet our liquidity needs through borrowings from the FHLB. We are eligible to borrow up of 25 percent of our total assets from the FHLB.

As of December 31, 2005, there were no material commitments for capital expenditures. We raise capital in the form of deposits, borrowings (primarily FHLB advances and junior subordinated debentures) and equity, and expect to continue to rely upon deposits as the primary source of capital.

Off-Balance Sheet Arrangements

For a discussion of off-balance sheet arrangements, see "Item 1. Business – Small Business Administration Guaranteed Loans" and "Item 1. Business – Off-Balance Sheet Commitments" in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

Contractual Obligations

Our contractual obligations as of December 31, 2005 are as follows:

Contractual Obligations (In Thousands)	*Less Than One Year*	*More Than One Year and Less Than Three Years*	*More Than Three Years and Less Than Five Years*	*More Than Five Years*	*Total*
Time deposits	$ 1,422,981	$ 8,067	$ 9,405	$ 237	$ 1,440,690
Long-term debt obligations	5,000	20,000	13,411	87,522	125,933
Operating lease obligations	2,570	4,376	2,415	5,484	14,845
Total contractual obligations	$ 1,430,551	$ 32,443	$ 25,231	$ 93,243	$ 1,581,468

Recently Issued Accounting Standards

In December 2004, the Financial Accounting Standards Board ("FASB") issued a revision to SFAS No. 123R (Revised), "*Share-Based Payment*" ("SFAS No. 123R"). This Statement 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 Statement of Income. This Statement replaces SFAS No. 123, "*Accounting for Stock-Based Compensation*," and supersedes Accounting Principles Board ("APB") Opinion No. 25, "*Accounting for Stock Issued to Employees*." In addition, this Statement amends SFAS No. 95, "*Statement of Cash Flows*," to require that excess tax benefits be reported as a financing cash inflow rather than as a reduction of taxes paid. This Statement is effective for Hanmi Financial as of January 1, 2006. We have elected to use the modified prospective method to adopt SFAS No. 123R.

As a result of the adoption of SFAS No. 123R, we estimate that we will recognize additional compensation expense of approximately $894,000, net of taxes, or $.02 per diluted share, for the full year 2006. Estimated future levels of compensation expense recognized related to stock based awards would be impacted by new awards, modifications to awards, or cancellation of awards after the adoption of SFAS No. 123R.

In February 2006, the FASB issued SFAS No. 155, "*Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and SFAS No. 140*" ("SFAS No. 155"). This Statement:

- permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation;
- clarifies which interest-only strips and principal-only strips are not subject to SFAS No. 133;
- establishes a requirement to evaluate interests in securitized financial assets to identify interests that are free-standing derivatives or hybrid financial instruments that contain an embedded derivative requiring bifurcation;
- clarifies that concentrations of credit risks in the form of subordinations are not embedded derivatives; and
- amends SFAS No. 140 to eliminate the prohibition on a QSPE from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. Early adoption of this statement is allowed. We have not determined the financial impact of the adoption of SFAS No. 155 or whether we will adopt SFAS No. 155 in 2006.

In May 2005, the FASB issued SFAS No. 154, "*Accounting Changes and Error Corrections*." SFAS No. 154 replaces 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. SFAS No. 154 is not expected to have a material impact on our financial position or results of operations.

In March 2004, the FASB issued Emerging Issues Task Force ("EITF") Issue No. 03-1, "*The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*" ("EITF No. 03-1"). This EITF describes a model involving three steps: (1) determine whether an investment is impaired; (2) determine whether the impairment is other-than-temporary; and (3) recognize any impairment loss in earnings. The EITF also requires several additional disclosures for cost-method investments. In September 2004, the FASB approved the deferral of the effective date for EITF No. 03-1 pending reconsideration of implementation guidance relating to debt securities that are impaired solely due to market interest rate fluctuation.

On November 3, 2005, FASB Staff Position ("FSP") FAS Nos. 115-1 and 124-1, "*The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*," was issued. This FSP nullifies certain requirements of EITF No. 03-1 and supersedes EITF Topic No. D-44, "*Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value*." This FSP nullified the requirements of paragraphs 10 to 18 of EITF No. 03-1, carried forward the requirements of paragraphs 8 and 9 of EITF No. 03-1 with respect to cost-method investments, and carried forward the disclosure requirements included in paragraphs 21 and 22 of EITF No. 03-1 and related examples. The guidance in this FSP is applicable to reporting periods beginning after December 15, 2005. Adoption is not expected to have a material impact on our financial position, results of operations or related disclosures.

In December 2003, the American Institute of Certified Public Accountants ("AICPA") released Statement of Position 03-3, "*Accounting for Certain Loans or Debt Securities Acquired in a Transfer*" ("SOP 03-3"). SOP 03-3 addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities acquired in a transfer if those differences are attributable to credit quality. SOP 03-3 is effective for loans acquired in fiscal years beginning after December 15, 2004. Adoption in 2005 did not have a material impact on our financial position or results of operations.

In December 2004, the FASB issued SFAS No. 153, "*Exchange of Non-Monetary Assets, an Amendment of APB Opinion No. 29, 'Accounting for Non-Monetary Transactions'*" ("SFAS No. 153"). SFAS No. 153 is based on the principle that exchange of non-monetary assets should be measured based on the fair market value of the assets exchanged. SFAS No. 153 eliminates the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. SFAS No. 153 is effective for non-monetary asset exchanges in fiscal periods beginning after June 15, 2005. We are currently assessing the provisions of SFAS No. 153 and its impact on our financial position and results of operations.

Quantitative and Qualitative Disclosures About Market Risk

For quantitative and qualitative disclosures regarding market risks in Hanmi Bank's portfolio, see "Management's Discussion and Analysis of Financial Condition and Results of Operations – Interest Rate Risk Management" and "– Liquidity and Capital Resources."

Management's Report on Internal Control Over Financial Reporting

Management of Hanmi Financial Corporation ("Hanmi Financial") is responsible for establishing and maintaining adequate internal control over financial reporting pursuant to the rules and regulations of the Securities and Exchange Commission. Hanmi Financial's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles;
- provide reasonable assurance that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of Hanmi Financial's internal control over financial reporting as of December 31, 2005. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of Hanmi Financial's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2005, Hanmi Financial maintained effective internal control over financial reporting.

KPMG LLP, the independent registered public accounting firm that audited and reported on the consolidated financial statements of Hanmi Financial, has issued a report on management's assessment of Hanmi Financial's internal control over financial reporting as of December 31, 2005. The report expresses unqualified opinions on management's assessment and on the effectiveness of Hanmi Financial's internal control over financial reporting as of December 31, 2005.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Hanmi Financial Corporation:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting included in Item 9A, that Hanmi Financial Corporation and subsidiary (the Company) maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of The Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of Hanmi Financial Corporation and subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of income, changes in shareholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2005, and our report dated March 15, 2006 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

Los Angeles, California
March 15, 2006

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Hanmi Financial Corporation:

We have audited the accompanying consolidated statements of financial condition of Hanmi Financial Corporation and subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of income, changes in shareholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2005. These consolidated financial statements are the responsibility of the Hanmi Financial Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hanmi Financial Corporation and subsidiary as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Hanmi Financial Corporation's internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 15, 2006 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

Los Angeles, California
March 15, 2006

Consolidated Statements of Financial Condition

(Dollars in Thousands)	*December 31,* 2005	2004
Assets		
Cash and due from banks	$ 103,477	$ 55,164
Federal funds sold and securities purchased under agreements to resell	60,000	72,000
Cash and cash equivalents	163,477	127,164
Federal Reserve Bank stock	12,350	12,099
Federal Home Loan Bank stock	12,237	9,862
Securities held to maturity, at amortized cost (fair value: 2005 – $1,051; 2004 – $1,093)	1,049	1,090
Securities available for sale, at fair value	442,863	417,883
Loans receivable, net of allowance for loan losses of $24,963 and $22,702 at December 31, 2005 and 2004, respectively	2,468,015	2,230,992
Loans held for sale, at the lower of cost or fair value	1,065	3,850
Customers' liability on acceptances	8,432	4,579
Premises and equipment, net	20,784	19,691
Accrued interest receivable	14,120	10,029
Deferred income taxes	9,651	5,009
Servicing asset	3,910	3,846
Goodwill	209,058	209,643
Core deposit intangible	8,691	11,476
Bank-owned life insurance	22,713	21,868
Other assets	15,837	15,107
Total assets	$ 3,414,252	$ 3,104,188
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits:		
Non-interest-bearing	$ 738,618	$ 729,583
Interest-bearing:		
Savings	121,574	153,862
Money market checking	526,171	613,662
Time deposits of $100,000 or more	1,161,950	756,580
Other time deposits	277,801	275,120
Total deposits	2,826,114	2,528,807
Accrued interest payable	11,911	7,100
Acceptances outstanding	8,432	4,579
Other borrowed funds	46,331	69,293
Junior subordinated debentures	82,406	82,406
Other liabilities	12,281	12,093
Total liabilities	2,987,475	2,704,278
Commitments and contingencies (Notes 16 and 17)		
Shareholders' equity:		
Common stock, $.001 par value; authorized 200,000,000 shares; 49,821,798 shares and 49,330,704 shares issued at December 31, 2005 and 2004, respectively	50	49
Additional paid-in capital	339,991	334,932
Unearned compensation	(1,150)	–
Accumulated other comprehensive income (loss) – unrealized gain (loss) on securities available for sale, interest-only strips and interest rate swaps, net of income taxes of ($1,671) and $744 at December 31, 2005 and 2004, respectively	(4,383)	1,035
Retained earnings	112,310	63,894
	446,818	399,910
Less treasury stock, at cost; 1,163,000 shares and 0 shares at December 31, 2005 and 2004, respectively	(20,041)	–
Total shareholders' equity	426,777	399,910
Total liabilities and shareholders' equity	$ 3,414,252	$ 3,104,188

See accompanying notes to consolidated financial statements

Consolidated Statements of Income

(Dollars in Thousands, Except Per Share Data)	*Years Ended December 31,* 2005	2004	2003
Interest Income:			
Interest and fees on loans	$ 179,011	$ 116,811	$ 64,505
Interest on investments	18,507	17,372	12,410
Interest on term Federal funds sold	—	—	225
Interest on Federal funds sold	1,589	183	277
Total interest income	199,107	134,366	77,417
Interest Expense:			
Interest on deposits	54,192	26,268	19,247
Interest on borrowings	7,919	6,349	1,549
Total interest expense	62,111	32,617	20,796
Net interest income before provision for credit losses	136,996	101,749	56,621
Provision for credit losses	5,395	2,907	5,680
Net interest income after provision for credit losses	131,601	98,842	50,941
Non-Interest Income:			
Service charges on deposit accounts	15,782	14,441	10,339
Trade finance fees	4,269	4,044	2,887
Remittance fees	2,122	1,653	952
Other service charges and fees	2,496	1,486	1,219
Bank-owned life insurance income	845	731	499
Increase in fair value of derivatives	1,105	232	35
Other income	2,459	1,681	840
Gain on sales of loans	3,021	2,997	2,157
Gain on sales of securities available for sale	117	134	1,094
Total non-interest income	32,216	27,399	20,022
Non-Interest Expenses:			
Salaries and employee benefits	36,839	33,540	21,214
Occupancy and equipment	8,978	8,098	5,198
Data processing	4,844	4,540	3,080
Advertising and promotion	2,913	3,001	1,635
Supplies and communication	2,556	2,433	1,496
Professional fees	2,201	2,068	1,167
Amortization of core deposit intangible	2,785	1,872	121
Decrease in fair value of embedded options	748	—	—
Other operating expense	7,778	8,961	5,414
Merger-related expenses	(509)	2,053	—
Total non-interest expenses	69,133	66,566	39,325
Income before income taxes	94,684	59,675	31,638
Income taxes	36,455	22,975	12,425
Net income	$ 58,229	$ 36,700	$ 19,213
Earnings per share:			
Basic	$ 1.18	$ 0.87	$ 0.68
Diluted	$ 1.17	$ 0.84	$ 0.67
Weighted-average shares outstanding:			
Basic	49,174,885	42,268,964	28,092,708
Diluted	49,942,356	43,517,257	28,662,026
Dividends declared per share	$ 0 .20	$ 0.20	$ 0.20

See accompanying notes to consolidated financial statements

Consolidated Statements of Changes in Shareholders' Equity and Comprehensive Income

Years Ended December 31, 2005, 2004 and 2003

	Common Stock – Number of Shares		
(Dollars in Thousands)	*Gross Shares Issued and Outstanding*	*Treasury Shares*	*Net Shares Issued and Outstanding*
Balance – December 31, 2002	27,830,866	–	27,830,866
Stock options exercised	495,954	–	495,954
Cash dividends	–	–	–
Comprehensive income:			
Net income	–	–	–
Change in unrealized gain on securities available for sale, interest-only strips and interest rate swaps, net of tax	–	–	–
Total comprehensive income			
Balance – December 31, 2003	28,326,820	–	28,326,820
Stock options exercised	670,576	–	670,576
Warrants exercised	20,000	–	20,000
Stock issued through private placement	7,894,654	–	7,894,654
Stock issued in PUB acquisition	12,418,654	–	12,418,654
Cash dividends	–	–	–
Comprehensive income:			
Net income	–	–	–
Change in unrealized gain on securities available for sale, interest-only strips and interest rate swaps, net of tax	–	–	–
Total comprehensive income			
Balance – December 31, 2004	49,330,704	–	49,330,704
Stock options exercised	391,094	–	391,094
Restricted stock award	100,000	–	100,000
Amortization of unearned compensation	–	–	–
Tax benefit from exercise of stock options	–	–	–
Stock repurchase	–	(1,163,000)	(1,163,000)
Cash dividends	–	–	–
Comprehensive income:			
Net income	–	–	–
Change in unrealized gain on securities available for sale, interest-only strips and interest rate swaps, net of tax	–	–	–
Total comprehensive income			
Balance – December 31, 2005	49,821,798	(1,163,000)	48,658,798

See accompanying notes to consolidated financial statements

Years Ended December 31, 2005, 2004 and 2003

Shareholders' Equity

Common Stock	*Additional Paid-in Capital*	*Unearned Compensation*	*Accumulated Other Comprehensive Income*	*Retained Earnings*	*Treasury Stock, at Cost*	*Total Shareholders' Equity*
$ 28	$ 99,927	$ —	$ 2,105	$ 22,408	$ —	$ 124,468
—	3,141	—	—	—	—	3,141
—	—	—	—	(5,636)	—	(5,636)
—	—	—	—	19,213	—	19,213
—	—	—	(1,719)	—	—	(1,719)
						17,494
28	103,068	—	386	35,985	—	139,467
1	3,234	—	—	—	—	3,235
—	190	—	—	—	—	190
8	71,702	—	—	—	—	71,710
12	156,738	—	—	—	—	156,750
—	—	—	—	(8,791)	—	(8,791)
—	—	—	—	36,700	—	36,700
—	—	—	649	—	—	649
						37,349
49	334,932	—	1,035	63,894	—	399,910
1	2,515	—	—	—	—	2,516
—	1,815	(1,815)	—	—	—	—
—	—	665	—	—	—	665
—	729	—	—	—		729
—	—	—	—	—	(20,041)	(20,041)
—	—	—	—	(9,813)	—	(9,813)
—	—	—	—	58,229	—	58,229
—	—	—	(5,418)	—	—	(5,418)
						52,811
$ 50	$ 339,991	$ (1,150)	$ (4,383)	$ 112,310	$ (20,041)	$ 426,777

Consolidated Statements of Cash Flows

(In Thousands)	*2005*	*2004*	*2003*
	Years Ended December 31,		
Cash Flows from Operating Activities:			
Net income	$ 58,229	$ 36,700	$ 19,213
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities:			
Depreciation and amortization of premises and equipment	2,704	2,447	1,558
Amortization of premiums and discounts on investments	565	3,246	121
Amortization of core deposit intangible	2,785	1,872	212
Amortization of unearned compensation	665	–	–
Provision for credit losses	5,395	2,907	5,680
Federal Reserve Bank and Federal Home Loan Bank stock dividends	(362)	(497)	(107)
Gain on sales of securities available for sale	(117)	(134)	(1,094)
Increase in fair value of derivatives	(1,105)	(232)	(35)
Decrease in fair value of embedded options	748	–	–
Gain on sales of loans	(3,021)	(2,997)	(2,157)
Gain on sales of other real estate owned	–	–	(82)
Loss on sales of premises and equipment	34	15	67
Tax benefit from exercise of stock options	729	–	–
Deferred tax (benefit) expense	(2,707)	694	(2,069)
Origination of loans held for sale	(61,709)	(53,855)	(45,858)
Proceeds from sales of loans held for sale	67,515	54,311	35,100
Change in:			
(Increase) decrease in accrued interest receivable	(4,091)	155	(1,153)
Increase in cash surrender value of bank-owned life insurance	(845)	(731)	(500)
(Increase) decrease in other assets	(5,347)	7,028	(1,832)
Increase (decrease) in accrued interest payable	4,811	(444)	1,018
Increase (decrease) in other liabilities	4,068	(12,751)	5,506
Net cash and cash equivalents provided by operating activities	68,944	37,734	13,588
Cash Flows from Investing Activities:			
Proceeds from matured term federal funds sold	–	–	30,000
Proceeds from sales of Federal Home Loan Bank Stock	–	5,031	–
Proceeds from matured or called securities available for sale	89,885	120,389	170,346
Proceeds from matured or called securities held to maturity	–	239	6,214
Proceeds from sales of securities available for sale	11,360	53,063	45,051
Proceeds from sales of other real estate owned	–	–	204
Net increase in loans receivable	(242,088)	(120,651)	(265,641)
Purchases of Federal Reserve Bank and Federal Home Loan Bank stock	(2,264)	(9,884)	(5,669)
Purchases of securities available for sale	(132,700)	(22,384)	(358,218)
Purchases of bank-owned life insurance	–	(10,000)	–
Purchases of premises and equipment	(3,831)	(2,049)	(2,031)
Acquisition of Pacific Union Bank, net of cash acquired	–	(63,498)	–
Net cash and cash equivalents used in investing activities	(279,638)	(49,744)	(379,744)

(In Thousands)	2005	2004	2003
	Years Ended December 31,		
Cash Flows from Financing Activities:			
Increase in deposits	297,307	146,273	161,856
Issuance of junior subordinated debentures	–	82,406	–
Proceeds from exercises of stock options	2,516	3,235	3,141
Proceeds from exercises of stock warrants	–	190	–
Stock issued through private placement	–	71,710	–
Cash paid to acquire treasury stock	(20,041)	–	–
Cash dividends paid	(9,813)	(7,740)	(4,220)
(Decrease) increase in other borrowed funds	(22,962)	(219,495)	145,202
Net cash and cash equivalents provided by financing activities	247,007	76,579	305,979
Net increase (decrease) in cash and cash equivalents	36,313	64,569	(60,177)
Cash and cash equivalents – beginning of year	127,164	62,595	122,772
Cash and Cash Equivalents – End of Year	$ 163,477	$ 127,164	$ 62,595
Supplemental Disclosures of Cash Flow Information:			
Interest paid	$ 41,266	$ 29,920	$ 19,778
Income taxes paid	$ 37,650	$ 25,400	$ 9,469
Supplemental Schedule of Non-Cash Investing and Financing Activities:			
Transfer of loans to other real estate owned	$ –	$ –	$ 122
Accrued dividend	$ 2,433	$ 2,467	$ 1,416
Reconciliation of Acquisition of Pacific Union Bank, Net of Cash Acquired:			
Fair value of assets acquired	$ –	$ 1,383,782	$ –
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)	$ –
Acquisition of Pacific Union Bank, net of cash acquired	$ –	$ 63,498	$ –

See accompanying notes to consolidated financial statements

Note 1 – Summary of Significant Accounting Policies

The accounting and reporting policies of Hanmi Financial Corporation and subsidiary conform to accounting principles generally accepted in the United States of America and to prevailing practices within the banking industry. A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

Principles of Consolidation

The consolidated financial statements include the accounts of Hanmi Financial Corporation ("Hanmi Financial", "we" or "us") and our wholly owned subsidiary, Hanmi Bank (the "Bank"), after elimination of all material intercompany transactions and balances.

Hanmi Financial was formed as a holding company of the Bank and registered with the Securities and Exchange Commission under the Securities Act of 1933 on March 17, 2001. Subsequent to our formation, each of the Bank's shares was exchanged for one share of Hanmi Financial with an equal value.

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. The 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. The Bank's full-service offices are located in business areas where many of the businesses are run by immigrants and other minority groups. The 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 our 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 December 31, 2005, the Bank maintained a branch network of 22 locations, serving individuals and small- to medium-sized businesses in Los Angeles and surrounding areas.

Cash and Cash Equivalents

Cash and cash equivalents include cash and due from banks, Federal funds sold and securities purchased under resale agreements, all of which have maturities of less than 90 days.

Federal Reserve Bank Stock

As a member of the Federal Reserve Bank of San Francisco ("FRB"), the Bank is required to maintain stock in the FRB based on a specified ratio relative to our capital. FRB stock is carried at cost and may be sold back to the FRB at its carrying value. Both cash and stock dividends received are reported as dividend income.

Federal Home Loan Bank Stock

As a member of the Federal Home Loan Bank of San Francisco ("FHLB"), the Bank is required to own common stock in the FHLB based upon our balance of residential mortgage loans and outstanding FHLB advances. FHLB stock is carried at cost and may be sold back to the FHLB at its carrying value. Both cash and stock dividends received are reported as dividend income.

Securities

Securities are classified into three categories and accounted for as follows:

1. Securities that we have the positive intent and ability to hold to maturity are classified as "held-to-maturity" and reported at amortized cost;
2. Securities that are bought and held principally for the purpose of selling them in the near future are classified as "trading securities" and reported at fair value. Unrealized gains and losses are recognized in earnings; and
3. Securities not classified as held-to-maturity or trading securities are classified as "available for sale" and reported at fair value. Unrealized gains and losses are reported as a separate component of shareholders' equity as Accumulated Other Comprehensive Income, Net of Income Taxes.

Accreted discounts and amortized premiums on investment securities are included in interest income using the effective interest method over the remaining period to the call date or contractual maturity and, in the case of mortgage-backed securities and securities with call features, adjusted for anticipated prepayments. Unrealized and realized gains or losses related to holding or selling of securities are calculated using the specific-identification method. To the extent there is an impairment of value deemed other than temporary for a security held to maturity or available for sale, a loss is recognized in earnings and a new cost basis established for the security.

We also have a minority investment of 4.99 percent in a non-publicly traded company, Pacific International Bank. The investment is included in Other Assets on the Consolidated Statements of Financial Condition and is carried at cost. As of December 31, 2005 and 2004, the carrying value was $511,000. We monitor the investment for impairment and makes appropriate reductions in carrying value when necessary.

Derivative Instruments

We account for derivatives in accordance with the provisions of SFAS No. 133, "*Accounting for Derivative Instruments and Hedging Activities*" ("SFAS No. 133). Under SFAS No. 133, all derivatives are recognized on the balance sheet at their fair value. On the date the derivative contract is entered into, we designate the derivative as a fair value hedge, a cash flow hedge, a hedge of a net investment in a foreign operation, or a non-hedging derivative. Fair value hedges include hedges of the fair value of a recognized asset or liability and certain foreign

currency hedges. Cash flow hedges include hedges of the variability of cash flows to be received or paid related to a recognized asset or liability and certain foreign currency hedges. Changes in the fair value of derivatives designated as fair value hedges, along with the change in fair value on the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings. Changes in the fair value of derivatives designated as cash flow hedges, to the extent effective as a hedge, are recorded in accumulated other comprehensive income and reclassified into earnings in the period during which the hedged item affects earnings. Changes in the fair value of derivatives used to hedge our net investment in foreign subsidiaries, to the extent effective as a hedge, are recorded in common shareholders' equity as a component of the cumulative translation adjustment account within accumulated other comprehensive income. Changes in the fair value of derivative instruments not designated as hedging instruments and ineffective portions of changes in the fair value of hedging instruments are recognized in other income in the current period.

We formally document all relationships between hedging instruments and hedged items. This documentation includes our risk management objective and strategy for undertaking various hedge transactions, as well as how hedge effectiveness and ineffectiveness will be measured. This process includes linking derivatives to specific assets and liabilities on the balance sheet. We also formally assess, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, we discontinue hedge accounting prospectively.

When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective hedge, the derivative will continue to be carried on the balance sheet at its fair value, with changes in its fair value recognized in current period earnings. For fair value hedges, the formerly hedged asset or liability will no longer be adjusted for changes in fair value and any previously recorded adjustments to the carrying value of the hedged asset or liability will be amortized in the same manner that the hedged item affects income. For cash flow hedges, amounts previously recorded in Accumulated Other Comprehensive Income will be reclassified into income as earnings are impacted by the variability in the cash flows of the hedged item.

If the hedging instrument is terminated early, the derivative is removed from the balance sheet. Accounting for the adjustments to the hedged asset or liability or adjustments to Accumulated Other Comprehensive Income are the same as described above when a derivative no longer qualifies as an effective hedge.

If the hedged asset or liability is sold or extinguished, the derivative will continue to be carried on the balance sheet at its fair value, with changes in its fair value recognized in current period earnings. The hedged item, including previously recorded mark-to-market adjustments, is derecognized immediately as a component of the gain or loss upon disposition.

Loans

We originate loans for investment, with such designation made at the time of origination. Loans are recorded at the contractual amounts due from borrowers, adjusted for unamortized discounts and premiums, undisbursed funds, net deferred loan fees and origination costs, and the allowance for loan losses.

Certain Small Business Administration ("SBA") loans that may be sold prior to maturity have been designated as held for sale at origination and are recorded at the lower of cost or fair value, determined on an aggregate basis. A valuation allowance is established if the market value of such loans is lower than their cost, and operations are charged or credited for valuation adjustments. Upon sales of such loans, we receive a fee for servicing the loans. The servicing asset is recorded based on the present value of the contractually specified servicing fee, net of adequate compensation, for the estimated life of the loan, discounted by a rate in the range of 11 percent to 12 percent and a constant prepayment rate ranging from 6 percent to 16 percent. The servicing asset is amortized in proportion to and over the period of estimated servicing income. Management periodically evaluates the servicing asset for impairment. Impairment, if it occurs, is recognized in a valuation allowance in the period of impairment.

Interest-only strips are recorded based on the present value of the excess of total servicing fee over the contractually specified servicing fee for the estimated life of the loan, calculated using the same assumptions as noted above. Such interest-only strips are accounted for at their estimated fair value, with unrealized gains or losses recorded as adjustments to Other Comprehensive Income.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loan Interest Income and Fees

Interest on loans is credited to income as earned and is accrued only if deemed collectible. Direct loan origination costs are offset by loan origination fees with the net amount deferred and recognized over the contractual lives of the loans in interest income as a yield adjustment using the effective interest method. Discounts or premiums associated with purchased loans are accreted or amortized to interest income using the interest method over the contractual lives of the loans, adjusted for prepayments. Accretion of discounts and deferred loan fees is discontinued when loans are placed on non-accrual status.

Loans are placed on non-accrual status when, in the opinion of management, the full timely collection of principal or interest is in doubt. Generally, the accrual of interest is discontinued when principal or interest payments become more than 90 days past due. However, in certain instances, we may place a particular loan on non-accrual status earlier, depending upon the individual circumstances surrounding the loan's delinquency. When an asset is placed on non-accrual status, previously accrued but unpaid interest is reversed against current income. Subsequent collections of cash are applied as principal reductions when received, except when the ultimate collectibility of principal is probable, in which case interest payments are credited to income. Non-accrual assets may be restored to accrual status when principal and interest become current and full repayment is expected. Interest income is recognized on the accrual basis for impaired loans not meeting the criteria for non-accrual.

Allowance for Loan Losses

Management believes the allowance for loan losses is adequate to provide for probable losses inherent in the loan portfolio. However, the allowance is an estimate that is inherently uncertain and depends on the outcome of future events. Management's estimates are based on previous loan loss experience; volume, growth and composition of the loan portfolio; the value of collateral; and current economic conditions. Our lending is concentrated in consumer, commercial, construction and real estate loans in the greater Los Angeles/Orange County area. Although management believes the level of the allowance is adequate to absorb probable losses inherent in the loan portfolio, a decline in the local economy may result in increasing losses that cannot reasonably be predicted at this date.

Non-performing loans are those that are not earning income, and (1) full payment of principal and interest is no longer anticipated, (2) principal or interest is 90 days or more delinquent, or (3) the loan payment or term has been restructured in accordance with troubled debt restructure procedures. The Bank generally places loans on non-accrual status when interest or principal payments become 90 days or more past due unless the outstanding principal and interest is adequately secured and, in the opinion of management, is deemed to be in the process of collection. When loans are placed on non-accrual status, accrued but unpaid interest is reversed against the current year's income, and interest income on non-accrual loans is recorded on a cash basis. The Bank may treat payments as interest income or return of principal depending upon management's opinion of the ultimate risk of loss on the individual loan. Cash payments are treated as interest income where management believes the remaining principal balance is fully collectible. Additionally, the Bank may place loans that are not 90 days past due on non-accrual status, if management reasonably believes the borrower will not be able to comply with the contractual loan repayment terms and collection of principal or interest is in question.

Loan losses are charged, and recoveries are credited, to the allowance account. Additions to the allowance account are charged to the provision for credit losses. The allowance for loan losses is maintained at a level considered adequate by management to absorb probable losses in the loan portfolio. The adequacy of the allowance is determined by management based upon an evaluation and review of the loan portfolio, consideration of historical loan loss experience, current economic conditions, changes in the composition of the loan portfolio, analysis of collateral values and other pertinent factors.

Loans are measured for impairment when it is probable that all amounts, including principal and interest, will not be collected in accordance with the contractual terms of the loan agreement. The amount of impairment and any subsequent changes are recorded through the provision for credit losses as an adjustment to the allowance for loan losses. Accounting standards require that an impaired loan be measured based on:

1. the present value of the expected future cash flows, discounted at the loan's effective interest rate; or
2. the loan's observable fair value; or
3. the fair value of the collateral, if the loan is collateral-dependent.

We evaluate installment loans for impairment on a pooled basis. These loans are considered to be smaller balance, homogeneous loans and are evaluated on a portfolio basis considering the projected net realizable value of the portfolio compared to the net carrying value of the portfolio.

Hanmi Bank follows the "*Interagency Policy Statement on the Allowance for Loan and Lease Losses*" and analyzes the allowance for loan losses on a monthly basis. In addition, as an integral part of the quarterly credit review process of the Bank, the allowance for loan losses and allowance for off-balance sheet items are reviewed for adequacy. The California Department of Financial Institutions ("DFI") and/or the FRB require the Bank to recognize additions to the allowance for loan losses based upon their assessment of the information available to them at the time of their examinations.

Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation on furniture, fixtures and equipment is computed on the straight-line method over the estimated useful lives of the related assets, which range from three to 30 years. Leasehold improvements are capitalized and amortized using the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

Goodwill

Goodwill, which represents the excess of purchase price over fair value of net assets acquired, amounted to $209.1 million and $209.6 million as of December 31, 2005 and 2004, respectively. We adopted SFAS No. 142, "*Goodwill and Other Intangible Assets*" ("SFAS No. 142"), effective January 1, 2002. SFAS No. 142 required that goodwill be recorded at the reporting unit level. Reporting units are defined as an operating segment. We have identified one reporting unit – our banking operations. SFAS No. 142 prohibits the amortization of goodwill, but requires that it be tested for impairment at least annually, or earlier if events have occurred that might indicate impairment. We ceased amortization of goodwill as of January 1, 2002. Our impairment test is performed in two phases. The first step involves comparing the fair value of the reporting unit with its carrying amount, including goodwill. Fair value of the reporting unit is estimated using two different valuation techniques: (a) discounted earnings cash flow and (b) average market price to earnings multiple using a management selected peer group. If the fair value of the reporting unit exceeds its fair value, an additional procedure must be performed. This additional procedure involves comparing the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. An impairment loss is recorded through earnings to the extent the carrying amount of goodwill exceeds its implied fair value. As of December 31, 2005 and 2004, management is unaware of any circumstances that would indicate a potential impairment of goodwill.

Core Deposit Intangible

We amortize the core deposit intangible ("CDI") balance using an accelerated method over eight years. As required upon adoption of SFAS No. 142, we evaluated the useful lives assigned to the CDI assets and determined that no change was necessary and amortization expense was not adjusted for the year ended December 31, 2005. As required by SFAS No. 142, the CDI balance is assessed for impairment or recoverability whenever events or changes in circumstances indicate the carrying amount may not be recoverable. The CDI recoverability analysis is consistent with our policy for assessing impairment of long-lived assets. As of and for the year ended December 31, 2005 and 2004, management is not aware of any circumstances that would indicate impairment of the CDI asset, and no impairment charges were recorded through earnings in 2005.

As of December 31, 2005 and 2004, the gross carrying amount of the CDI balance totaled $13.8 million and $13.8 million, respectively, and the related accumulated amortization totaled $5.1 million and $2.3 million, respectively. The total amortization expense on the CDI balance was $2,785,000, $1,872,000 and $121,000 during the years ended December 31, 2005, 2004 and 2003, respectively.

Estimated future amortization expense of the CDI balance is as follows: $2,379,000 in 2006; $2,039,000 in 2007; $1,675,000 in 2008; $1,284,000 in 2009; $865,000 in 2010; and $450,000 thereafter.

Junior Subordinated Debentures

We have established three statutory business trusts that are wholly owned subsidiaries of Hanmi Financial. In three separate private placement transactions, the Trusts issued variable rate capital securities representing undivided preferred beneficial interests in the assets of the Trusts. Hanmi Financial is the owner of all the beneficial interests represented by the common securities of the Trusts.

FASB Interpretation No. 46R, "*Consolidation of Variable Interest Entities (Revised December 2003) – an Interpretation of ARB No. 51*," requires that variable interest entities be consolidated by a company if that company is subject to a majority of expected loss from the variable interest entity's activities or is entitled to receive a majority of the entity's expected residual returns or both. Junior subordinated debt represents liabilities of the Hanmi Financial to the Trusts.

Income Taxes

We provide for income taxes using the asset and liability method. Under this method, 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 and operating loss and tax credit carryforwards. 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. A valuation allowance is provided when it is more likely than not that some portion or all of the deferred tax assets will not be realized.

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, compensation cost for stock options and restricted stock awards is measured as the excess, if any, of the quoted market price of our stock at the date of grant over the exercise price an employee must pay to acquire the stock. 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:

(Dollars in Thousands, Except Per Share Amounts)	*Years Ended December 31,* 2005	2004	2003
Net income – as reported	$ 58,229	$ 36,700	$ 19,213
Add – stock-based employee compensation expense included in reported net income, net of related tax effects (restricted stock award)	409	–	–
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	(1,214)	(408)	(521)
Net income – pro forma	$ 57,424	$ 36,292	$ 18,692
Earnings per share – as reported:			
Basic	$ 1.18	$ 0.87	$ 0.68
Diluted	$ 1.17	$ 0.84	$ 0.67
Earnings per share – pro forma:			
Basic	$ 1.17	$ 0.86	$ 0.67
Diluted	$ 1.15	$ 0.83	$ 0.65

The estimated weighted-average fair value of options granted was $4.96 per share in 2005, $3.94 per share in 2004 and $3.30 per share in 2003. The weighted-average fair value of options granted under our fixed stock option plan was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions: dividend yield of 1.18 percent, 1.40 percent and 0.00 percent in 2005, 2004 and 2003, respectively; expected volatility of 32.6 percent, 32.4 percent and 31.0 percent in 2005, 2004 and 2003; respectively; expected lives of 4.1 years, 4.2 years and 4.5 years in 2005, 2004 and 2003, respectively; and risk-free interest rates of 4.13 percent, 2.90 percent and 1.87 percent in 2005, 2004 and 2003, respectively.

In February 2005, 100,000 shares of restricted stock were awarded 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 each 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 year ended December 31, 2005, compensation expense of $665,000 was recognized in the Consolidated Statements of Income.

Earnings Per Share

Basic earnings per share ("EPS") is computed by dividing earnings available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution of securities that could share in the earnings.

Treasury Stock

We use the cost method of accounting for treasury stock. The cost method requires us to record the reacquisition cost of treasury stock as a deduction from shareholders' equity on the Consolidated Statements of Financial Condition.

Impairment of Long-Lived Assets

We account for long-lived assets in accordance with the provisions of SFAS No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets*." This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recently Issued Accounting Standards

In December 2004, the Financial Accounting Standards Board ("FASB") issued a revision to SFAS No. 123R (Revised), "*Share-Based Payment*" ("SFAS No. 123R"). This Statement 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 Statement of Income. This Statement replaces SFAS No. 123, "*Accounting for Stock-Based Compensation*," and supersedes Accounting Principles Board ("APB") Opinion No. 25, "*Accounting for Stock Issued to Employees*." In addition, this Statement amends SFAS No. 95, "*Statement of Cash Flows*," to require that excess tax benefits be reported as a financing cash inflow rather than as a reduction of taxes paid. This Statement is effective for Hanmi Financial as of January 1, 2006. We have elected to use the modified prospective method to adopt SFAS No. 123R.

As a result of the adoption of SFAS No. 123R, we estimate that we will recognize additional compensation expense of approximately $894,000, net of taxes, or $.02 per diluted share, for the full year 2006. Estimated future levels of compensation expense recognized related to stock based awards would be impacted by new awards, modifications to awards, or cancellation of awards after the adoption of SFAS No. 123R.

In February 2006, the FASB issued SFAS No. 155, "*Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and SFAS No. 140*" ("SFAS No. 155"). This Statement:

- permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation;
- clarifies which interest-only strips and principal-only strips are not subject to SFAS No. 133;
- establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or hybrid financial instruments that contain an embedded derivative requiring bifurcation;
- clarifies that concentrations of credit risks in the form of subordinations are not embedded derivatives; and
- amends SFAS No. 140 to eliminate the prohibition on a QSPE from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. Early adoption of this statement is allowed. We have not determined the financial impact of the adoption of SFAS No. 155 or whether we will adopt SFAS No. 155 in 2006.

In May 2005, the FASB issued SFAS No. 154, "*Accounting Changes and Error Corrections*." SFAS No. 154 replaces 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. SFAS No. 154 is not expected to have a material impact on our financial position or results of operations.

In March 2004, the FASB issued Emerging Issues Task Force ("EITF") Issue No. 03-1, "*The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*" ("EITF No. 03-1"). This EITF describes a model involving three steps: (1) determine whether an investment is impaired; (2) determine whether the impairment is other-than-temporary; and (3) recognize any impairment loss in earnings. The EITF also requires several additional disclosures for cost-method investments. In September 2004, the FASB approved the deferral of the effective date for EITF No. 03-1 pending reconsideration of implementation guidance relating to debt securities that are impaired solely due to market interest rate fluctuation.

On November 3, 2005, FASB Staff Position ("FSP") FAS Nos. 115-1 and 124-1, "*The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*," was issued. This FSP nullifies certain requirements of EITF No. 03-1 and supersedes EITF Topic No. D-44, "*Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value*." This FSP nullified the requirements of paragraphs 10 to 18 of EITF No. 03-1, carried forward the requirements of paragraphs 8 and 9 of EITF No. 03-1 with respect to cost-method investments, and carried forward the disclosure requirements included in paragraphs 21 and 22 of EITF No. 03-1 and related examples. The guidance in this FSP is applicable to reporting periods beginning after December 15, 2005. Adoption is not expected to have a material impact on our financial position, results of operations or related disclosures.

In December 2003, the American Institute of Certified Public Accountants ("AICPA") released Statement of Position 03-3, "*Accounting for Certain Loans or Debt Securities Acquired in a Transfer*" ("SOP 03-3"). SOP 03-3 addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities acquired in a transfer if those differences are attributable to credit quality. SOP 03-3 is effective for loans acquired in fiscal years beginning after December 15, 2004. Adoption in 2005 did not have a material impact on our financial position or results of operations.

In December 2004, the FASB issued SFAS No. 153, "*Exchange of Non-Monetary Assets, an Amendment of APB Opinion No. 29, 'Accounting for Non-Monetary Transactions'*" ("SFAS No. 153"). SFAS No. 153 is based on the principle that exchange of non-monetary assets should be measured based on the fair market value of the assets exchanged. SFAS No. 153 eliminates the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. SFAS No. 153 is effective for non-monetary asset exchanges in fiscal periods beginning after June 15, 2005. Adoption is not expected to have a material impact on our financial position or results of operations.

Reclassifications

Certain reclassifications were made to the prior year's presentation to conform to the current year's presentation.

Note 2 – Business Combination

On April 30, 2004, we completed our acquisition of PUB and merged PUB with Hanmi Bank. We paid $164.6 million in cash to acquire 5,537,431 of the PUB shares owned by Korea Exchange Bank. All of the remaining PUB shares were converted in the acquisition into shares of Hanmi Financial's common stock based on an exchange ratio of 2.312 Hanmi Financial shares for each PUB share.

In addition, all outstanding PUB employee stock options were converted into 137,414 options to purchase Hanmi Financial stock valued at $1.1 million in total. Based on Hanmi Financial's average price of $12.53 for the five-day trading period from April 28 through May 4, 2004, the total consideration paid for PUB was $324.6 million and resulted in the recognition of goodwill aggregating $207.2 million.

Purchase Price and Acquisition Costs

The purchase price was as follows:

(Dollars in Thousands, Except Share Prices)

Common Stock:		
Number of shares of PUB stock outstanding as of April 30, 2004		10,908,821
Less shares acquired for cash		(5,537,431)
Number of shares of PUB stock to be exchange for Hanmi stock		5,371,390
Exchange ratio		2.312
Stock issued in PUB acquisition		12,418,654
Multiplied by Hanmi Financial's average stock price for the period two days before through two days after the April 29, 2004 pricing of the merger agreement	$	12.53
	$	155,606
Stock Options:		
Estimated fair value of 137,414 Hanmi Financial stock options to be issued in Exchange for 59,443 PUB outstanding stock options, calculated using the Black-Scholes option pricing model, modified for dividends, with model assumptions estimated as of April 30, 2004 and a Hanmi Financial stock price of $12.53, the average stock price for the period two days before through two days after the April 29, 2004 pricing of the merger agreement		1,063
Cash		164,562
Transaction Costs:		
Cash		3,320
Stock warrants		145
Total purchase price	$	324,696

The purchase price was allocated based on the fair values of the assets acquired and liabilities assumed:

(In Thousands)		
Book value of net assets acquired	$	110,683
Adjustments:		
Adjustment to record acquired securities at estimated fair value		(1,489)
Adjustment to record acquired loans at estimated fair value		376
Adjustment to record acquired fixed assets at estimated fair value		5,459
Adjustment to record core deposit intangible asset		13,137
Adjustment to record various other assets at estimated fair value		15
Adjustment to record interest-bearing deposits at fair value		(264)
Adjustment to record other borrowings at fair value		(789)
Adjustment to record severance benefits associated with the elimination of positions, termination of certain contractual obligations of PUB and other miscellaneous adjustments		(1,711)
Adjustment to record deferred tax liability		(7,948)
Adjustment to record goodwill associated with the acquisition of PUB		207,227
Total purchase price	$	324,696

As of December 31, 2005, the carrying amount of goodwill from the PUB acquisition was $207.2 million compared to $207.8 million at December 31, 2004, a decrease of $585,000. The decrease was due to adjustments based on the final valuation of net assets acquired.

The fair value of PUB net assets acquired was as follows:

(In Thousands)		
Assets:		
Cash and due from banks	$	27,483
Federal fund sold		76,900
Federal home loan bank stock		6,256
Securities available for sale		157,905
Loans receivable, net of allowance for loan losses		865,743
Premises and equipment		11,668
Accrued interest receivable		3,498
Goodwill		207,227
Core deposit intangible		13,137
Other assets		12,888
Total assets	$	1,382,705
Liabilities:		
Deposits	$	936,699
Borrowings		105,789
Other liabilities		15,521
Total liabilities	$	1,058,009
Net assets acquired	$	324,696

The core deposit intangible is being amortized using an accelerated method over eight years. None of the goodwill balance is expected to be deductible for income tax purposes.

Merger-related costs recognized as expenses during 2004 consisted of employee retention bonuses, the costs of vacating duplicative branches within the existing network and the impairment of fixed assets (primarily leasehold improvements) associated with such branches. Of the $2,053,000 provided in 2004, $767,000 and $777,000 was utilized and charged against the related liability in 2005 and 2004, respectively. The remaining balance of $509,000 was reversed in 2005.

Certain costs (primarily PUB employee severance, data processing contract termination costs, and the costs of vacating duplicative branches within PUB's network) were recognized as liabilities assumed in the business combination or impairments of fixed assets associated with such branches. Accordingly, they have been considered part of the purchase price of PUB and recorded as an increase in the balance of goodwill. Of the $4,515,000 provided, $834,000 and $2,444,000 was utilized and charged against the related liability in 2005 and 2004, respectively, and $1,142,000 was reversed in 2005. The remaining balance of $95,000 is related to certain lease commitments that may continue into 2009.

We incurred the following merger-related costs for the years ended December 31, 2005 and 2004:

(In Thousands)		*Expensed (Credited)*		*Included in Cost of Acquisition*
Merger-related costs – 2005:				
Reversal of merger-related costs	$	(509)	$	(1,142)
Total merger-related costs – 2005	$	(509)	$	(1,142)
Merger-related costs – 2004:				
Employee termination costs	$	1,364	$	1,425
Contract termination costs		–		1,828
Leasehold termination costs		348		1,262
Asset impairments		341		–
Total merger-related costs – 2004	$	2,053	$	4,515

Note 3 – Securities Purchased Under Agreements to Resell

We purchase government agency securities and/or whole loans under agreements to resell the same securities (reverse repurchase agreements) with primary dealers. Amounts advanced under these agreements represent cash and cash equivalents. Securities subject to the reverse repurchase agreements are held in the name of Hanmi Financial by dealers who arrange the transactions. In the event that the fair value of the securities decreases below the carrying amount of the related reverse repurchase agreement, the counterparties are required to designate an equivalent value of additional securities in the name of Hanmi Financial.

The following is a summary of the securities purchased under agreements to resell at December 31, 2005 and 2004:

(Dollars in Thousands)	*December 31,* 2005	2004
Balance at year-end	$ 20,000	$ 10,000
Average balance outstanding during the year	$ 13,137	$ 55
Maximum amount outstanding at any month-end during the year	$ 25,000	$ 10,000
Weighted-average interest rate during the year	3.38%	2.33%

Note 4 – Securities

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

Note 4 – Securities

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

(In Thousands)	*Amortized Cost*	*Gross Unrealized Gain*	*Gross Unrealized Loss*	*Estimated Fair Value*
December 31, 2005:				
Municipal bonds	$ 692	$ —	$ —	$ 692
Mortgage-backed securities	357	2	—	359
	$ 1,049	$ 2	$ —	$ 1,051
December 31, 2004:				
Municipal bonds	$ 691	$ —	$ —	$ 691
Mortgage-backed securities	399	3	—	402
	$ 1,090	$ 3	$ —	$ 1,093

The following is a summary of securities available for sale:

(In Thousands)	*Amortized Cost*	*Gross Unrealized Gain*	*Gross Unrealized Loss*	*Estimated Fair Value*
December 31, 2005:				
Mortgage-backed securities	$ 149,311	$ 144	$ 2,187	$ 147,268
U.S. Government agencies	129,589	—	1,776	127,813
Collateralized mortgage obligations	83,068	3	1,615	81,456
Municipal bonds	71,536	1,758	74	73,220
Corporate bonds	8,235	—	182	8,053
Other	4,999	156	102	5,053
	$ 446,738	$ 2,061	$ 5,936	$ 442,863
December 31, 2004:				
Mortgage-backed securities	$ 148,706	$ 1,014	$ 546	$ 149,174
U.S. Government agencies	89,345	381	49	89,677
Collateralized mortgage obligations	93,172	236	869	92,539
Municipal bonds	71,771	1,938	93	73,616
Corporate bonds	8,380	76	12	8,444
Other	4,437	34	38	4,433
	$ 415,811	$ 3,679	$ 1,607	$ 417,883

The amortized cost and estimated fair value of investment securities at December 31, 2005, by contractual maturity, are shown below. Although mortgage-backed securities and collateralized mortgage obligations have contractual maturities through 2035, expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale		*Held to Maturity*	
(In Thousands)	*Amortized Cost*	*Estimated Fair Value*	*Amortized Cost*	*Estimated Fair Value*
Within one year	$ 15,245	$ 15,205	$ –	$ –
Over one year through five years	129,260	127,392	–	–
Over five years through ten years	7,279	7,397	692	692
Over ten years	62,575	64,145	–	–
	214,359	214,139	692	692
Mortgage-backed securities	149,311	147,268	357	359
Collateralized mortgage obligations	83,068	81,456	–	–
	232,379	228,724	357	359
	$ 446,738	$ 442,863	$ 1,049	$ 1,051

Gross unrealized losses on investment securities and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were as follows as of December 31, 2005 and 2004:

	Holding Period					
	Less than 12 Months		*12 Months or More*		*Total*	
(In Thousands)	*Unrealized Losses*	*Estimated Fair Value*	*Unrealized Losses*	*Estimated Fair Value*	*Unrealized Losses*	*Estimated Fair Value*
Available for Sale – December 31, 2005:						
Mortgage-backed securities	$ 922	$ 78,891	$ 1,265	$ 40,364	$ 2,187	$ 119,255
U.S. Government agency securities	1,682	112,931	94	9,882	1,776	122,813
Collateralized mortgage obligations	383	29,281	1,232	42,988	1,615	72,269
Municipal bonds	31	4,126	43	2,353	74	6,479
Corporate bonds	106	5,102	76	2,951	182	8,053
Other	21	979	81	1,919	102	2,898
	$ 3,145	$ 231,310	$ 2,791	$ 100,457	$ 5,936	$ 331,767
Available for Sale – December 31, 2004:						
Mortgage-backed securities	$ 135	$ 22,747	$ 411	$ 37,428	$ 546	$ 60,175
U.S. Government agency securities	264	13,780	605	39,824	869	53,604
Collateralized mortgage obligations	49	14,883	–	–	49	14,883
Municipal bonds	–	–	93	3,775	93	3,775
Corporate bonds	12	3,103	–	–	12	3,103
Other	–	–	38	1,962	38	1,962
	$ 460	$ 54,513	$ 1,147	$ 82,989	$ 1,607	$ 137,502

All individual securities that have been in a continuous unrealized loss position for 12 months or longer at December 31, 2005 and 2004 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 December 31, 2005 and 2004. These securities have fluctuated in value since their purchase dates as market interest rates have fluctuated. However, we have 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 December 31, 2005 and 2004 are not other-than-temporarily impaired, and therefore, no impairment charges as of December 31, 2005 and 2004 are warranted.

Securities with carrying values of $279.7 million and $307.5 million as of December 31, 2005 and 2004, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

There were $117,000, $134,000 and $1,094,000 in net realized gains on sales of securities available for sale during the years ended December 31, 2005, 2004 and 2003, respectively. In 2005, $3.6 million ($2.6 million, net of tax) of unrealized losses arose during the year and were included in comprehensive income and $114,000 ($83,000, net of tax) of previously unrealized gains were realized in earnings. In 2004, $983,000 ($713,000, net of tax) of unrealized losses arose during the year and were included in comprehensive income and $167,000 ($122,000, net of tax) of previously unrealized losses were realized in earnings. In 2003, $1.8 million ($1.3 million, net of tax) of unrealized losses arose during the year and were included in comprehensive income and $1.1 million ($692,000, net of tax) of previously unrealized gains were realized in earnings.

Note 5 – Loans Receivable and Allowance for Loan Losses

Loans receivable consisted of the following at December 31:

(In Thousands)	*2005*	*2004*
Real Estate Loans:		
Commercial property	$ 733,650	$ 783,539
Construction	152,080	92,521
Residential property	87,377	80,786
Total real estate loans	973,107	956,846
Commercial and Industrial Loans:		
Commercial term loans	945,210	754,108
Commercial lines of credit	224,271	201,940
SBA loans	155,491	162,435
International loans	106,520	95,936
Total commercial loans	1,431,492	1,214,419
Consumer Loans	92,154	87,526
Total gross loans	2,496,753	2,258,791
Allowance for loans losses	(24,963)	(22,702)
Deferred loan fees	(3,775)	(5,097)
Loans receivable, net	$ 2,468,015	$ 2,230,992

Activity in the allowance for loan losses and allowance for off-balance sheet items was as follows:

	As of and for the Years Ended December 31,								
	2005			*2004*			*2003*		
(In Thousands)	*Allowance for Loan Losses*	*Allowance for Off-Balance Sheet Items*	*Total*	*Allowance for Loan Losses*	*Allowance for Off-Balance Sheet Items*	*Total*	*Allowance for Loan Losses*	*Allowance for Off-Balance Sheet Items*	*Total*
Balance – beginning of year	$ 22,702	$ 1,800	$ 24,502	$ 13,349	$ 1,385	$ 14,734	$ 11,254	$ 1,015	$ 12,269
Allowance for loan losses acquired in PUB acquisition	–	–	–	10,566	–	10,566	–	–	–
Provision charged to operating expense	5,065	330	5,395	2,492	415	2,907	5,310	370	5,680
Loans charged off	(5,198)	–	(5,198)	(5,485)	–	(5,485)	(4,423)	–	(4,423)
Recoveries, net of charge-offs	2,394	–	2,394	1,780	–	1,780	1,208	–	1,208
Balance – end of year	$ 24,963	$ 2,130	$ 27,093	$ 22,702	$ 1,800	$ 24,502	$ 13,349	$ 1,385	$ 14,734

The following is a summary of interest foregone on impaired loans for the years ended December 31:

(In Thousands)	*2005*	*2004*	*2003*
Interest income that would have been recognized had impaired loans performed in accordance with their original terms	$ 957	$ 678	$ 362
Less: interest income recognized on impaired loans	(603)	(350)	(204)
Interest foregone on impaired loans	$ 354	$ 328	$ 158

The following table provides information on impaired loans for the periods indicated:

	As of and for the Years Ended December 31,		
(In Thousands)	*2005*	*2004*	*2003*
Recorded investment with related allowance	$ 7,548	$ 4,391	$ 5,893
Recorded investment with no related allowance	3,235	3,262	392
Allowance on impaired loans	(4,991)	(3,039)	(2,972)
Net recorded investment in impaired loans	$ 5,792	$ 4,614	$ 3,313
Average total recorded investment in impaired loans	$ 14,340	$ 9,850	$ 6,400

There were no commitments to lend additional funds to borrowers whose loans are included above.

Loans on non-accrual status totaled $10.1 million and $5.8 million at December 31, 2005 and 2004, respectively. Loans past due 90 days or more and still accruing interest totaled $9,000 and $208,000 at December 31, 2005 and 2004, respectively. Restructured loans totaled $4.0 million and $2.6 million at December 31, 2005 and 2004, respectively.

The following is an analysis of all loans to officers and directors of Hanmi Financial and their affiliates. In the opinion of management, all such loans were made under terms that are consistent with our normal lending policies.

	December 31,	
(In Thousands)	*2005*	*2004*
Outstanding balance, beginning of year	$ 1,552	$ 885
Credit granted, including renewals	–	951
Repayments	(702)	(284)
Outstanding balance, end of year	$ 850	$ 1,552

Income from these loans totaled $81,000, $70,000 and $153,000 for the years ended December 31, 2005, 2004 and 2003, respectively, and is reflected in the accompanying Consolidated Statements of Income.

Servicing Assets

Changes in loan servicing rights, net of amortization, were as follows:

	December 31,	
(In Thousands)	*2005*	*2004*
Balance – beginning of year	$ 3,846	$ 2,364
Additions	1,150	2,172
Amortization	(1,086)	(690)
Balance – end of year	$ 3,910	$ 3,846

At December 31, 2005 And 2004, we serviced loans sold to unaffiliated parties in the amounts of $183.4 million and $173.7 million, respectively. All of the loans being serviced were SBA loans.

Note 6 – Premises and Equipment

The following is a summary of the major components of premises and equipment:

	December 31,	
(In Thousands)	*2005*	*2004*
Land	$ 6,120	$ 6,120
Buildings and improvements	7,804	7,354
Furniture and equipment	12,095	11,116
Leasehold improvements	7,924	7,845
Software	387	–
	34,330	32,435
Accumulated depreciation and amortization	(13,546)	(12,744)
Total premises and equipment, net	$ 20,784	$ 19,691

Depreciation and amortization expense totaled $2,704,000, $2,447,000 and $1,558,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

Note 7 – Deposits

Time deposits by maturity were as follows:

	December 31,	
(In Thousands)	*2005*	*2004*
Less than three months	$ 701,140	$ 534,394
After three months to six months	314,151	289,134
After six months to twelve months	407,689	174,548
After twelve months	16,771	33,624
Total time deposits	$ 1,439,751	$ 1,031,700

For time deposits having a remaining term of more than one year, the aggregate amount of maturities for each of the five years following the balance sheet date are as follows: none in 2006; $7,027,000 in 2007; $1,040,000 in 2008; $9,350,000 in 2009; and $55,000 in 2010.

A summary of interest expense on deposits was as follows for the years ended December 31, 2005, 2004 and 2003:

(In Thousands)	2005	2004	2003
Money market checking	$ 12,964	$ 8,098	$ 2,584
Savings	2,130	1,790	1,894
Time deposits of $100,000 or more	31,984	10,966	7,415
Other time deposits	7,114	5,414	7,354
Total interest expense on deposits	$ 54,192	$ 26,268	$ 19,247

Total deposits reclassified to loans due to overdraft at December 31, 2005 and 2004 were $3.7 million and $3.0 million, respectively.

Note 8 – Other Borrowed Funds

Other borrowed funds consisted of the following:

	December 31,	
(In Thousands)	2005	2004
FHLB advances	$ 43,527	$ 66,363
Note issued to U.S. Treasury	2,804	2,930
Total other borrowed funds	$ 46,331	$ 69,293

FHLB advances represent collateralized obligations with the FHLB of San Francisco. A summary of contractual maturities follows:

(In Thousands) Year	Amount	Interest Rate
2006	$ 5,000	3.56%
2007	20,000	3.85%
2008	–	–
2009	6,000	5.63%
2010	7,411	4.44%
Thereafter	5,116	5.27%
	$ 43,527	

Financial data pertaining to FHLB advances were as follows:

	Years Ended December 31,		
(Dollars in Thousands)	2005	2004	2003
Weighted-average interest rate at end of year	4.33%	4.12%	1.65%
Weighted-average interest rate during the year	3.70%	2.23%	2.74%
Average balance of FHLB advances	$ 74,437	$ 137,827	$ 52,577
Maximum amount outstanding at any month-end	$ 100,700	$ 261,000	$ 148,400

All of the FHLB advances had fixed interest rates.

We have pledged investment securities available for sale with a carrying value of $279.7 million as collateral with the FHLB for this borrowing facility. The total borrowing capacity available from the collateral that has been pledged is $1,062.3 million, of which $782.6 million remained available as of December 31, 2005.

For the years ended December 31, 2005, 2004 and 2003, interest expense on other borrowed funds totaled $3.0 million, $3.3 million and $1.5 million, respectively, and the weighted-average interest rates were 3.36 percent, 2.14 percent and 2.45 percent, respectively.

In 2005, we obtained additional lines of credit totaling $69.0 million. Total credit lines for borrowing amounted to $154.0 million at December 31, 2005. As of December 31, 2005 and 2004, there were no borrowings under these credit lines.

Note 9 – Junior Subordinated Debentures

During the first half of 2004, we issued two junior subordinated notes bearing interest at the three-month London InterBank Offered Rate ("LIBOR") plus 2.90 percent totaling $61.8 million and one junior subordinated note bearing interest at the three-month LIBOR plus 2.63 percent totaling $20.6 million. The outstanding subordinated debentures related to these offerings, the proceeds of which were used to finance the purchase of PUB, totaled $82.4 million at December 31, 2005.

For the years ended December 31, 2005 and 2004, interest expense on the junior subordinated debentures totaled $4.9 million and $3.0 million, respectively, and the weighted-average interest rates were 5.94 percent and 4.41 percent, respectively.

Note 10 – Income Taxes

A summary of income taxes for the years ended December 31, 2005, 2004 and 2003 follows:

(In Thousands)	2005	2004	2003
Current:			
Federal	$ 29,779	$ 16,010	$ 10,852
State	9,383	6,271	3,642
	39,162	22,281	14,494
Deferred:			
Federal	(2,350)	1,032	(1,732)
State	(357)	(338)	(337)
	(2,707)	694	(2,069)
Income taxes	$ 36,455	$ 22,975	$ 12,425

As of December 31, 2005 and 2004, the Federal and state deferred tax assets are as follows:

(In Thousands)	2005	2004
Deferred tax assets:		
Credit loss provision	$ 12,419	$ 11,232
Depreciation	591	816
State taxes	2,928	1,475
Unrealized loss on securities available for sale, interest-only strips and interest rate swaps	1,671	–
Other	59	42
Total deferred tax assets	17,668	13,565
Deferred tax liabilities:		
Purchase accounting	(6,497)	(7,022)
Unrealized gain on securities available for sale, interest-only strips and interest rate swaps	–	(744)
Other	(1,520)	(790)
Total deferred tax liabilities	(8,017)	(8,556)
Net deferred tax assets	$ 9,651	$ 5,009

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets, net of the valuation allowance.

A reconciliation of the difference between the Federal statutory income tax rate and the effective tax rate as of December 31 is shown in the following table:

	2005	2004	2003
Statutory tax rate	35.0%	35.0%	35.0%
State taxes, net of federal tax benefits	6.2%	6.5%	6.6%
Tax-exempt municipal securities	(1.2%)	(1.8%)	(1.5%)
Reversal of valuation allowance	–	(0.7%)	–
Other	(1.5%)	(0.5%)	(0.8%)
Effective tax rate	38.5%	38.5%	39.3%

At December 31, 2005, net current taxes payable of $2.3 million were included in Other Liabilities in the Consolidated Statements of Financial Condition. At December 31, 2004, net current taxes receivable of $2.4 million were included in Other Assets in the Consolidated Statements of Financial Condition.

Note 11 – Shareholders' Equity

Year 2000 Stock Option Plan

The Bank adopted a Stock Option Plan in 1992, which was replaced by the Hanmi Financial Corporation Year 2000 Stock Option Plan (the "Plan"), under which options to purchase shares of Hanmi Financial common stock may be granted to key employees and directors. The Plan provides that the option price shall not be less than the fair value of the stock on the effective date of the grant. Generally, options will vest over five years. No option may be granted with a term of more than ten years.

The following is a summary of the transactions under the Plan described above for the periods indicated:

	2005		2004		2003	
	Number of Shares	Weighted-Average Exercise Price Per Share	Number of Shares	Weighted-Average Exercise Price Per Share	Number of Shares	Weighted-Average Exercise Price Per Share
Options outstanding, beginning of year	1,618,836	$ 9.33	1,500,064	$ 5.52	2,137,012	$ 5.32
Options granted	135,554	$ 17.10	791,000	$ 13.51	80,000	$ 8.75
Options assumed in PUB acquisition	–	$ –	137,414	$ 5.11	–	$ –
Options exercised	(391,094)	$ 6.44	(670,576)	$ 4.82	(495,954)	$ 4.53
Options cancelled/expired	(189,584)	$ 13.26	(139,066)	$ 9.61	(220,994)	$ 6.99
Options outstanding – end of year	1,173,712	$ 10.55	1,618,836	$ 9.33	1,500,064	$ 5.52
Options exercisable – end of year	520,602	$ 7.00	487,242	$ 6.10	655,154	$ 5.26

As of December 31, 2005, stock options outstanding under the Plan were as follows:

	Options Outstanding			Options Exercisable	
Exercise Price Range	*Number Outstanding*	*Weighted-Average Exercise Price Per Share*	*Weighted-Average Remaining Contractual Life*	*Number Outstanding*	*Weighted-Average Exercise Price Per Share*
$ 3.27 to $ 3.99	211,602	$ 3.81	4.7 years	211,602	$ 3.81
$ 4.00 to $ 7.99	287,332	$ 7.06	5.3 years	205,909	$ 7.07
$ 8.00 to $11.99	3,624	$ 10.44	0.4 years	3,624	$ 10.44
$ 12.00 to $15.99	585,600	$ 13.67	8.3 years	99,467	$ 13.51
$ 16.00 to $19.10	85,554	$ 17.64	9.2 years	–	$ –
	1,173,712	$ 10.55		520,602	$ 7.00

2004 CEO Stock Option Plan

The Bank adopted the 2004 CEO Stock Option Plan (“CEO Plan”) under which 350,000 options to purchase shares of Hanmi Financial common stock were granted to the Chief Executive Officer. The CEO Plan provided that the option price on the effective date of the grant was equal to the fair value of the stock, which was $17.17. The options will vest over six years and expire after ten years.

Stock Warrants

In 2004, we issued stock warrants to affiliates of Castle Creek Financial LLC for services rendered in connection with the placement of our equity securities. Under the terms of the warrants, the warrant holders can purchase a total of 508,558 shares of common stock at an exercise price of $9.50 per share. The warrants were immediately exercisable and expire after five years. During 2005 and 2004, 0 and 20,000 shares of common stock, respectively, were issued for the exercise of stock warrants.

Repurchase of Common Stock

On August 25, 2005, we repurchased 1,163,000 shares of our common stock from Korea Exchange Bank for an aggregate purchase price of $20.0 million as part of our ongoing capital management program. Repurchased shares are held in treasury pending use for general corporate purposes, including issuances under our employee stock option plan.

Note 12 – Regulatory Matters

Hanmi Financial and the Bank are subject to various regulatory capital requirements administered by the Federal banking regulatory 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 our consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, Hanmi Financial and the Bank must meet specific capital guidelines that involve quantitative measures of the assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The 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 Hanmi Financial and the Bank to maintain minimum 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 that, as of December 31, 2005 and 2004, Hanmi Financial and the Bank met all capital adequacy requirements to which they were subject.

As of December 31, 2005, the most recent notification from the Federal Reserve Board 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 below. There are no conditions or events since that notification which management believes have changed the institution’s category.

The capital ratios of Hanmi Financial and Hanmi Bank at December 31, 2005 and 2004 were as follows:

	Actual		Minimum Regulatory Requirement		Minimum to Be Categorized as "Well Capitalized"	
(Dollars in Thousands)	*Amount*	*Ratio*	*Amount*	*Ratio*	*Amount*	*Ratio*
December 31, 2005						
Total capital (to risk-weighted assets):						
Hanmi Financial	$ 319,866	12.04%	$ 212,617	8.00%	N/A	N/A
Hanmi Bank	$ 318,099	11.98%	$ 212,383	8.00%	$ 265,478	10.00%
Tier 1 capital (to risk-weighted assets):						
Hanmi Financial	$ 292,750	11.03%	$ 106,191	4.00%	N/A	N/A
Hanmi Bank	$ 290,983	10.96%	$ 106,191	4.00%	$ 159,287	6.00%
Tier 1 capital (to average assets):						
Hanmi Financial	$ 295,750	9.11%	$ 128,56	4.00%	N/A	N/A
Hanmi Bank	$ 290,983	9.06%	$ 128,447	4.00%	$ 160,558	5.00%
December 31, 2004						
Total capital (to risk-weighted assets):						
Hanmi Financial	$ 281,684	11.98%	$ 188,173	8.00%	N/A	N/A
Hanmi Bank	$ 277,075	11.80%	$ 187,921	8.00%	$ 234,901	10.00%
Tier 1 capital (to risk-weighted assets):						
Hanmi Financial	$ 257,182	10.93%	$ 94,087	4.00%	N/A	N/A
Hanmi Bank	$ 252,573	10.75%	$ 93,960	4.00%	$ 140,940	6.00%
Tier 1 capital (to average assets):						
Hanmi Financial	$ 257,182	8.93%	$ 115,235	4.00%	N/A	N/A
Hanmi Bank	$ 252,573	8.78%	$ 115,055	4.00%	$ 143,818	5.00%

The average reserve balance required to be maintained with the FRB was $1.5 million as of December 31, 2005 and 2004.

Memorandum of Understanding

On July 20, 2005, following a joint regular examination by the FRB and the DFI, 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.

In January 2006, the FRB completed a Target Examination of compliance with the BSA. Management believes we have made significant progress in achieving full compliance with the terms of the Memorandum. In March 2006, the DFI and FRB initiated the Bank's annual joint regular examination for fiscal year 2005. Management cannot predict the outcome of this examination or whether the Memorandum will be lifted.

Note 13 – Earnings Per Share

The following is a reconciliation of the numerators and denominators of the basic and diluted per share computations for the years ended December 31, 2005, 2004 and 2003:

(Dollars in Thousands, Except Per Share Amounts)		*Income (Numerator)*	*Weighted-Average Shares (Denominator)*		*Per Share Amount*
2005:					
Basic EPS – income available to common shareholders	$	58,229	49,174,885	$	1.18
Effect of dilutive securities – options and warrants		–	767,471		(0.01)
Diluted EPS – income available to common shareholders	$	58,229	49,942,356	$	1.17
2004:					
Basic EPS – income available to common shareholders	$	36,700	42,268,964	$	0.87
Effect of dilutive securities – options and warrants		–	1,248,293		(0.03)
Diluted EPS – income available to common shareholders	$	36,700	43,517,257	$	0.84
2003:					
Basic EPS – income available to common shareholders	$	19,213	28,092,708	$	0.68
Effect of dilutive securities – options		–	569,318		(0.01)
Diluted EPS – income available to common shareholders	$	19,213	28,662,026	$	0.67

For the years ended December 31, 2005, 2004 and 2003, there were 50,554, 354,000 and 0 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.

Note 14 – Employee Benefits

We have a Section 401(k) plan for the benefit of substantially all of our employees. We match 75 percent of participant contributions to the 401(k) plan up to 8 percent of each 401(k) plan participant's annual compensation. We made contributions to the 401(k) plan for the years ended December 31, 2005, 2004 and 2003 of $918,000, $858,000 and $553,000, respectively.

In 2001 and 2004, we purchased single premium life insurance policies called bank-owned life insurance covering certain officers. Hanmi Bank is the beneficiary under the policy. In the event of the death of a covered officer, we will receive the specified insurance benefit from the insurance carrier.

Note 15 – Derivative Financial Instruments

During 2004, to hedge interest rate risk, the Bank entered into an interest rate swap agreement maturing in 2009, 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. During 2003, to hedge interest rate risk, the Bank entered into four interest rate swap agreements maturing in 2008, 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. These swaps were designated as cash flow hedges for accounting purposes.

In 2005, the Bank terminated these swaps. At such time, the swaps were in an unfavorable position of $2,139,000. Such amount is being amortized in amounts proportional to the interest income associated with the hedged loan pools over the remaining terms of the swaps or the lives of the hedged loans, whichever is shorter. Prior to the termination of the swaps, income of $0, $19,000 and $35,000 related to hedge ineffectiveness was recognized for the years ended December 31, 2005, 2004 and 2003, respectively.

In 2004, the Bank offered a certificate of deposit ("CD") product that paid interest tied to the movement in the Standard & Poor's 500 Index plus 1.00 percent annual interest. The economic characteristics and risks of the embedded option were not clearly and closely related to the CD. Therefore, the embedded option was separated from the CD and accounted for separately in liabilities. As of December 31, 2005 and 2004, the fair value of the embedded option was $1,280,000 and $1,396,000, respectively, and the change in the liability during 2005 and 2004 was ($4,000) and $242,000, respectively. The change was recognized in earnings.

To economically hedge the interest risk described above, the Bank entered into an agreement to purchase an equity swap with a notional amount of $9,340,000. As of December 31, 2005 and 2004, the fair value of the equity swap was $4,000 and $212,000, respectively, which was also equal to the change during those years. The change was recognized in earnings.

In 2005, the Bank offered a CD product that pays interest based on the increase in the weighted-average value of five Asian currencies (Korean Won, Singapore Dollar, Taiwan Dollar, Thai Baht and Chinese Yuan) against the U.S. Dollar plus 0.25 percent annual interest. The economic characteristics and risks of the embedded option were not clearly and closely related to the CD. Therefore, the embedded option was separated from the CD and accounted for separately in liabilities. As of December 31, 2005, the fair value of the embedded option was $5,000, and the change in the liability during 2005 was ($19,000). The change was recognized in earnings.

To economically hedge the interest risk described above, the Bank entered into an agreement to purchase a currency swap with a notional amount of $14,274,000. As of December 31, 2005, the fair value of the currency swap was ($105,000), and the change recognized in earnings for 2005 was $119,000.

Note 16 – Commitments and Contingencies

We lease our premises under non-cancelable operating leases. At December 31, 2005, future minimum annual rental commitments under these non-cancelable operating leases, with initial or remaining terms of one year or more, is as follows:

(In Thousands)

Year Ending December 31,	*Amount*
2006	$ 2,570
2007	2,457
2008	1,919
2009	1,284
2010	1,131
Thereafter	5,484
	$ 14,845

Rental expenses recorded under such leases in 2005, 2004 and 2003 amounted to $3,389,000, $3,226,000 and $2,008,000, respectively.

In the normal course of business, we are involved in various legal claims. Management has reviewed all legal claims against us with in-house or outside legal counsel and has taken into consideration the views of such counsel as to the outcome of the claims. In management's opinion, the final disposition of all such claims will not have a material adverse effect on our financial position or results of operations.

Note 17 – Off-Balance Sheet Commitments

We are a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the Consolidated Statements of Financial Condition. The Bank's exposure to credit losses in the event of non-performance by the other party to commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for extending loan facilities to customers. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty.

Collateral held varies but may include accounts receivable; inventory; property, plant and equipment; and income-producing or borrower-occupied properties. The following table shows the distribution of undisbursed loan commitments as of the dates indicated:

	December 31,	
(In Thousands)	*2005*	*2004*
Commitments to extend credit	$ 555,736	$ 367,708
Commercial letters of credit	58,036	49,699
Standby letters of credit	42,768	47,901
Unused credit card lines	14,892	14,324
Total undisbursed loan commitments	$ 671,432	$ 479,632

Note 18 – Fair Value of Financial Instruments

The estimated fair value of financial instruments has been determined by using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data in order to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that we could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

	December 31, 2005		December 31, 2004	
(In Thousands)	*Carrying Amount*	*Estimated Fair Value*	*Carrying Amount*	*Estimated Fair Value*
Assets:				
Cash and cash equivalents	$ 163,477	$ 163,477	$ 127,164	$ 127,164
Federal Reserve Bank stock	12,350	12,350	12,099	12,099
Federal Home Loan Bank stock	12,237	12,237	9,862	9,862
Securities held to maturity	1,049	1,051	1,090	1,093
Securities available for sale	442,863	442,863	417,883	417,883
Loans receivable, net	2,468,015	2,460,092	2,230,992	2,229,096
Loans held for sale	1,065	1,074	3,850	4,026
Accrued interest receivable	14,120	14,120	10,029	10,029
Interest rate swaps	–	–	(293)	(293)
Equity swap	4	4	212	212
Liabilities:				
Non-interest-bearing deposits	738,618	738,618	729,853	729,853
Interest-bearing deposits	2,087,496	2,087,496	1,799,22	1,799,224
Other borrowed funds and junior subordinated debentures	128,737	129,441	151,699	153,541
Accrued interest payable	11,911	11,911	7,100	7,100
Currency swap	(105)	(105)	–	–
Embedded derivative	1,280	1,280	1,396	1,396

The methods and assumptions used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value are explained below:

(a) Cash and cash equivalents – The carrying amounts approximate fair value due to the short-term nature of these instruments.

(b) Federal Reserve Bank stock and Federal Home Loan Bank stock – The carrying amounts approximate fair value as the stock may be resold to the issuer at carrying value.

(c) Securities – The fair value of securities is generally obtained from market bids for similar or identical securities or obtained from independent securities brokers or dealers.

(d) Loans – Fair values are estimated for portfolios of loans with similar financial characteristics, primarily fixed and adjustable rate interest terms. The fair values of fixed rate mortgage loans are based on discounted cash flows utilizing applicable risk-adjusted spreads relative to the current pricing of similar fixed rate loans, as well as anticipated repayment schedules. The fair value of adjustable rate commercial loans is based on the estimated discounted cash flows utilizing the discount rates that approximate the pricing of loans collateralized by similar commercial properties. The fair value of non-performing loans at December 31, 2005 and 2004 was not estimated because it is not practicable to reasonably assess the credit adjustment that would be applied in the marketplace for such loans. The estimated fair value is net of allowance for loan losses.

(e) Accrued interest receivable – The carrying amount of accrued interest receivable approximates its fair value.

(f) Deposits – The fair value of non-maturity deposits is the amount payable on demand at the reporting date. Non-maturity deposits include non-interest-bearing demand deposits, savings accounts and money market checking. Discounted cash flows have been used to value term deposits such as certificates of deposit. The discount rate used is based on interest rates currently being offered by the Bank on comparable deposits as to amount and term.

(g) Accrued interest payable – The carrying amount of accrued interest payable approximates its fair value.

(h) Other borrowed funds and junior subordinated debentures – Discounted cash flows have been used to value other borrowed funds and junior subordinated debentures.

(i) Loan commitments and standby letters of credit – The fair value of loan commitments and standby letters of credit is based upon the difference between the current value of similar loans and the price at which the Bank has committed to make the loans. The fair value of loan commitments and standby letters of credit is immaterial at December 31, 2005 and 2004.

(j) Interest rate swaps, equity swap, embedded derivative and currency swap – The carrying amounts of the interest rate swaps, equity swap, embedded derivative and currency swap approximate their fair value.

Note 19 – Condensed financial information of parent company

Statements of Financial Condition

	December 31,	
(In Thousands)	*2005*	*2004*
Assets:		
Cash	$ 1,470	$ 5,376
Receivable from Hanmi Bank	–	455
Investment in Hanmi Bank	505,009	475,302
Investment in unconsolidated subsidiaries	2,986	2,986
Other assets	3,091	1,799
Total assets	$ 512,556	$ 485,918
Liabilities and Shareholders' Equity:		
Liabilities:		
Junior subordinated debentures	$ 82,406	$ 82,406
Other liabilities	3,373	3,602
Shareholders' equity	426,777	399,910
Total liabilities and shareholders' equity	$ 512,556	$ 485,918

Statements of Income

	Years Ended December 31,		
(In Thousands)	*2005*	*2004*	*2003*
Equity in earnings of Hanmi Bank	$ 62,001	$ 39,574	$ 19,578
Other expenses, net	(6,133)	(4,673)	(602)
Income tax benefit	2,361	1,799	237
Net income	$ 58,229	$ 36,700	$ 19,213

Statements of Cash Flows

(In Thousands)	*Years Ended December 31,* 2005	2004	2003
Cash Flows from Operating Activities:			
Net income	$ 58,229	$ 36,700	$ 19,213
Adjustments to reconcile net income to net cash used in operating activities:			
Earnings of Hanmi Bank	(62,001)	(39,574)	(19,578)
Decrease (increase) in receivable from Hanmi Bank	455	(224)	(231)
Increase in other assets	(1,292)	(718)	(1,968)
(Decrease) increase in other liabilities	(229)	132	1,065
Tax benefit from exercise of non-qualified stock options	729	–	–
Net cash used in operating activities	(4,109)	(3,684)	(1,499)
Cash Flows from Investing Activities:			
Dividends received from Hanmi Bank	27,541	11,990	2,300
Capital contribution to Hanmi Bank	–	(80,000)	–
Acquisition of Pacific Union Bank	–	(71,710)	–
Purchase of investment in unconsolidated subsidiaries	–	(2,475)	(161)
Net cash provided by (used in) investing activities	27,541	(142,195)	2,139
Cash Flows from Financing Activities:			
Issuance of junior subordinated debentures	–	82,406	–
Proceeds from exercise of stock options	2,528	3,425	3,141
Stock issued through private placement	–	71,710	–
Repurchase of common stock	(20,041)	–	–
Cash dividends paid	(9,825)	(7,740)	(4,220)
Net cash (used in) provided by financing activities	(27,338)	149,801	(1,079)
Net (decrease) increase in cash	(3,906)	3,922	(439)
Cash – beginning of year	5,376	1,454	1,893
Cash – end of year	$ 1,470	$ 5,376	$ 1,454

Note 20 – Quarterly Financial Data (Unaudited)

Summarized quarterly financial data follows:

	Quarters Ended			
(Dollars in Thousands, Except Per Share Amounts)	*March 31*	*June 30*	*September 30*	*December 31*
2005:				
Interest income	$ 43,209	$ 47,607	$ 51,952	$ 56,339
Interest expense	11,347	13,462	16,831	20,471
Net interest income before provision for credit losses	31,862	34,145	35,121	35,868
Provision for credit losses	136	450	3,157	1,652
Non-interest income	7,357	7,347	9,200	8,312
Non-interest expenses	17,405	16,212	16,991	18,525
Income before income taxes	21,678	24,830	24,173	24,003
Income taxes	8,346	9,792	9,204	9,113
Net income	$ 13,332	$ 15,038	$ 14,969	$ 14,890
Earnings per share:				
Basic	$ 0.27	$ 0.30	$ 0.30	$ 0.31
Diluted	$ 0.27	$ 0.30	$ 0.30	$ 0.30
2004:				
Interest income	$ 21,998	$ 31,514	$ 39,144	$ 41,710
Interest expense	5,170	7,484	9,276	10,687
Net interest income before provision for credit losses	16,828	24,030	29,868	31,023
Provision for credit losses	900	850	–	1,157
Non-interest income	4,905	6,951	7,279	8,264
Non-interest expenses	10,364	17,762	18,989	19,451
Income before income taxes	10,469	12,369	18,158	18,679
Income taxes	4,083	4,824	7,089	6,979
Net income	$ 6,386	$ 7,545	$ 11,069	$ 11,700
Earnings per share:				
Basic	$ 0.22	$ 0.18	$ 0.23	$ 0.24
Diluted	$ 0.22	$ 0.18	$ 0.22	$ 0.23

Reclassifications have been made to the 2005 and 2004 quarterly financial statements to conform to the current presentation.

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