

24 30235  
**Annual Report**

05

**Filings Services**  
April 7, 2006  
SNL Financial, LC  
1-800-969-4121

Central Valley  
**Community**  
Bankcorp





24 30235

**Annual Report**

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Central Valley  
Community  
Bancorp



# To Our Shareholders

## **2005: An Investment Year Yielded Excellent Results**

The year 2005 will be remembered as an extremely good year for Central Valley Community Bank, both in terms of financial performance and in the internal performance of the Bank. The year was highlighted by record earnings and significant growth in all areas of the Bank and in each of our markets, as the Bank completed its first full year of operation following the merger with Bank of Madera County. The Bank achieved all the benefits expected from the merger, and found the employees and customers in the Madera and Oakhurst markets to be even more outstanding than we could have hoped.

## **A Year Of Substantial Shareholder Value**

Central Valley Community Bancorp (CVCY) stock price appreciation performed better than most peers, not only in 2005, but for the past five years as indicated in the chart on page 7 of this report. We believe that the two-for-one stock split in October 2005 will encourage greater potential liquidity of CVCY stock and broaden its marketability to investors.

While the community bank sector has generally performed well overall, we believe banks that create an exceptional presence in good market areas, build fortress balance sheets and financially outperform their peers, will have better stock price performance over the long term. Our goal and direction is to meet these criteria by delivering quality performance and service through our outstanding team of bankers.

## **A Year Of Significant Branch Activity**

Central Valley Community Bank was quite active in 2005, adding offices in Madera and Oakhurst through the Bank of Madera County merger, and relocating the Clovis & Herndon office inside the expanded Save Mart Supermarket at Herndon & Fowler Avenues in Clovis. Construction was completed on the new Fresno Downtown office, which opened on February 13, 2006. In a continued effort to further enhance our service area and customer convenience, we have planned to relocate two current branch offices to larger spaces in 2006, and one new branch site has been targeted for possible expansion in the coming year.

## **A Year Of Added Convenience And Safety For Customers**

Our pursuit for new products to meet the financial needs of our customers and provide them with increased privacy continued through 2005. Privacy is one of our highest priorities and we continue to add software and controls to protect our customers. Three of the year's most noteworthy new products included the launch of Visa Travel Money, Visa Gift Card and Business Check Card. The Bank also enhanced customer convenience with BankLine (bank-by-phone) and

ATM/Check Cards allowing access to change passwords over the phone. Additionally, Internet banking will be enhanced and our web site will be completely upgraded in 2006. The Bank also anticipates establishing an interest in Central Valley Community Insurance Services, LLC. The purpose of this new entity is to market insurance products and services primarily to business customers in the area of employee benefit plans.

## **A Year Of Local Economic Improvement**

The overall economy in the Central Valley including Sacramento was generally very good in 2005. Unemployment in our core service areas fell below double-digit numbers for the first time in over two decades, and while these unemployment rates continue to run higher than the rest of the state, it is encouraging to see the benefits of added employment for the local economy. The driving force behind half of the job growth in 2005 can be attributed to the health of the construction industry, with the remainder of the job growth coming from various other sectors. One area that has seen diminishing job opportunities is the agriculture sector, due in part to increased automation. While the core market is still very dependent on agriculture, it is encouraging to see growth in manufacturing, logistics and healthcare along with the construction industry. Unfortunately, the net number of new companies in the Central Valley is not growing at the same pace as other parts of the state. However, there continue to be many initiatives at work to bring significant improvement in the quality of life and economic opportunity for the communities we call home. Our bank and employees are dedicated to helping improve those areas and are actively engaged in many of the organizations and efforts that are providing a better life for our community, our customers and our Company.

## **A Year Of Outstanding Earnings**

As mentioned earlier, 2005 was a record earnings year for Central Valley Community Bank. The 64% increase in net consolidated income was achieved from the successful merger with Bank of Madera County on December 31, 2004, as well as organic growth in loans and deposits throughout the Bank, and the benefits of the increasing interest rate environment. Loan growth increased 44%, with deposits increasing 32%. There was significant improvement in the net interest margin to 5.46% from 4.91%, and control of non-interest expense moving the Efficiency Ratio to 58.7% at year-end 2005 (compared to 69.2% for year-end 2004). Asset quality continued to be a strength for the Company, with non-performing loans at 0.2% of gross loans at year-end 2005. Also, for the sixth year in a row, the Bank was recognized as the largest SBA 504 lender in Fresno, Kings and Madera counties.

## *Investing In So Many Ways.*

At Central Valley Community Bank, we know the value of investing, and not just in the financial sense. In ways large and small, we're deeply invested in the communities we call home. From business owners to community leaders, local philanthropies to worthy projects, wherever good ideas need a helping hand to take root, we'll be there. Whatever it takes to make the Central Valley a better place to live, work and raise families. That was a forward-thinking philosophy when we were founded in 1980. And now, 26 years later, our commitment is stronger than ever. We thank our employees, our shareholders, our customers and our communities for the investment you've placed in us. We pledge to extend it to strengthen and improve the Central Valley for us all.



# *A 26-Year Tradition of Service & Dedication*

Central Valley Community Bancorp (the "Company") was established as the holding company for Central Valley Community Bank (the "Bank") on November 15, 2000, and is registered as a bank holding company with the Board of Governors of the Federal Reserve System. The Company currently conducts no operation other than through its ownership of the Bank. The common stock of the Company trades on the NASDAQ stock exchange under the symbol CVCY.

## **A History of Growth**

Central Valley Community Bank, founded in 1979 as Clovis Community Bank, is a California State chartered bank with deposit accounts insured by the Federal Deposit Insurance Corporation. The Bank commenced operations on January 10, 1980, in Clovis, California, with 12 professional bankers and beginning assets of \$2,000,000. Currently, the Bank operates ten full-service offices in Clovis, Fresno, Kerman, Madera, Oakhurst, Prather and Sacramento, plus Commercial, Real Estate, SBA and Agribusiness Lending Departments. Investment services are also provided by Investment Centers of America. Now with over 150 employees and assets of over \$483,000,000, Central Valley Community Bank has grown into a well-capitalized institution, with a proven track record of financial strength, security and stability. Yet despite the Bank's growth, it has remained true to its original "roots" – a commitment to the core values of integrity, trustworthiness, caring, loyalty, leadership and teamwork.

Central Valley Community Bank distinguishes itself from other financial institutions by providing superior client service and by remaining independent since opening 26 years ago. In recent years, the Bank has expanded its unique brand of personalized service by expanding its markets in the Central Valley and opening new offices in Sacramento,

Kerman, Madera, Oakhurst and Downtown Fresno. Guided by a hands-on board of directors and a seasoned senior management team, the Bank continues to focus on customer service and retention while remaining committed to the retention of high-quality employees.

## **Competitive Products, State-of-the-Art Convenience**

Central Valley Community Bank maintains state-of-the-art data processing and information systems, and offers a complete line of competitive business and personal deposit and loan products. For maximum convenience, personal and business Internet banking is available at [www.cvcb.com](http://www.cvcb.com) and 24-hour Automated Teller Machines (ATMs) are available at most Central Valley Community Bank offices. Additionally, BankLine 24-hour telephone banking is available to provide customer access to account information, deposit and withdrawal history, interest earned or paid, and the ability to transfer checking and savings funds via touch-tone phone.

## **"Relationship Banking" Means Service**

The Bank is committed to increasing and enhancing the products and services offered to customers, while emphasizing needs-based consulting within the branch environment. Serving both new and long-time customers continues to be an important factor in the Bank's growth as evidenced in ongoing customer referrals. Dependable values and security have always been important to America's banking customers, and the Bank is well-positioned to provide them, with an increased emphasis on privacy, security and convenience. The Bank takes protecting the privacy and security of customer information very seriously, as demonstrated by a range of expanded operational security measures. These include specialized software, procedures and helpful customer tools like the Bank's identity theft protection kit. All designed to give Central Valley Community Bank's customers maximum protection and peace of mind.

Central Valley Community Bank offers investment services provided by licensed representatives from the Investment Centers of America. The Bank's Real Estate Department provides comprehensive processing of residential and commercial interim construction loans, all types of single-family residential loans and other real-estate related transactions. The Bank supports small business growth and community job



Central Valley Community Bank  
Senior Management  
from left to right:

Shirley Wilburn  
Daniel J. Doyle  
Gayle Graham  
Gary Quisenberry  
Thomas L. Sommer.

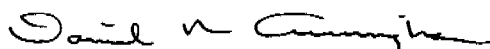
This level of performance would not be possible without a team of highly professional and dedicated employees focused on providing superior customer service. We expect our employees to be advocates for our customers, and it is a role we all take very seriously.

#### **A Year Of Change In The Banking Industry**

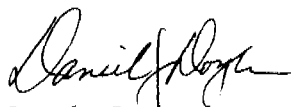
Competition continued to increase in our primary markets in 2005, with new start-up banks and branch expansion by other community banks. While the Fresno area is growing in population, the net number of new businesses is not growing as fast as some other regions. Since most community banks focus on business customers as their primary target, we expect there to be intense competition for this sector, and this could be reflected in pressure on pricing for the services we provide. However, we are not troubled by competition, and believe that with our strong local presence and team of committed employees, we can compete aggressively in the market. We also feel that we have positioned our balance sheet to allow flexibility for the potential interest rate trends in the coming year. We are optimistic for the Company's future and our ability to remain competitive and provide the best possible products and services for our customers, now and for years to come.

#### **A Bright Year Ahead**

As we move into 2006, we are encouraged by the economic strength we see in our markets for all of the sectors with which we work. Likewise, the Bank's geographic reach appears to be strong throughout the Central Valley and Foothills. We continue to look for opportunities to strengthen our presence in a prudent and long term approach that will allow us to grow with our customers, to enable our employees to invest in their careers, and to meet the needs of our communities. If we do all of these things well, we believe that you – our shareholders – will be rewarded. We thank you for your confidence and support, and we don't take them lightly; after all, we know you have many opportunities in which you can invest your funds. We are energized and optimistic about 2006, and about pursuing results we know can be achieved.



Daniel N. Cunningham  
Chairman of the Board



Daniel J. Doyle  
President and Chief Executive Officer

#### **Daniel N. Cunningham**

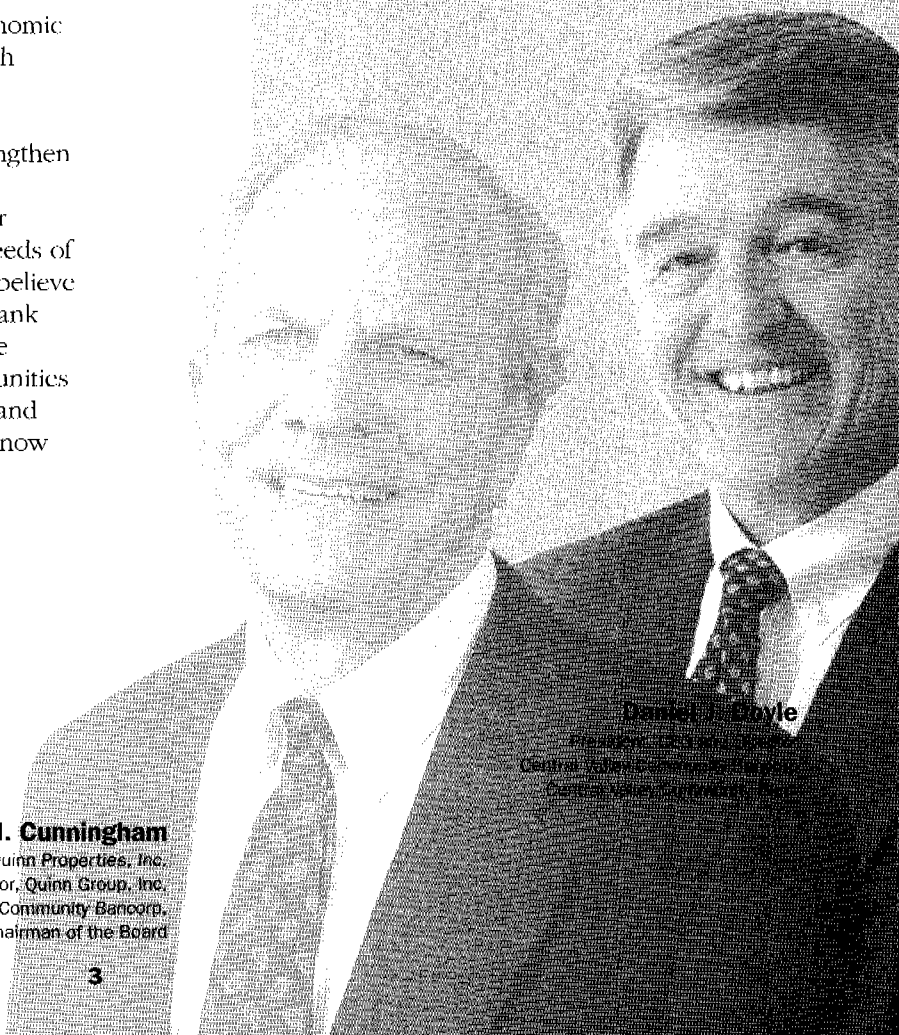
Vice President and Director, Quinn Properties, Inc.  
Director, Quinn Group, Inc.  
Central Valley Community Bancorp.  
Founding Director and Chairman of the Board

*Financial Strength,  
Security and Stability  
All from Central Valley  
Community Bancorp*

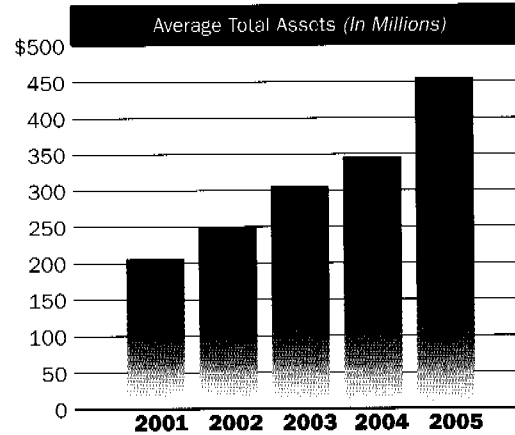
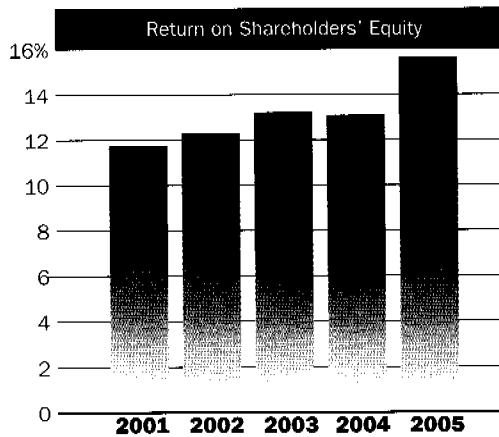
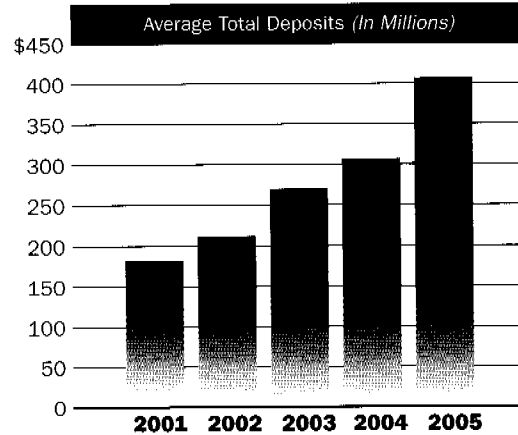
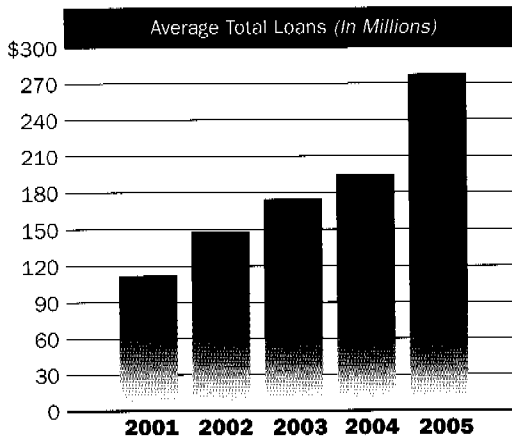
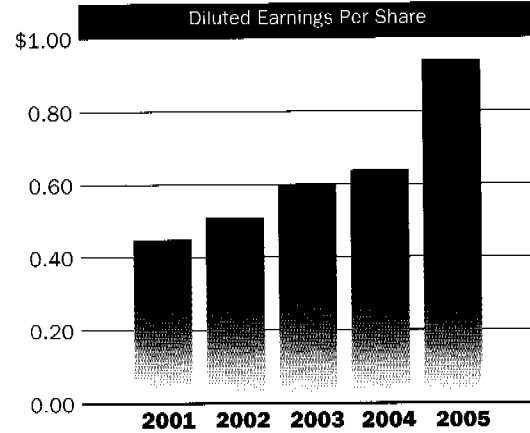
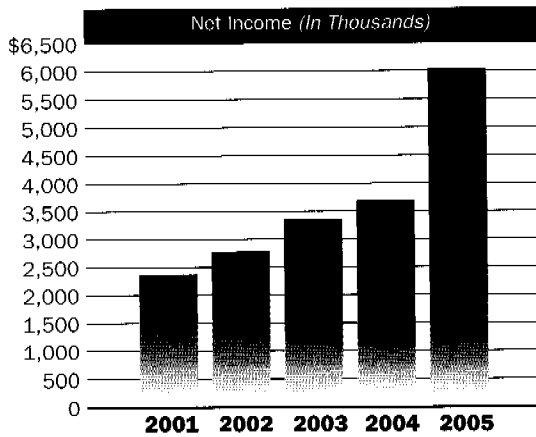
*Central Valley  
Community Bank*

*Investment Centers  
of America*

*Central Valley  
Community Insurance  
Services, LLC*



# Central Valley Community Bancorp Trend Analysis





creation, as evidenced by its certification in SBA's Preferred Lender Program, which allows for rapid loan response to local small business customers throughout the Central Valley. Central Valley Community Bank has been recognized for the sixth consecutive year as being the top lender in the Small Business Administration 504 loan program in the counties it serves. The Bank's participation in progressive and specialized lending programs for small businesses in all areas of the Central Valley demonstrates its ongoing commitment to building a stronger, healthier Valley economy.

Central Valley Community Bank has built a reputation for superior banking service by offering personalized "relationship banking" for businesses, professionals and individuals. Serving the business community has always been a primary focus for Central Valley Community Bank, and the Bank continues to expand its commercial banking team to enhance the level of service to even more individual and business customers. This sector is further served by courier service for business customers.

#### **"Community", It's More Than Just the Bank's Middle Name**

At Central Valley Community Bank, serving a community means more than just being in business there. More than meeting the material needs of its people. It means investing time, talent, and resources to make a community a strong and satisfying place to live. That's a role the Bank takes very seriously.

Which is why Central Valley Community Bank supports such a wide variety of local charities, agencies and philanthropies. From educational causes to disease research, the arts to the underprivileged, all are helped each year by Central Valley Community Bank. And not only with the Bank's financial support, but also with its people who generously volunteer their time to serve these important causes. Community is truly more than just the Bank's middle name.

#### **Strategic Vision**

Through the vision of our holding company, Central Valley Community Bancorp, and the leadership of its board of directors, the Bank has grown consistently over the past 26 years, keeping pace with the needs of its customers and its community. Now more than ever, Central Valley Community Bank is positioned to fulfill its mission of providing "common sense solutions" to its personal and business customers alike.

## *Investing in Communities Throughout the Valley*

### *Clovis*

- *Serving the area since 1980*
- *2 offices*
- *Population of 82,374*

### *Fresno*

- *Serving the area since 1995*
- *3 offices*
- *Population of 457,719*

### *Kerman*

- *Serving the area since 2002*
- *1 office*
- *Population of 10,238*

### *Madera*

- *Serving the area since 2005*
- *1 office*
- *Population of 50,043*

### *Oakhurst*

- *Serving the area since 2005*
- *1 office*
- *Population of 2,868*

### *Prather*

- *Serving the area since 1987*
- *1 office*
- *Population of 2,053*

### *Sacramento*

- *Serving the area since 2002*
- *1 office*
- *Population of 454,330*

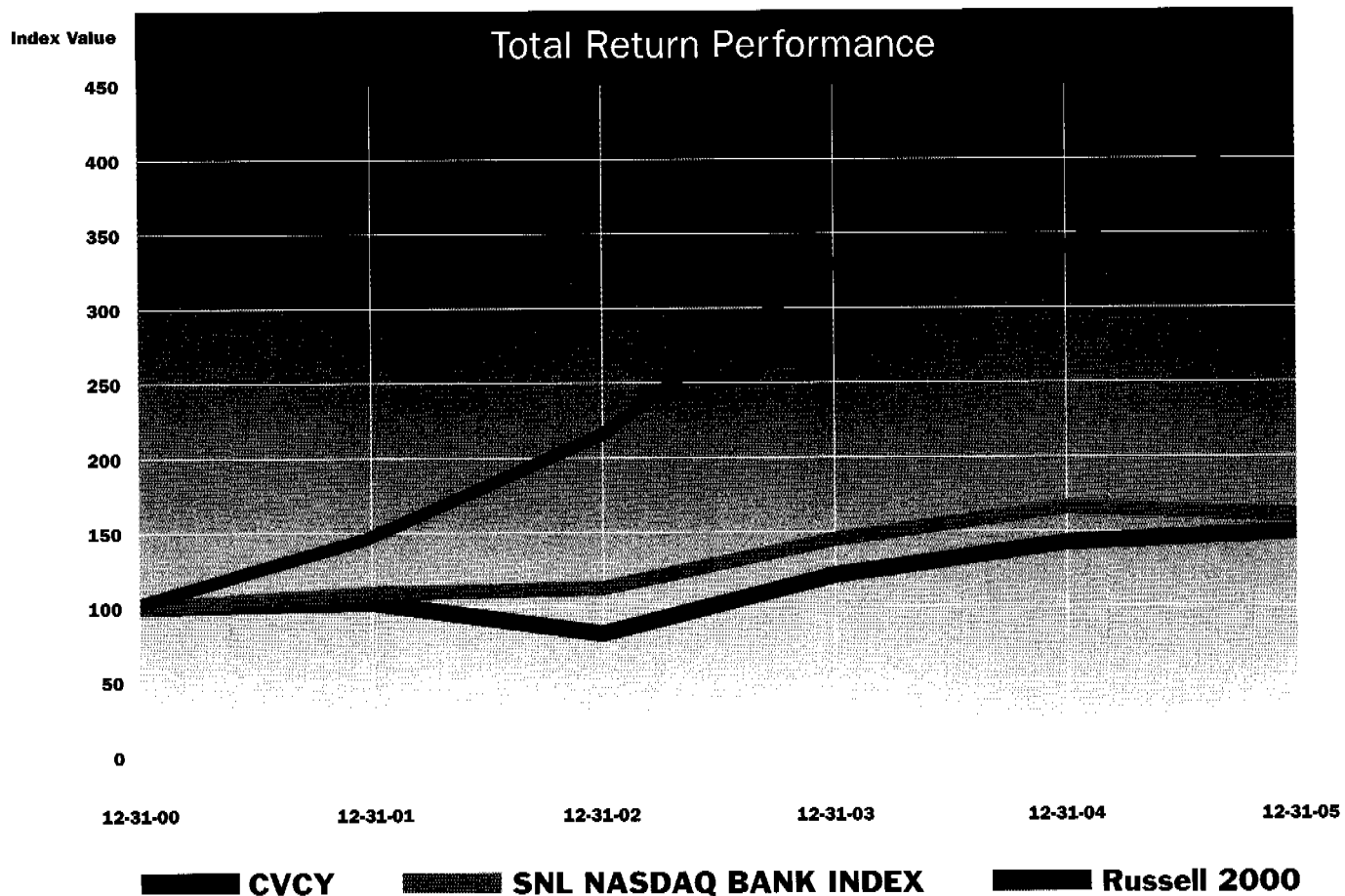
*\*Population based on U.S. Census  
2004 estimates*

# Consolidated Balance Sheet

December 31, 2005 and 2004 (In thousands, except share amounts)

| <b>ASSETS</b>  | <b>2005</b>       | <b>2004</b>       |
|--|-------------------|-------------------|
| Cash and due from banks  | \$ 22,165         | \$ 17,507         |
| Federal funds sold   | <u>29,830</u>     | <u>26,307</u>     |
| <b>Total cash and cash equivalents</b>   | 51,995            | 43,814            |
| Interest bearing deposits in other banks   | 918               | 2,605             |
| Available-for-sale investment securities (Notes 3 and 8)   | 105,592           | 98,983            |
| Loans, less allowance for credit losses of \$3,339<br>in 2005 and \$2,697 in 2004 (Notes 4, 10 and 14)   | 298,463           | 206,582           |
| Bank premises and equipment, net (Notes 6 and 10)  | 2,912             | 2,724             |
| Bank owned life insurance (Note 13)  | 6,725             | 6,075             |
| Federal Home Loan Bank stock   | 1,659             | 1,420             |
| Goodwill (Note 2)  | 8,955             | -                 |
| Intangible assets (Note 2)   | 1,286             | -                 |
| Accrued interest receivable and other assets (Note 9)  | <u>5,172</u>      | <u>5,944</u>      |
| <b>Total assets</b>  | <u>\$ 483,677</u> | <u>\$ 368,147</u> |
| <br><b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                   |                   |
| Deposits:  |                   |                   |
| Non-interest bearing   | \$ 153,004        | \$ 105,235        |
| Interest bearing (Note 7)  | <u>277,985</u>    | <u>220,951</u>    |
| <b>Total deposits</b>  | 430,989           | 326,186           |
| Short-term borrowings (Note 8)   | 3,250             | 2,000             |
| Long term debt (Note 8)  | 3,250             | 6,500             |
| Accrued interest payable and other liabilities (Note 13)   | <u>4,665</u>      | <u>3,855</u>      |
| <b>Total liabilities</b>   | <u>442,154</u>    | <u>338,541</u>    |
| Commitments and contingencies (Note 10)  |                   |                   |
| <b>Shareholders' equity (Note 11):</b>   |                   |                   |
| Preferred stock, no par value; 10,000,000 shares<br>authorized, no shares issued or outstanding  | -                 | -                 |
| Common stock, no par value; 80,000,000 shares<br>authorized, 5,891,820 and 5,257,734 shares issued<br>and outstanding in 2005 and 2004, respectively | 13,053            | 6,343             |
| Retained earnings  | 28,977            | 22,933            |
| Accumulated other comprehensive (loss) income, net of taxes<br>(Notes 3 and 15)  | <u>(507)</u>      | <u>330</u>        |
| <b>Total shareholders' equity</b>  | <u>41,523</u>     | <u>29,606</u>     |
| <b>Total liabilities and shareholders' equity</b>  | <u>\$ 483,677</u> | <u>\$ 368,147</u> |

The accompanying notes are an integral part of these consolidated financial statements.



Source: SNL Financial LC

Note: The stock price performance shown in the graphs above should not be indicative of potential future stock price performance.

# Consolidated Statement of Changes in Shareholders' Equity

For the Years Ended December 31, 2005, 2004 and 2003 (In thousands, except share and per share amounts)

|   | Common Stock |           | Retained Earnings | Accumulated Other Comprehensive Income (loss) (Net of Taxes) | Total Shareholders' Equity | Total Comprehensive Income |
|---|--------------|-----------|-------------------|--|----------------------------|----------------------------|
|   | Shares       | Amount    |                   |  |                            |                            |
| Balance, January 1, 2003  | 5,146,484    | \$ 5,854  | \$ 16,387         | \$ 1,858   | \$ 24,099                  |                            |
| Comprehensive income (Note 15):   |              |           |                   |  |                            |                            |
| Net income  |              |           | 3,372             |  | 3,372                      | \$ 3,372                   |
| Other comprehensive loss, net of tax:   |              |           |                   |  |                            |                            |
| Net change in unrealized gains on available-for-sale investment securities          |              |           |                   | (735)  | (735)                      | (735)                      |
| Total comprehensive income  |              |           |                   |  |                            | \$ 2,637                   |
| Cash dividend - \$.05 per share (Note 11)   |              |           | (258)             |  | (258)                      |                            |
| Stock options exercised and related tax benefit (Note 11)                           | 62,296       | 323       |                   |  | 323                        |                            |
| Repurchase and retirement of common stock (Note 11)                                 | (10,926)     | (81)      |                   |  | (81)                       |                            |
| Balance, December 31, 2003  | 5,197,854    | 6,096     | 19,501            | 1,123  | 26,720                     |                            |
| Comprehensive income (Note 15):   |              |           |                   |  |                            |                            |
| Net income  |              |           | 3,695             |  | 3,695                      | \$ 3,695                   |
| Other comprehensive loss, net of tax:   |              |           |                   |  |                            |                            |
| Net change in unrealized gains on available-for-sale investment securities          |              |           |                   | (793)  | (793)                      | (793)                      |
| Total comprehensive income  |              |           |                   |  |                            | \$ 2,902                   |
| Cash dividend - \$.05 per share (Note 11)   |              |           | (263)             |  | (263)                      |                            |
| Stock options exercised and related tax benefit (Note 11)                           | 77,880       | 460       |                   |  | 460                        |                            |
| Repurchase and retirement of common stock (Note 11)                                 | (18,000)     | (213)     |                   |  | (213)                      |                            |
| Balance, December 31, 2004  | 5,257,734    | 6,343     | 22,933            | 330  | 29,606                     |                            |
| Comprehensive income (Note 15):   |              |           |                   |  |                            |                            |
| Net income  |              |           | 6,044             |  | 6,044                      | \$ 6,044                   |
| Other comprehensive loss, net of tax:   |              |           |                   |  |                            |                            |
| Net change in unrealized gains on available-for-sale investment securities          |              |           |                   | (837)  | (837)                      | (837)                      |
| Total comprehensive income  |              |           |                   |  |                            | \$ 5,207                   |
| Stock issued for acquisition (Note 2)   | 522,106      | 6,079     |                   |  | 6,079                      |                            |
| Stock options exercised and related tax benefit (Note 11)                           | 111,980      | 631       |                   |  | 631                        |                            |
| Balance, December 31, 2005  | 5,891,820    | \$ 13,053 | \$ 28,977         | \$ (507)   | \$ 41,523                  |                            |
|   |              |           | <b>2005</b>       | <b>2004</b>  | <b>2003</b>                |                            |
| Disclosure of reclassification amount, net of taxes (Note 15):                      |              |           |                   |  |                            |                            |
| Unrealized holding losses arising during the year                                   |              |           | \$ (782)          | \$ (474)   | \$ (386)                   |                            |
| Less reclassification adjustment for net gains included in net income               |              |           | 55                | 319  | 349                        |                            |
| Net change in unrealized (losses) gains on available-for-sale investment securities |              |           | \$ (837)          | \$ (793)   | \$ (735)                   |                            |

The accompanying notes are an integral part of these consolidated financial statements.

# Consolidated Statement of Income

For the Years Ended December 31, 2005, 2004 and 2003 (In thousands, except per share amounts)

|   | 2005            | 2004            | 2003            |
|---|-----------------|-----------------|-----------------|
| <b>INTEREST INCOME:</b>   |                 |                 |                 |
| Interest and fees on loans  | \$ 21,115       | \$ 13,227       | \$ 12,039       |
| Interest on Federal funds sold  | 702             | 234             | 185             |
| Interest and dividends on investment securities:  |                 |                 |                 |
| Taxable   | 3,061           | 2,499           | 1,992           |
| Exempt from Federal income taxes  | 1,192           | 839             | 754             |
| <b>Total interest income</b>  | <u>26,070</u>   | <u>16,799</u>   | <u>14,970</u>   |
| <b>INTEREST EXPENSE:</b>  |                 |                 |                 |
| Interest on deposits (Note 7)   | 3,886           | 1,793           | 2,004           |
| Other (Note 8)  | 253             | 185             | 286             |
| <b>Total interest expense</b>   | <u>4,139</u>    | <u>1,978</u>    | <u>2,290</u>    |
| <b>Net interest income before provision for credit losses</b>                                 | 21,931          | 14,821          | 12,680          |
| <b>PROVISION FOR CREDIT LOSSES (NOTE 4)</b>   | 510             | -               | -               |
| <b>Net interest income after provision for credit losses</b>                                  | <u>21,421</u>   | <u>14,821</u>   | <u>12,680</u>   |
| <b>NON-INTEREST INCOME:</b>   |                 |                 |                 |
| Service charges   | 2,414           | 2,340           | 2,215           |
| Loan placement fees   | 390             | 330             | 488             |
| Appreciation in cash surrender value of bank owned life insurance (Note 13)                   | 215             | 200             | 303             |
| Net realized gains on sales and calls of investment securities (Note 3)                       | 92              | 483             | 506             |
| Federal Home Loan Bank stock dividends  | 68              | 41              | 28              |
| Rentals from equipment leased to others (Note 5)  | -               | 38              | 485             |
| Other income  | 581             | 505             | 521             |
| <b>Total non-interest income</b>  | <u>3,760</u>    | <u>3,937</u>    | <u>4,546</u>    |
| <b>NON-INTEREST EXPENSES:</b>   |                 |                 |                 |
| Salaries and employee benefits (Notes 4 and 13)   | 9,178           | 7,539           | 7,152           |
| Occupancy and equipment (Notes 6 and 10)  | 2,133           | 1,621           | 1,576           |
| Depreciation, net of reduction in allowance for losses on equipment leased to others (Note 5) | -               | 38              | 202             |
| Other expenses (Notes 10 and 12)  | 4,482           | 3,921           | 3,425           |
| <b>Total non-interest expenses</b>  | <u>15,793</u>   | <u>13,119</u>   | <u>12,355</u>   |
| <b>Income before provision for income taxes</b>   | 9,388           | 5,639           | 4,871           |
| <b>PROVISION FOR INCOME TAXES (NOTE 9)</b>  | 3,344           | 1,944           | 1,499           |
| <b>Net income</b>   | <u>\$ 6,044</u> | <u>\$ 3,695</u> | <u>\$ 3,372</u> |
| <b>Basic earnings per share (Note 11)</b>   | <u>\$ 1.03</u>  | <u>\$ 0.71</u>  | <u>\$ 0.65</u>  |
| <b>Diluted earnings per share (Note 11)</b>   | <u>\$ 0.94</u>  | <u>\$ 0.64</u>  | <u>\$ 0.60</u>  |

The accompanying notes are an integral part of these consolidated financial statements.

# Notes to Consolidated Financial Statements

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**General** - Central Valley Community Bancorp (the "Company") was incorporated on February 7, 2000 and subsequently obtained approval from the Board of Governors of the Federal Reserve System to be a bank holding company in connection with its acquisition of Central Valley Community Bank (the "Bank"). The Company became the sole shareholder of the Bank on November 15, 2000 in a statutory merger, pursuant to which each outstanding share of the Bank's common stock was exchanged for one share of common stock of the Company.

The Bank operates nine branches in Clovis, north Fresno, west and northeast Fresno County, Madera County, and Sacramento, California. The Bank's primary source of revenue is providing loans to customers who are predominately small and middle-market businesses and individuals. The Bank's subsidiaries have nominal activity with the exception of Central Valley Community Realty, LLC ("CVCR"). Effective April 15, 2005, CVCR was dissolved and no longer operates as a subsidiary of the Bank.

The accounting and reporting policies of Central Valley Community Bancorp and subsidiary conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Management has determined that since all of the banking products and services offered by the Company are available in each branch of the Bank, all branches are located within the same economic environment and management does not allocate resources based on the performance of different lending or transaction activities, it is appropriate to aggregate the Bank branches and report them as a single operating segment. No customer accounts for more than 10 percent of revenues for the Company or the Bank.

On September 21, 2005, the Company's Board of Directors approved a two-for-one stock split for shareholders of record at the close of business on October 5, 2005 and effective on October 31, 2005. All share and per share data in the consolidated financial statements have been retroactively restated to give effect to the stock split.

Certain reclassifications have been made to prior years' balances to conform to classifications used in 2005.

**Principles of Consolidation** - The consolidated financial statements include the accounts of the Company and the consolidated accounts of its wholly-owned subsidiary, the Bank. In addition, the accounts of the Bank's wholly owned subsidiaries, Clovest Corporation ("Clovest") and Clovis Securities Corporation (an inactive company), are included in the consolidated financial statements. The operating results of Clovest were not significant. All significant intercompany accounts and transactions have been eliminated in consolidation.

**Use of Estimates** - 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. These estimates and assumptions affect the reported amounts of 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 these estimates.

**Cash and Cash Equivalents** - For the purpose of the statement of cash flows, cash, due from banks and Federal funds sold are considered to be cash equivalents. Generally, Federal funds are sold for one-day periods.

**Investment Securities** - Investments are classified into the following categories:

- Available-for-sale securities, reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income (loss) within shareholders' equity.
- Held-to-maturity securities, which management has the positive intent and ability to hold to maturity, reported at amortized cost, adjusted for the accretion of discounts and amortization of premiums.

Management determines the appropriate classification of its investments at the time of purchase and may only change the classification in certain limited circumstances. All transfers between categories are accounted for at fair value. As of December 31, 2005 and 2004, all of the Company's investments were classified as available-for-sale.

Gains or losses on the sale of investment securities are computed on the specific identification method. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

Investment securities are evaluated for impairment on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in their value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Company to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

**Loans** - Loans are stated at principal balances outstanding. Interest is accrued daily based upon outstanding loan balances. However, when, in the opinion of management, loans are considered impaired and the future collectibility of interest and principal is in serious doubt, a loan is placed on nonaccrual status and the accrual of interest income is suspended. Any interest accrued but unpaid is charged against income. Payments received are applied to reduce principal to the extent necessary to ensure collection. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectibility of principal is not in doubt, are applied first to earned but unpaid interest and then to principal.

An impaired loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical matter, at the loan's observable market price or the fair value of collateral if the loan is collateral dependent. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due (including both principal and interest) in accordance with the contractual terms of the loan agreement. Interest income on impaired loans, if appropriate, is recognized on a cash basis.

Substantially all loan origination fees, commitment fees, direct loan origination costs and purchase premiums and discounts on loans are deferred and recognized as an adjustment of yield, to be amortized to interest income over the contractual term of the loan. The unamortized balance of deferred fees and costs is reported as a component of net loans.

The Company may acquire loans through a business combination or a purchase for which differences may exist between the contractual cash flows and the cash flows expected to be collected due, at least in part, to credit quality. When the Company acquires such loans, the yield that may be accreted (accretible yield) is limited to the excess of the Company's estimate of undiscounted cash flows expected to be collected over the Company's initial investment in the loan. The excess of contractual cash flows over cash flows expected to be collected may not be recognized as an adjustment to yield, loss, or a valuation allowance. Subsequent increases in cash flows expected to be collected generally should be recognized prospectively through adjustment of the loan's yield over its remaining life. Decreases in cash flows expected to be collected should be recognized as an impairment. The Company may not "carry over" or create a valuation allowance in the initial accounting for loans acquired under these circumstances. At December 31, 2005, there were no such loans being accounted for under this policy.

# Consolidated Statement of Cash Flows

For the Years Ended December 31, 2005, 2004 and 2003 (In thousands)

|   | 2005             | 2004             | 2003             |
|---|------------------|------------------|------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                  |                  |                  |
| Net income  | \$ 6,044         | \$ 3,695         | \$ 3,372         |
| Adjustments to reconcile net income to net cash provided by operating activities:                             |                  |                  |                  |
| Reduction in allowance for residual losses on equipment leased to others                                      | -                | -                | (203)            |
| Net increase (decrease) in deferred loan fees   | 94               | (150)            | 160              |
| Depreciation, accretion and amortization, net   | 2,368            | 2,106            | 2,851            |
| Provision for loan losses   | 510              | -                | -                |
| Net realized gains on sales and calls of available-for-sale investment securities                             | (92)             | (483)            | (506)            |
| (Gain) loss on sale of equipment  | (1)              | (1)              | 10               |
| Increase in bank owned life insurance, net of expenses  | (210)            | (196)            | (298)            |
| FHLB stock dividends  | (68)             | (41)             | (28)             |
| Net decrease (increase) in accrued interest receivable and other assets                                       | 1,889            | (2,307)          | (154)            |
| Net increase in accrued interest payable and other liabilities  | 546              | 354              | 155              |
| Provision for deferred income taxes   | (147)            | (409)            | (39)             |
| Net cash provided by operating activities   | <u>10,933</u>    | <u>2,568</u>     | <u>5,320</u>     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                  |                  |                  |
| Cash and cash equivalents acquired in acquisition   | 13,844           | -                | -                |
| Purchases of available-for-sale investment securities   | (50,046)         | (40,781)         | (65,192)         |
| Proceeds from sales or calls of available-for-sale investment securities                                      | 15,487           | 4,775            | 9,105            |
| Proceeds from maturity of available-for-sale investment securities  | -                | 4,500            | 1,630            |
| Proceeds from principal repayments of available-for-sale investment securities                                | 25,463           | 26,488           | 34,039           |
| Net decrease (increase) in interest bearing deposits in other banks   | 1,687            | (2,105)          | -                |
| Net FHLB stock (purchases) redemptions  | -                | (807)            | 115              |
| Net increase in loans   | (47,458)         | (22,583)         | (27,716)         |
| Purchases of premises and equipment   | (781)            | (539)            | (586)            |
| Proceeds from sale of equipment   | -                | 5                | -                |
| Purchases of bank owned life insurance  | (440)            | -                | -                |
| Net cash used in investing activities   | <u>(42,244)</u>  | <u>(31,047)</u>  | <u>(48,605)</u>  |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |                  |                  |                  |
| Net increase in demand, interest-bearing and savings deposits   | 32,000           | 38,466           | 40,743           |
| Net increase (decrease) in time deposits  | 9,034            | (2,845)          | 3,485            |
| Proceeds from borrowings from Federal Home Loan Bank  | -                | 6,000            | -                |
| Repayments to Federal Home Loan Bank  | (2,000)          | (7,000)          | (2,000)          |
| Proceeds from borrowings from other financial institutions  | -                | 2,500            | -                |
| Cash paid for dividends   | -                | (263)            | (258)            |
| Share repurchase and retirement   | -                | (213)            | (81)             |
| Proceeds from exercise of stock options   | 458              | 317              | 245              |
| Net cash provided by financing activities   | <u>39,492</u>    | <u>36,962</u>    | <u>42,134</u>    |
| Increase (decrease) in cash and cash equivalents  | 8,181            | 8,483            | (1,151)          |
| <b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>   | <u>43,814</u>    | <u>35,331</u>    | <u>36,482</u>    |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>   | <u>\$ 51,995</u> | <u>\$ 43,814</u> | <u>\$ 35,331</u> |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>  |                  |                  |                  |
| Cash paid during the year for:  |                  |                  |                  |
| Interest expense  | \$ 3,947         | \$ 2,000         | \$ 2,327         |
| Income taxes  | \$ 3,223         | \$ 2,409         | \$ 1,080         |
| <b>NON-CASH INVESTING ACTIVITIES:</b>   |                  |                  |                  |
| Net change in unrealized (loss) gain on available-for sale investment securities                              | \$ (1,407)       | \$ (1,090)       | \$ (1,080)       |
| <b>NON-CASH FINANCING ACTIVITIES:</b>   |                  |                  |                  |
| Tax benefit from stock options exercised  | \$ 173           | \$ 143           | \$ 78            |
| <b>SUPPLEMENTAL SCHEDULE RELATED TO ACQUISITION:</b>  |                  |                  |                  |
| Acquisition of Bank of Madera County:   |                  |                  |                  |
| Deposits  | \$ 63,769        |                  |                  |
| Other liabilities   | 439              |                  |                  |
| Loans, net  | (45,028)         |                  |                  |
| Goodwill and intangibles  | (10,455)         |                  |                  |
| Premises and equipment  | (390)            |                  |                  |
| Federal Home Loan Bank stock  | (172)            |                  |                  |
| Other assets  | (398)            |                  |                  |
| Stock issued  | 6,079            |                  |                  |
| Cash and cash equivalents acquired, net of cash paid to Bank of Madera County shareholders and option holders | <u>\$ 13,844</u> |                  |                  |

The accompanying notes are an integral part of these consolidated financial statements.

# Notes to Consolidated Financial Statements

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Impact of New Financial Accounting Standards - (continued)

On November 3, 2005, the FASB issued FASB Staff Position (FSP) Nos. FAS 115-1 and FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. This FSP addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. This FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. This FSP nullifies certain requirements of EITF Issue 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*. The guidance in this FSP amends FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. The FSP is effective for reporting periods beginning after December 15, 2005. The Company does not anticipate any material impact to its financial condition or results of operations as a result of the adoption of this guidance.

### Share Based Payments

In December 2004, the FASB issued Statement No. 123 (revised 2004) (FAS 123 (R)), *Share-Based Payments*. FAS 123 (R) requires all entities to recognize compensation expense in an amount equal to the fair value of share-based payments such as stock options granted to employees. The Company may elect to adopt FAS 123 (R) using a modified prospective method or modified retrospective method. Under the modified retrospective method, the Company would restate previously issued financial statements, basing the compensation expense on that previously reported in their pro forma disclosures required by FAS 123. The modified prospective method would require the Company to record compensation expense for the unvested portion of previously granted awards that remain outstanding at the date of adoption as these awards continue to vest. FAS 123 (R) is effective for the first fiscal year beginning after June 15, 2005. Management has elected to use the modified prospective method and has completed its evaluation of the effect of FAS 123 (R), and does not expect it to have a material impact on its financial position or results of operations.

### Accounting Changes and Error Corrections

On June 7, 2005, the FASB issued Statement No. 154 (FAS 154), *Accounting Changes and Error Corrections - a replacement of Accounting Principles Board (APB) Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements*. Under the provisions of FAS 154, voluntary changes in accounting principles are applied retrospectively to prior periods' financial statements unless it would be impractical to do so. FAS 154 supersedes APB Opinion No. 20, which required that most voluntary changes in accounting principles be recognized by including in the current period's net income the cumulative effect of the change. FAS 154 also makes a distinction between "retrospective application" of a change in accounting principle and the "restatement" of financial statements to reflect the correction of an error. The provisions of FAS 154 are effective for accounting changes made in fiscal years beginning after December 15, 2005. Management of the Company does not expect the adoption of this standard to have a material impact on its financial position or results of operations.

## 2. MERGER OF BANK OF MADERA COUNTY INTO CENTRAL VALLEY COMMUNITY BANCORP

After the close of business on December 31, 2004, the Company and Bank of Madera County (BMC) completed their previously announced merger and BMC was merged into the Bank. The Company acquired 100% of the outstanding common shares of BMC and the results of BMC's operations have been included in the consolidated financial statements beginning January 1, 2005. Management believes that the merger will allow the Bank to further accommodate a growing customer base in Madera County and provide BMC customers with more convenient locations in the Central Valley, as well as offer new advancement and geographic opportunities for their employees. As a result of the above factors, management believes that the potential for the combined performance exceeds what each entity could accomplish independently and the goodwill in this transaction arose from the synergies associated with the merger. The acquisition is part of the Company's long-term strategy to increase its presence from Sacramento to Bakersfield along the Highway 99 corridor and the surrounding foothills.

As of the date of acquisition, BMC had total assets of \$68,080,000, comprised of \$2,842,000 in cash and due from banks, \$19,250,000 in Federal funds sold, \$45,028,000 in loans (net of allowance for credit losses of \$751,000), \$390,000 in premises and equipment and \$570,000 in other assets. Total liabilities acquired amounted to \$64,208,000, including \$63,769,000 in deposits.

The total consideration paid to BMC shareholders and option holders was approximately \$14,311,000 which was comprised of \$1,911,000 in cash payments to holders of outstanding BMC stock options, \$6,200,000 in cash and 522,106, split adjusted, shares of the Company's common stock (valued at \$6,200,000 for purposes of the merger agreement). Total consideration paid to BMC shareholders was established under the terms of the merger agreement based on a value of \$26.22 per share of BMC common stock.

The excess of the purchase price over the estimated fair value of the net assets acquired was \$8,955,000, which was recorded as goodwill, is not subject to amortization, and is not expected to be deductible for tax purposes. In addition, assets acquired also included a core deposit intangible of \$1,500,000 which is being amortized using a straight-line method over a period of seven years with no significant residual value. Amortization expense recognized in 2005 was \$214,000.

The accompanying consolidated financial statements include the accounts of BMC since January 1, 2005. The following supplemental pro forma information discloses selected financial information for the periods indicated as though the BMC merger had been completed as of the beginning of each of the periods being reported. Dollars are in thousands except per share data. 2004 pro forma net income includes non-recurring merger expenses for legal, accounting and other professional fees, net of tax, totaling \$602,000.

|                            | Year Ended December 31, |           |
|----------------------------|-------------------------|-----------|
|                            | 2005                    | 2004      |
| Revenue                    | \$ 29,830               | \$ 24,475 |
| Net income                 | \$ 6,044                | \$ 3,153  |
| Diluted earnings per share | \$ 0.94                 | \$ 0.50   |



# Notes to Consolidated Financial Statements

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

**Allowance for Credit Losses** - The allowance for credit losses is maintained to provide for losses related to impaired loans and other losses that can be expected to occur in the normal course of business. The determination of the allowance is based on estimates made by management, to include consideration of the character of the loan portfolio, specifically identified problem loans, potential losses inherent in the portfolio taken as a whole and economic conditions in the Bank's service area.

Classified loans and loans determined to be impaired are individually evaluated by management for specific risk of loss. In addition, a reserve factor is assigned to currently performing loans based on the Bank's historical loss experience. Management also computes specific and expected loss reserves for loan commitments. These estimates are susceptible to changes in the economic environment and market conditions.

The Bank's Audit Committee reviews the adequacy of the allowance for credit losses quarterly, to include consideration of the relative risks in the portfolio, current economic conditions and other factors. The allowance is adjusted based on that review if, in the judgment of the Audit Committee and management, changes are warranted.

This allowance is established through a provision for credit losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. The allowance for credit losses at December 31, 2005 and 2004, respectively, reflects management's estimate of potential losses in the portfolio.

**Bank Premises and Equipment** - Bank premises and equipment are carried at cost. Depreciation is determined using the straight line method over the estimated useful lives of the related assets. The useful lives of Bank premises are estimated to be between twenty and forty years. The useful lives of improvements to Bank premises, furniture, fixtures and equipment are estimated to be three to ten years. Leasehold improvements are amortized over the life of the asset or the term of the related lease, whichever is shorter. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred.

The Bank evaluates premises and equipment for financial impairment as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

**Income Taxes** - The Company files its income taxes on a consolidated basis with its subsidiary. The allocation of income tax expense (benefit) represents each entity's proportionate share of the consolidated provision for income taxes.

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. On the balance sheet, net deferred tax assets are included in accrued interest receivable and other assets.

**Stock-Based Compensation** - The Company has three stock-based compensation plans, the Central Valley Community Bancorp 2005 Omnibus Incentive Plan and 2000 and 1992 Stock Option Plans. The Company accounts for these plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. No stock-based compensation cost is reflected in net income, as all options granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

In February 2005, the Company accelerated the vesting of 186,000 options previously granted to certain directors and executive officers. The pro forma consolidated net earnings and earnings per share information for the year ended December 31, 2005, presented in the table below, reflects the acceleration. No stock based compensation cost is reflected in net income as a result of the acceleration of the vesting as it is expected

that generally all of the directors and executive management whose options were accelerated will remain with the Company through the original vesting period.

Pro forma adjustments to the Company's consolidated net earnings and earnings per share are disclosed during the years in which the options become vested.

|  | 2005                                     | 2004            | 2003            |
|--|--|-----------------|-----------------|
|  | (In thousands, except per share amounts) |                 |                 |
| Net income, as reported  | \$ 6,044                                 | \$ 3,695        | \$ 3,372        |
| Deduct: Total stock-based compensation expense determined under the fair value based method for all awards, net of related tax effects | 513                                      | 250             | 205             |
| Pro forma net income   | <u>\$ 5,531</u>                          | <u>\$ 3,445</u> | <u>\$ 3,167</u> |
| Basic earnings per share - as reported   | \$ 1.03                                  | \$ 0.71         | \$ 0.65         |
| Basic earnings per share - pro forma   | \$ 0.95                                  | \$ 0.66         | \$ 0.61         |
| Diluted earnings per share - as reported   | \$ 0.94                                  | \$ 0.64         | \$ 0.60         |
| Diluted earnings per share - pro forma   | \$ 0.87                                  | \$ 0.60         | \$ 0.57         |
| Weighted average fair value of options granted during the year   | \$ 6.56                                  | \$ 9.60         | \$ 5.84         |

The fair value of each option is estimated on the date of grant using an option-pricing model with the following assumptions:

|                         | 2005      | 2004     | 2003           |
|-------------------------|-----------|----------|----------------|
| Dividend yield          | .5%       | .5%      | .5%            |
| Expected volatility     | 50.29%    | 66.27%   | 65.4 to 72.77% |
| Risk-free interest rate | 4.16%     | 4.17%    | 2.05 to 3.18%  |
| Expected option life    | 6.5 years | 10 years | 10 years       |

**Earnings Per Share** - Basic earnings per share (EPS), which excludes dilution, is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which shares in the earnings of the Company. All data with respect to computing earnings per share is retroactively adjusted to reflect stock dividends and splits and the treasury stock method is applied to determine the dilutive effect of stock options in computing diluted EPS.

### Impact of New Financial Accounting Standards -

#### Other-Than-Temporary Impairment of Securities

In March 2004, the Financial Accounting Standards Board (FASB) and Emerging Issues Task Force (EITF) reached consensus on several issues being addressed in EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. The consensus provides guidance for evaluating whether an investment is other-than-temporarily impaired and was effective for other-than-temporary impairment evaluations made in reporting periods beginning after June 15, 2004. The disclosure provisions of EITF Issue No. 03-1 continue to be effective for the Company's consolidated financial statements for the year ended December 31, 2005.

# Notes to Consolidated Financial Statements

## 4. LOANS AND ALLOWANCE FOR CREDIT LOSSES

Outstanding loans are summarized as follows:

|  | December 31,      |                   |
|--|-------------------|-------------------|
|  | 2005              | 2004              |
|  | (In thousands)    |                   |
| Commercial   | \$ 82,978         | \$ 57,669         |
| Real estate  | 124,043           | 75,424            |
| Real estate – construction, land development<br>and other land loans | 46,523            | 35,364            |
| Equity lines of credit   | 23,604            | 18,714            |
| Agricultural   | 17,547            | 15,946            |
| Installment  | 7,539             | 6,420             |
| Other  | 160               | 240               |
|  | <u>302,394</u>    | <u>209,777</u>    |
| Deferred loan fees, net  | (592)             | (498)             |
| Allowance for credit losses  | <u>(3,339)</u>    | <u>(2,697)</u>    |
|  | <u>\$ 298,463</u> | <u>\$ 206,582</u> |

At December 31, 2005 and 2004, loans originated under Small Business Administration (SBA) programs totaling \$27,760,000 and \$24,311,000, respectively, were included in the real estate and commercial categories.

Salaries and employee benefits totaling \$495,000, \$354,000 and \$214,000 have been deferred as loan origination costs for the years ended December 31, 2005, 2004 and 2003, respectively.

Changes in the allowance for credit losses were as follows:

|  | Year Ended December 31, |                 |                 |
|--|-------------------------|-----------------|-----------------|
|  | 2005                    | 2004            | 2003            |
|  | (In thousands)          |                 |                 |
| Balance, beginning of year                               | \$ 2,697                | \$ 2,425        | \$ 2,433        |
| Provision charged to operations                          | 510                     | -               | -               |
| Losses charged to the allowance                          | (787)                   | (24)            | (217)           |
| Recoveries   | 168                     | 296             | 209             |
| Allowance acquired in merger of<br>Bank of Madera County | 751                     | -               | -               |
| Balance, end of year                                     | <u>\$ 3,339</u>         | <u>\$ 2,697</u> | <u>\$ 2,425</u> |

There were two loans considered to be impaired at December 31, 2005 totaling \$616,000. There were no loans considered to be impaired at December 31, 2004. There was no required valuation allowance for these impaired loans. The average investment in impaired loans during 2005, 2004 and 2003 was \$776,000, \$36,000 and \$651,000, respectively. No interest income was recognized for impaired loans in 2005, 2004 or 2003.

At December 31, 2005, nonaccrual loans totaled \$616,000 and interest foregone on nonaccrual loans totaled \$76,000 for the year then ended. There were no loans on nonaccrual at December 31, 2004 or interest foregone on nonaccrual loans for the year then ended. Interest foregone on nonaccrual loans totaled \$27,000 for the year ended December 31, 2003.

## 5. EQUIPMENT LEASED TO OTHERS

Prior to 2003, the Bank entered into leasing arrangements through certain leasing brokers to lease computer equipment to various entities. During 2004, the remaining leases matured and the underlying equipment was fully depreciated. As a result, there was no recorded investment in equipment leased to others at December 31, 2005 and 2004. Rental income for the years ended December 31, 2004 and 2003 was \$38,000 and \$485,000, respectively. Depreciation expense, net of the reduction in provision for allowance for losses on equipment, was \$38,000 and \$202,000 for 2004 and 2003, respectively.

## 6. BANK PREMISES AND EQUIPMENT

Bank premises and equipment consisted of the following:

|   | December 31,    |                 |
|---|-----------------|-----------------|
|   | 2005            | 2004            |
|   | (In thousands)  |                 |
| Land  | \$ 250          | \$ 250          |
| Buildings and improvements                        | 1,161           | 1,161           |
| Furniture, fixtures and equipment                 | 4,693           | 3,862           |
| Leasehold improvements                            | 1,718           | 1,702           |
|   | <u>7,822</u>    | <u>6,975</u>    |
| Less accumulated depreciation<br>and amortization | <u>(4,910)</u>  | <u>(4,251)</u>  |
|   | <u>\$ 2,912</u> | <u>\$ 2,724</u> |

Depreciation and amortization included in occupancy and equipment expense totaled \$982,000, \$796,000 and \$721,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

## 7. DEPOSITS

Interest-bearing deposits consisted of the following:

|                         | December 31,      |                   |
|-------------------------|-------------------|-------------------|
|                         | 2005              | 2004              |
|                         | (In thousands)    |                   |
| Savings                 | \$ 24,389         | \$ 20,518         |
| Money market            | 108,024           | 89,904            |
| NOW accounts            | 56,991            | 52,571            |
| Time, \$100,000 or more | 48,670            | 25,854            |
| Time, under \$100,000   | 39,911            | 32,104            |
|                         | <u>\$ 277,985</u> | <u>\$ 220,951</u> |

Aggregate annual maturities of time deposits are as follows (in thousands):

| Year Ending December 31, |                  |
|--------------------------|------------------|
| 2006                     | \$ 70,615        |
| 2007                     | 13,002           |
| 2008                     | 547              |
| 2009                     | 2,796            |
| 2010                     | 1,621            |
|                          | <u>\$ 88,581</u> |

# Notes to Consolidated Financial Statements

## 3. AVAILABLE-FOR-SALE INVESTMENT SECURITIES

The amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2005 and 2004 consisted of the following:

|   | 2005              |                        |                         |                      |
|---|-------------------|------------------------|-------------------------|----------------------|
|   | Amortized Cost    | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
| (In thousands)  |                   |                        |                         |                      |
| Debt securities:  |                   |                        |                         |                      |
| U.S. Government agencies  | \$ 23,314         | \$ -                   | \$ (658)                | \$ 22,656            |
| Obligations of states and political subdivisions                | 31,036            | 371                    | (473)                   | 30,934               |
| U.S. Government agencies collateralized by mortgage obligations | 48,479            | 237                    | (285)                   | 48,431               |
| Other securities  | 3,608             | -                      | (37)                    | 3,571                |
|   | <u>\$ 106,437</u> | <u>\$ 608</u>          | <u>\$ (1,453)</u>       | <u>\$ 105,592</u>    |

|   | 2004             |                        |                         |                      |
|---|------------------|------------------------|-------------------------|----------------------|
|   | Amortized Cost   | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
| (In thousands)  |                  |                        |                         |                      |
| Debt securities:  |                  |                        |                         |                      |
| U.S. Government agencies  | \$ 22,492        | \$ 119                 | \$ (267)                | \$ 22,344            |
| Obligations of states and political subdivisions                | 19,993           | 637                    | (121)                   | 20,509               |
| U.S. Government agencies collateralized by mortgage obligations | 52,292           | 466                    | (255)                   | 52,503               |
| Other securities  | 3,644            | -                      | (17)                    | 3,627                |
|   | <u>\$ 98,421</u> | <u>\$ 1,222</u>        | <u>\$ (660)</u>         | <u>\$ 98,983</u>     |

Investment securities with unrealized losses at December 31, 2005 are summarized and classified according to the duration of the loss period as follows:

|   | Less than 12 Months |                   | 12 Months or More |                   | Total            |                   |
|---|---------------------|-------------------|-------------------|-------------------|------------------|-------------------|
|   | Fair Value          | Unrealized Losses | Fair Value        | Unrealized Losses | Fair Value       | Unrealized Losses |
| (In thousands)  |                     |                   |                   |                   |                  |                   |
| Debt securities:  |                     |                   |                   |                   |                  |                   |
| U.S. Government agencies  | \$ 2,939            | \$ (55)           | \$ 19,717         | \$ (603)          | \$ 22,656        | \$ (658)          |
| Obligations of states and political subdivisions                | 13,646              | (270)             | 4,181             | (203)             | 17,827           | (473)             |
| U.S. Government agencies collateralized by mortgage obligations | 19,473              | (161)             | 9,887             | (124)             | 29,360           | (285)             |
| Other securities  | 1,463               | (37)              | -                 | -                 | 1,463            | (37)              |
|   | <u>\$ 37,521</u>    | <u>\$ (523)</u>   | <u>\$ 33,785</u>  | <u>\$ (930)</u>   | <u>\$ 71,306</u> | <u>\$ (1,453)</u> |

At December 31, 2005, the Company held 143 investment securities of which 50 were in a loss position for less than twelve months and 24 were in a loss position and had been in a loss position for twelve months or more. Management periodically evaluates each investment security for other than temporary impairment, relying primarily on industry analyst reports and observation of market conditions and interest rate fluctuations. Management believes it will be able to collect all amounts due according to the contractual terms of the underlying investment securities and that the noted decline in fair value is considered temporary and due only to interest rate fluctuations.

Net unrealized (losses) gains on available-for-sale investment securities totaling \$(845,000) and \$562,000 are recorded net of \$338,000 and \$(232,000) in tax benefit (expense) as accumulated other comprehensive (loss) income within shareholders' equity at December 31, 2005 and 2004, respectively.

Proceeds and gross realized gains from sales or calls of available-for-sale investment securities totaled \$15,487,000 and \$92,000, respectively, for the year ended December 31, 2005. Proceeds and gross realized gains from sales or calls of available-for-sale investment securities totaled \$4,775,000 and \$483,000, respectively, for the year ended December 31, 2004. Proceeds and gross realized gains from sales or calls of available-for-sale investment securities totaled \$9,105,000 and \$506,000, respectively, for the year ended December 31, 2003.

The amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2005 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

|   | Amortized Cost    | Estimated Fair Value |
|---|-------------------|----------------------|
| (In thousands)  |                   |                      |
| Within one year   | \$ 997            | \$ 986               |
| After one year through five years                               | 26,347            | 25,712               |
| After five years through ten years                              | 12,705            | 12,521               |
| After ten years   | 14,301            | 14,338               |
|   | 54,350            | 53,590               |
| Investment securities not due at a single maturity date:        |                   |                      |
| U.S. Government agencies collateralized by mortgage obligations | 48,479            | 48,431               |
| Other securities  | 3,608             | 3,571                |
|   | <u>\$ 106,437</u> | <u>\$ 105,592</u>    |

Investment securities with amortized costs totaling \$27,877,000 and \$30,248,000 and fair values totaling \$27,800,000 and \$30,807,000 were pledged to secure public deposits, other contractual obligations, short-term borrowings and long-term debt at December 31, 2005 and 2004, respectively.

# Notes to Consolidated Financial Statements

## 9. INCOME TAXES (Continued)

The provision for income taxes differs from amounts computed by applying the statutory Federal income tax rates to operating income before income taxes. The significant items comprising these differences for the years ended December 31, 2005, 2004 and 2003 consisted of the following:

|  | 2005          | 2004          | 2003          |
|--|---------------|---------------|---------------|
| Federal income tax, at statutory rate          | 34.0 %        | 34.0 %        | 34.0 %        |
| State franchise tax, net of Federal tax effect | 7.1 %         | 7.1 %         | 6.1 %         |
| Tax exempt investment security income, net     | (4.2)%        | (4.9)%        | (5.1)%        |
| Bank owned life insurance, net                 | (0.9)%        | (1.4)%        | (2.2)%        |
| Other  | (0.4)%        | (0.3)%        | (2.0)%        |
| Total income tax expense                       | <u>35.6 %</u> | <u>34.5 %</u> | <u>30.8 %</u> |

## 10. COMMITMENTS AND CONTINGENCIES

**Leases** - The Bank leases certain of its branch facilities and administrative offices under noncancelable operating leases. Rental expense included in occupancy and equipment and other expenses totaled \$518,000, \$359,000 and \$334,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

Future minimum lease payments on noncancelable operating leases are as follows (in thousands):

| Year Ending December 31, |                 |
|--------------------------|-----------------|
| 2006                     | \$ 600          |
| 2007                     | 522             |
| 2008                     | 475             |
| 2009                     | 365             |
| 2010                     | 307             |
| Thereafter               | <u>624</u>      |
|                          | <u>\$ 2,893</u> |

**Federal Reserve Requirements** Banks are required to maintain reserves with the Federal Reserve Bank equal to a percentage of their reservable deposits. The amount of such reserve balances required at December 31, 2005 and 2004 was \$1,385,000 and \$753,000, respectively.

**Correspondent Banking Agreements** - The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. Uninsured deposits totaled \$5,098,000 at December 31, 2005.

**Financial Instruments With Off-Balance-Sheet Risk** - The Bank is a party to financial instruments with off balance sheet risk in the normal course of business in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of 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 on the balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and standby letters of credit as it does for loans included on the balance sheet.

The following financial instruments represent off-balance-sheet credit risk:

|                              | December 31,   |            |
|------------------------------|----------------|------------|
|                              | 2005           | 2004       |
|                              | (In thousands) |            |
| Commitments to extend credit | \$ 133,876     | \$ 106,561 |
| Standby letters of credit    | \$ 80          | \$ 1,255   |

Commitments to extend credit consist primarily of unfunded single-family residential and commercial real estate construction loans and commercial revolving lines of credit. Construction loans are established under standard underwriting guidelines and policies and are secured by deeds of trust, with disbursements made over the course of construction. Commercial revolving lines of credit have a high degree of industry diversification. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Standby letters of credit are generally secured and are issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to customers. The fair value of the liability related to these standby letters of credit, which represents the fees received for issuing the guarantees, was not significant at December 31, 2005 and 2004. The Company recognizes these fees as revenue over the term of the commitment or when the commitment is used.

At December 31, 2005, commercial loan commitments represent approximately 52% of total commitments and are generally secured by collateral other than real estate or unsecured. Real estate loan commitments represent 37% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 80%. Consumer loan commitments represent the remaining 11% of total commitments and are generally unsecured. In addition, the majority of the Bank's loan commitments have variable interest rates.

**Concentrations of Credit Risk** - At December 31, 2005, in management's judgment, a concentration of loans existed in commercial loans and real-estate-related loans. At that date, approximately 91.7% of the Bank's loans were commercial and real-estate-related, representing 27.5% and 64.2% of total loans, respectively.

At December 31, 2004, in management's judgment, a concentration of loans existed in commercial loans and real-estate-related loans. At that date, approximately 89.2% of the Bank's loans were commercial and real-estate-related, representing 27.5% and 61.7% of total loans, respectively.

Although management believes the loans within these concentrations have no more than the normal risk of collectibility, a substantial decline in the performance of the economy in general or a decline in real estate values in the Company's primary market area, in particular, could have an adverse impact on collectibility, increase the level of real-estate-related nonperforming loans, or have other adverse effects which alone or in the aggregate could have a material adverse effect on the financial condition of the Company.

**Contingencies** - During 2005, the Company wrote down its investment in a title and insurance company by an additional \$100,000 to its estimated fair value of \$250,000. This investment is included in accrued interest receivable and other assets in the consolidated balance sheet. The title and insurance company was sold in 2005. To date, the Company has received \$176,000 from the sale. The Company anticipates full recovery of the balance of the investment.

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

# Notes to Consolidated Financial Statements

## 7. DEPOSITS (Continued)

Interest expense recognized on interest-bearing deposits consisted of the following:

|                              | Year Ended December 31, |                 |                 |
|------------------------------|-------------------------|-----------------|-----------------|
|                              | 2005                    | 2004            | 2003            |
|                              | (In thousands)          |                 |                 |
| Savings                      | \$ 89                   | \$ 67           | \$ 66           |
| Money market                 | 1,500                   | 660             | 659             |
| NOW accounts                 | 60                      | 51              | 49              |
| Time certificates of deposit | 2,237                   | 1,015           | 1,230           |
|                              | <u>\$ 3,886</u>         | <u>\$ 1,793</u> | <u>\$ 2,004</u> |

## 8. BORROWING ARRANGEMENTS

### Federal Home Loan Bank Advances

Advances from the Federal Home Loan Bank (FHLB) of San Francisco at December 31, 2005 and 2004 consisted of the following:

| 2005                   |       |                         | 2004                   |       |                         |
|------------------------|-------|-------------------------|------------------------|-------|-------------------------|
| Amount                 | Rate  | Maturity Date           | Amount                 | Rate  | Maturity Date           |
| (Dollars in thousands) |       |                         | (Dollars in thousands) |       |                         |
| \$ 2,000               | 2.10% | Feb. 13, 2006           | \$ 2,000               | 1.38% | Feb. 11, 2005           |
| 2,000                  | 2.66% | Feb. 12, 2007           | 2,000                  | 2.10% | Feb. 13, 2006           |
|                        |       |                         | 2,000                  | 2.66% | Feb. 12, 2007           |
| 4,000                  |       |                         | 6,000                  |       |                         |
| (2,000)                |       | Less short-term portion | (2,000)                |       | Less short-term portion |
| <u>\$ 2,000</u>        |       | Long-term debt          | <u>\$ 4,000</u>        |       | Long-term debt          |

FHLB advances are secured by investment securities with amortized costs totaling \$6,680,000 and \$9,668,000 and market values totaling \$6,598,000 and \$9,822,000 at December 31, 2005 and 2004, respectively. The Bank's credit limit varies according to the amount and composition of the investment and loan portfolios pledged as collateral.

**Other Long Term Debt** - The Company has a note payable to a financial institution with a balance of \$2,500,000 at December 31, 2005. The note bears a variable interest rate of LIBOR plus 2.5% (6.56% as of December 31, 2005). Payment terms call for interest only payments based on the financial institution's prime rate or LIBOR at the Company's discretion. Payments are due on March 31, June 30, September 30 and December 31, 2006. Beginning on March 31, 2006, one-eighth (1/8) of the principal is due with each quarterly payment, along with all accrued interest. The remaining principal and accrued interest is due when the note matures on December 31, 2007. The note is secured by 20% of the issued and outstanding stock of the Company's subsidiary bank (Central Valley Community Bank) with the value of pledged stock to be not less than 200% of the outstanding principal balance.

Other long term debt matures as follows:

| Year Ending December 31, |                     |
|--------------------------|---------------------|
| 2006                     | \$ 1,250,000        |
| 2007                     | 1,250,000           |
|                          | <u>\$ 2,500,000</u> |

**Lines of Credit** - The Bank had unsecured lines of credit with its correspondent banks which, in the aggregate, amounted to \$14,100,000 and \$10,100,000 at December 31, 2005 and 2004, respectively, at interest rates which vary with market conditions. The Bank also had a line of credit with the Federal Reserve Bank of San Francisco at December 31, 2005 and 2004 which bears interest at the prevailing discount rate collateralized by investment securities with amortized costs totaling \$3,350,000 and \$3,504,000 and market values totaling \$3,252,000 and \$3,456,000, respectively. At December 31, 2005 and 2004, the Bank had no outstanding borrowings under these lines of credit.

## 9. INCOME TAXES

The provision for income taxes for the years ended December 31, 2005, 2004 and 2003 consisted of the following:

|                            | Federal         | State         | Total           |
|----------------------------|-----------------|---------------|-----------------|
|                            | (In thousands)  |               |                 |
| <b>2005</b>                |                 |               |                 |
| Current                    | \$ 2,512        | \$ 979        | \$ 3,491        |
| Deferred                   | (72)            | (75)          | (147)           |
| Provision for income taxes | <u>\$ 2,440</u> | <u>\$ 904</u> | <u>\$ 3,344</u> |
| <b>2004</b>                |                 |               |                 |
| Current                    | \$ 1,719        | \$ 634        | \$ 2,353        |
| Deferred                   | (313)           | (96)          | (409)           |
| Provision for income taxes | <u>\$ 1,406</u> | <u>\$ 538</u> | <u>\$ 1,944</u> |
| <b>2003</b>                |                 |               |                 |
| Current                    | \$ 1,258        | \$ 280        | \$ 1,538        |
| Deferred                   | (96)            | 57            | (39)            |
| Provision for income taxes | <u>\$ 1,162</u> | <u>\$ 337</u> | <u>\$ 1,499</u> |

Deferred tax assets (liabilities) consisted of the following:

|   | December 31,    |                 |
|---|-----------------|-----------------|
|   | 2005            | 2004            |
|   | (In thousands)  |                 |
| <b>Deferred tax assets:</b>                                 |                 |                 |
| Allowance for credit losses                                 | \$ 768          | \$ 539          |
| Other reserves  | 122             | 111             |
| Bank premises and equipment                                 | 271             | 153             |
| Deferred compensation                                       | 1,199           | 1,003           |
| Future benefit of State deferred tax liability              | 300             | 92              |
| Unrealized loss on available-for-sale investment securities | 388             | -               |
| State net operating loss                                    | 80              | -               |
| Total deferred tax assets                                   | <u>3,078</u>    | <u>1,898</u>    |
| <b>Deferred tax liabilities:</b>                            |                 |                 |
| Other accruals  | (118)           | (157)           |
| Unrealized gain on available-for-sale investment securities | -               | (232)           |
| Future liability of State deferred tax asset                | (157)           | -               |
| Core deposit intangible                                     | (577)           | -               |
| Total deferred tax liabilities                              | <u>(852)</u>    | <u>(389)</u>    |
| Net deferred tax assets                                     | <u>\$ 2,226</u> | <u>\$ 1,509</u> |

# Notes to Consolidated Financial Statements

## 11. SHAREHOLDERS' EQUITY (Continued)

### Stock Options - (continued)

On November 15, 2000, the Company adopted, and subsequently amended on December 20, 2000, the Central Valley Community Bancorp 2000 Stock Option Plan for which 1,085,290 shares remain reserved for issuance for options already granted to employees and directors under incentive and nonstatutory agreements and 62,426 remain reserved for future grants. The plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the option price must be paid in full at the time it is exercised. The options under the plan expire on dates determined by the Board of Directors, but not later than ten years from the date of grant. The vesting period is determined by the Board of Directors and is generally over five years.

In March 2005, the Company adopted the Central Valley Community Bancorp 2005 Omnibus Incentive Plan. The plan provides for awards in the form of incentive stock options, non-statutory stock options, stock appreciation rights, and restricted stock. The plan also allows for performance awards that may be in the form of cash or shares of the Company, including restricted stock. The maximum number of shares that can be issued with respect to all awards under the plan is 476,000. The plan requires that the exercise price may not be less than 100% of the fair market value of the stock at the date the option is granted, and that the option price must be paid in full at the time it is exercised. The options and awards under the plan expire on dates determined by the Board of Directors, but not later than ten years from the date of grant. The vesting period for the options and option related stock appreciation rights is determined by the Board of Directors and is generally over five years. There were no grants under this plan in 2005.

A summary of the combined activity of the plans, adjusted to give effect to stock splits, follows:

|  | 2005                                      |         | 2004                                      |         | 2003                                      |         |
|--|---|---------|---|---------|---|---------|
|  | Weighted<br>Average<br>Exercise<br>Shares | Price   | Weighted<br>Average<br>Exercise<br>Shares | Price   | Weighted<br>Average<br>Exercise<br>Shares | Price   |
| Options outstanding, beginning of year | 1,052,860                                 | \$ 4.69 | 1,131,580                                 | \$ 4.64 | 1,062,176                                 | \$ 4.01 |
| Options granted                        | 156,300                                   | \$13.50 | 1,000                                     | \$11.30 | 156,200                                   | \$ 8.61 |
| Options exercised                      | (111,980)                                 | \$ 4.08 | (77,880)                                  | \$ 4.04 | (62,296)                                  | \$ 3.93 |
| Options canceled                       | (11,890)                                  | \$ 8.86 | (1,840)                                   | \$ 6.34 | (24,500)                                  | \$ 4.45 |
| Options outstanding, end of year       | <u>1,085,290</u>                          | \$ 5.97 | <u>1,052,860</u>                          | \$ 4.69 | <u>1,131,580</u>                          | \$ 4.64 |
| Options exercisable, end of year       | <u>841,770</u>                            | \$ 4.62 | <u>681,760</u>                            | \$ 4.19 | <u>574,800</u>                            | \$ 3.99 |

A summary of options outstanding at December 31, 2005 follows:

| Range of Exercise Prices | Number of<br>Options<br>Outstanding<br>December 31,<br>2005 | Weighted<br>Average<br>Remaining<br>Contractual<br>Life | Number of<br>Options<br>Exercisable<br>December 31,<br>2005 |
|--------------------------|---|---|---|
| \$3.25 to \$3.88         | 410,760   | 4.64 years  | 386,650   |
| \$4.32 to \$5.02         | 308,560   | 3.84 years  | 287,200   |
| \$5.38 to \$7.75         | 69,800  | 6.65 years  | 53,600  |
| \$8.63 to \$13.50        | <u>296,170</u>  | 8.54 years  | <u>114,320</u>  |
|                          | <u>1,085,290</u>  |   | <u>841,770</u>  |

## 12. OTHER EXPENSES

Other expenses consisted of the following:

|   | Year Ended December 31, |                 |                 |
|---|-------------------------|-----------------|-----------------|
|   | 2005                    | 2004            | 2003            |
|   | (in thousands)          |                 |                 |
| Data processing                         | \$ 707                  | \$ 663          | \$ 684          |
| Advertising                             | 412                     | 365             | 360             |
| Audit and accounting fees               | 334                     | 244             | 222             |
| Amortization of core deposit intangible | 214                     | -               | -               |
| Legal fees                              | 192                     | 129             | 101             |
| Regulatory assessments                  | 164                     | 92              | 74              |
| Other expenses                          | <u>2,459</u>            | <u>2,428</u>    | <u>1,984</u>    |
|   | <u>\$ 4,482</u>         | <u>\$ 3,921</u> | <u>\$ 3,425</u> |

## 13. EMPLOYEE BENEFITS

**401(k) and Profit Sharing Plan** - The Bank has established a 401(k) and profit sharing plan. The 401(k) plan covers substantially all employees who have completed a six month period in which they are credited with at least 1,000 hours of service. Participants in the profit sharing plan are eligible to receive employer contributions after completion of two years of service. Bank contributions to the profit sharing plan are determined at the discretion of the Board of Directors. Participants are automatically vested 100% in all employer contributions. The Bank contributed \$275,000, \$105,000 and \$120,000 to the profit sharing plan in 2005, 2004 and 2003, respectively.

Additionally, the Bank may elect to make a matching contribution to the participants' 401(k) plan accounts. The amount to be contributed is announced by the Bank at the beginning of the plan year. For the years ended December 31, 2005, 2004 and 2003, the Bank made a 100% matching contribution on all deferred amounts up to 3% of eligible compensation and a 50% matching contribution on all deferred amounts above 3% to a maximum of 5%. For the years ended December 31, 2005, 2004 and 2003, the Bank made matching contributions totaling \$210,000, \$188,000 and \$157,000, respectively.

**Deferred Compensation Plan** - The Bank has a nonqualified Deferred Compensation Plan which provides directors and a former key executive with an unfunded, deferred compensation program. Under the plan, eligible participants may elect to defer some or all of their current compensation or director fees. Deferred amounts earn interest at an annual rate determined by the Board of Directors (6.25% at December 31, 2005). At December 31, 2005 and 2004, the total net deferrals included in accrued interest payable and other liabilities were \$1,285,000 and \$1,190,000, respectively.

In connection with the implementation of the above plan, single premium universal life insurance policies on the life of each participant were purchased by the Bank, which is beneficiary and owner of the policies. The cash surrender value of the policies totaled \$3,921,000 and \$3,801,000 at December 31, 2005 and 2004, respectively. The current annual tax-free interest rates on these policies is 5.2%. Income recognized on these policies, net of related expenses, for the years ended December 31, 2005, 2004 and 2003 totaled \$120,000, \$111,000 and \$171,000, respectively.

# Notes to Consolidated Financial Statements

## 11. SHAREHOLDERS' EQUITY

**Regulatory Capital** - The Company and the Bank are subject to certain regulatory requirements administered by the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation (FDIC). Failure to meet these minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's and the Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets. Each of these components is defined in the regulations. Management believes that the Company and the Bank meet all their capital adequacy requirements as of December 31, 2005.

In addition, the most recent notification from the FDIC 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 below. There are no conditions or events since that notification that management believes have changed the Bank's category.

|  | 2005      |        | 2004      |        |
|--|-----------|--------|-----------|--------|
|  | Amount    | Ratio  | Amount    | Ratio  |
| (Dollars in thousands)                                 |           |        |           |        |
| <b>Tier 1 Leverage Ratio</b>                           |           |        |           |        |
| Central Valley Community Bancorp and Subsidiary        | \$ 31,767 | 6.84%  | \$ 29,259 | 8.03%  |
| Minimum regulatory requirement                         | \$ 18,572 | 4.00%  | \$ 14,574 | 4.00%  |
| Central Valley Community Bank                          | \$ 32,493 | 7.00%  | \$ 29,913 | 8.24%  |
| Minimum requirement for "Well-Capitalized" institution | \$ 23,204 | 5.00%  | \$ 18,155 | 5.00%  |
| Minimum regulatory requirement                         | \$ 18,563 | 4.00%  | \$ 14,524 | 4.00%  |
| <b>Tier 1 Risk-Based Capital Ratio</b>                 |           |        |           |        |
| Central Valley Community Bancorp and Subsidiary        | \$ 31,767 | 9.26%  | \$ 29,259 | 11.55% |
| Minimum regulatory requirement                         | \$ 13,719 | 4.00%  | \$ 10,137 | 4.00%  |
| Central Valley Community Bank                          | \$ 32,493 | 9.48%  | \$ 29,913 | 11.83% |
| Minimum requirement for "Well-Capitalized" institution | \$ 20,572 | 6.00%  | \$ 15,166 | 6.00%  |
| Minimum regulatory requirement                         | \$ 13,715 | 4.00%  | \$ 10,111 | 4.00%  |
| <b>Total Risk-Based Capital Ratio</b>                  |           |        |           |        |
| Central Valley Community Bancorp and Subsidiary        | \$ 35,106 | 10.24% | \$ 31,956 | 12.61% |
| Minimum regulatory requirement                         | \$ 27,437 | 8.00%  | \$ 20,273 | 8.00%  |
| Central Valley Community Bank                          | \$ 35,832 | 10.45% | \$ 32,610 | 12.90% |
| Minimum requirement for "Well-Capitalized" institution | \$ 34,287 | 10.00% | \$ 25,277 | 10.00% |
| Minimum regulatory requirement                         | \$ 27,429 | 8.00%  | \$ 20,222 | 8.00%  |

**Dividends** - The Company did not pay any cash dividends in 2005.

On May 19, 2004, the Board of Directors declared a \$.05 per share cash dividend for shareholders of record as of June 4, 2004, paid on or about June 30, 2004. On May 21, 2003, the Board of Directors declared a \$.05 per share cash dividend to shareholders of record as of June 2, 2003, paid on or about June 30, 2003.

The Company's primary source of income with which to pay cash dividends is dividends from the Bank. The California Financial Code restricts the total amount of dividends payable by a bank at any time without obtaining the prior approval of the California Department of Financial Institutions to the lesser of (1) the bank's retained earnings or (2) the bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. At December 31, 2005, retained earnings of \$13,389,000 were free of such restrictions.

**Share Repurchase Plan** - During 2004 and 2003, the Company approved stock repurchase plans authorizing the purchase of shares up to a total cost of \$500,000, or approximately 2% of its common stock, in each year. As of December 31, 2004 and 2003, the Company repurchased 18,000 and 10,926 shares at a total cost of \$213,000 and \$81,000, respectively. On October 20, 2004, the Company's Board of Directors suspended the stock repurchase program.

**Earnings Per Share** - A reconciliation of the numerators and denominators of the basic and diluted earnings per share computations is as follows

|  | Year Ended December 31, |           |           |
|--|-------------------------|-----------|-----------|
|  | 2005                    | 2004      | 2003      |
| (In thousands, except share and per share amounts)                   |                         |           |           |
| <b>Basic Earnings Per Share:</b>                                     |                         |           |           |
| Net income   | \$ 6,044                | \$ 3,695  | \$ 3,372  |
| Weighted average shares outstanding                                  | 5,844,110               | 5,253,658 | 5,172,704 |
| Net income per share   | \$ 1.03                 | \$ 0.71   | \$ 0.65   |
| <b>Diluted Earnings Per Share:</b>                                   |                         |           |           |
| Net income   | \$ 6,044                | \$ 3,695  | \$ 3,372  |
| Weighted average shares outstanding                                  | 5,844,110               | 5,253,658 | 5,172,704 |
| Effect of dilutive stock options                                     | 571,298                 | 585,252   | 484,972   |
| Weighted average shares of common stock and common stock equivalents | 6,415,408               | 5,838,910 | 5,657,676 |
| Net income per diluted share   | \$ 0.94                 | \$ 0.64   | \$ 0.60   |

**Stock Options** - During 1992, the Bank established a Stock Option Plan for which shares are reserved for issuance to employees and directors under incentive and nonstatutory agreements. The Company assumed all obligations under this plan as of November 15, 2000, and options to purchase shares of the Company's common stock were substituted for options to purchase shares of common stock of the Bank. Outstanding options under this plan are exercisable until their expiration; however, no new options will be granted under this plan.

# Notes to Consolidated Financial Statements

## 16. DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Available-for-sale investment securities and interest-bearing deposits in other banks - For available-for-sale investment securities and interest-bearing deposits in other banks, fair values are based on quoted market prices, where available. If quoted market prices are not available, fair values are estimated using quoted market prices for similar securities and deposits and indications of value provided by brokers.

Loans - For variable rate loans that reprice frequently with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates being offered at each reporting date for loans with similar terms to borrowers of comparable creditworthiness adjusted for the allowance for credit losses. The carrying amount of accrued interest receivable approximates its fair value.

Bank owned life insurance - The fair value of bank owned life insurance policies is based on cash surrender values at each reporting date as provided by the insurers.

Federal Home Loan Bank stock - The carrying amount of Federal Home Loan Bank (FHLB) stock approximates fair value. This investment is carried at cost and is redeemable at par with certain restrictions.

Deposits - The fair values for demand deposits are, by definition, equal to the amount payable on demand at the reporting date represented by their carrying amount. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow analysis using interest rates being offered at each reporting date by the Bank for certificates with similar remaining maturities. The carrying amount of accrued interest payable approximates its fair value.

Short-term borrowings and long-term debt - The fair values of fixed-rate borrowings are estimated by discounting their future cash flows using rates at each reporting date for similar instruments.

Commitments to extend credit and letters of credit - Off-balance-sheet commitments to extend credit are primarily for adjustable rate loans. For these commitments, there are no differences between the committed amounts and their fair values. Commitments to fund fixed rate loans and standby letters of credit are at rates which approximate fair value at each reporting date.

|   | December 31, 2005 |            | December 31, 2004 |            |
|---|-------------------|------------|-------------------|------------|
|   | Carrying Amount   | Fair Value | Carrying Amount   | Fair Value |
|   | (In thousands)    |            |                   |            |
| <b>Financial assets:</b>                        |                   |            |                   |            |
| Cash and due from banks                         | \$ 22,165         | \$ 22,165  | \$ 17,507         | \$ 17,507  |
| Federal funds sold                              | 29,830            | 29,830     | 26,307            | 26,307     |
| Interest-bearing deposits in other banks        | 918               | 918        | 2,605             | 2,605      |
| Available-for-sale investment securities        | 105,592           | 105,592    | 98,983            | 98,983     |
| Loans   | 298,463           | 298,261    | 206,582           | 211,393    |
| Bank owned life insurance                       | 6,725             | 6,725      | 6,075             | 6,075      |
| FHLB stock                                      | 1,659             | 1,659      | 1,420             | 1,420      |
| Accrued interest receivable                     | 2,232             | 2,232      | 1,413             | 1,413      |
| <b>Financial liabilities:</b>                   |                   |            |                   |            |
| Deposits  | \$ 430,989        | \$ 429,153 | \$ 326,186        | \$ 308,325 |
| Short-term borrowings                           | 3,250             | 3,250      | 2,000             | 2,000      |
| Long-term debt                                  | 3,250             | 3,144      | 6,500             | 6,310      |
| Accrued interest payable                        | 394               | 394        | 202               | 202        |
| <b>Off balance-sheet financial instruments:</b> |                   |            |                   |            |
| Commitments to extend credit                    | \$ 133,876        | \$ 133,876 | \$ 106,561        | \$ 106,561 |
| Standby letters of credit                       | 80                | 80         | 1,255             | 1,255      |

## 17. PARENT ONLY CONDENSED FINANCIAL STATEMENTS

### CONDENSED BALANCE SHEET December 31, 2005 and 2004 (In thousands)

|  | 2005      | 2004      |
|--|-----------|-----------|
| <b>ASSETS</b>  |           |           |
| Cash and cash equivalents                            | \$ 1,205  | \$ 709    |
| Investment in subsidiary                             | 42,249    | 30,261    |
| Other assets   | 639       | 1,257     |
| Total assets   | \$ 44,093 | \$ 32,227 |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>          |           |           |
| <b>Liabilities:</b>                                  |           |           |
| Short-term debt                                      | \$ 1,250  | \$ -      |
| Long-term debt                                       | 1,250     | 2,500     |
| Other liabilities                                    | 70        | 121       |
| Total liabilities                                    | 2,570     | 2,621     |
| <b>Shareholders' equity:</b>                         |           |           |
| Common stock   | 13,053    | 6,343     |
| Retained earnings                                    | 28,977    | 22,933    |
| Accumulated other comprehensive income, net of taxes | (507)     | 330       |
| Total shareholders' equity                           | 41,523    | 29,606    |
| Total liabilities and shareholders' equity           | \$ 44,093 | \$ 32,227 |



# Notes to Consolidated Financial Statements

## 13. EMPLOYEE BENEFITS (Continued)

**Salary Continuation Plans** The Board of Directors approved salary continuation plans for certain key executives during 2002. Under these plans, the Bank is obligated to provide the executives with annual benefits for fifteen years after retirement. These benefits are substantially equivalent to those available under split-dollar life insurance policies purchased by the Bank on the life of the executives. In addition, the estimated present value of these future benefits are accrued from the effective date of the plans until the executives' expected retirement date based on a discount rate of 6.25%. The expense recognized under these plans for the years ended December 31, 2005, 2004 and 2003 totaled \$332,000, \$285,000 and \$256,000, respectively. Accrued compensation payable under the salary continuation plan totaled \$1,293,000 and \$968,000 at December 31, 2005 and 2004, respectively.

In connection with these plans, the Bank purchased single premium life insurance policies with cash surrender values totaling \$2,804,000 and \$2,274,000 at December 31, 2005 and 2004, respectively. Income recognized on these policies, net of related expense, for the years ended December 31, 2005, 2004 and 2003 totaled \$90,000, \$85,000 and \$90,000, respectively.

## 14. LOANS TO RELATED PARTIES

During the normal course of business, the Bank enters into loans with related parties, including executive officers and directors. These loans are made with substantially the same terms, including rates and collateral, as loans to unrelated parties. The following is a summary of the aggregate activity involving related party borrowers (in thousands):

|  |                 |
|--|-----------------|
| Balance, January 1, 2005   | \$ 420          |
| Disbursements  | 212             |
| Amounts repaid   | <u>(185)</u>    |
| Balance, December 31, 2005                                       | <u>\$ 447</u>   |
| Undisbursed commitments to related parties,<br>December 31, 2005 | <u>\$ 1,485</u> |

## 15. COMPREHENSIVE INCOME

Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of other comprehensive income (loss) that historically has not been recognized in the calculation of net income. The Company's only source of other comprehensive income (loss) is unrealized gains and losses on the Company's available-for-sale investment securities. Total comprehensive income and the components of accumulated other comprehensive income (loss) are presented in the consolidated statement of changes in shareholders' equity.

At December 31, 2005, 2004 and 2003, the Company held securities classified as available-for-sale which had net unrealized gains or losses as follows:

|   | Before<br>Tax     | Tax<br>(Expense)<br>Benefit<br>(In thousands) | After<br>Tax    |
|---|-------------------|---|-----------------|
| <b>For the Year Ended December 31, 2005</b>                                 |                   |   |                 |
| Other comprehensive loss:   |                   |   |                 |
| Unrealized holding losses   | \$ (1,315)        | \$ 533  | \$ (782)        |
| Less reclassification<br>adjustment for net gains<br>included in net income | <u>92</u>         | <u>(37)</u>                                   | <u>55</u>       |
| Total other<br>comprehensive loss   | <u>\$ (1,407)</u> | <u>\$ 570</u>                                 | <u>\$ (837)</u> |
| <b>For the Year Ended December 31, 2004</b>                                 |                   |   |                 |
| Other comprehensive loss:   |                   |   |                 |
| Unrealized holding losses   | \$ (607)          | \$ 133  | \$ (474)        |
| Less reclassification<br>adjustment for net gains<br>included in net income | <u>483</u>        | <u>(164)</u>                                  | <u>319</u>      |
| Total other<br>comprehensive loss   | <u>\$ (1,090)</u> | <u>\$ 297</u>                                 | <u>\$ (793)</u> |
| <b>For the Year Ended December 31, 2003</b>                                 |                   |   |                 |
| Other comprehensive loss:   |                   |   |                 |
| Unrealized holding gains  | \$ (574)          | \$ 188  | \$ (386)        |
| Less reclassification<br>adjustment for net gains<br>included in net income | <u>506</u>        | <u>(157)</u>                                  | <u>349</u>      |
| Total other<br>comprehensive loss   | <u>\$ (1,080)</u> | <u>\$ 345</u>                                 | <u>\$ (735)</u> |

## 16. DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

Disclosures include estimated fair values for financial instruments for which it is practicable to estimate fair value. These estimates are made at a specific point in time based on relevant market data and information about the financial instruments. These estimates do not reflect any premium or discount that could result from offering the Company's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the fair values presented.

The following methods and assumptions were used by the Company to estimate the fair value of its financial instruments at December 31, 2005 and 2004:

**Cash and cash equivalents** - For cash and cash equivalents, the carrying amount is estimated to be fair value.

# *Report Of Independent Registered Public Accounting Firm*

The Shareholders and Board of Directors  
Central Valley Community Bancorp and Subsidiary

We have audited the accompanying consolidated balance sheet of Central Valley Community Bancorp and subsidiary as of December 31, 2005 and 2004 and the related consolidated statements of income, changes in shareholders' equity 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 Company'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 audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 provided a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Central Valley Community Bancorp and subsidiary as of December 31, 2005 and 2004 and the consolidated 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 accounting principles generally accepted in the United States of America.



Sacramento, California  
January 25, 2006

# Notes to Consolidated Financial Statements

## 17. PARENT ONLY CONDENSED FINANCIAL STATEMENTS (Continued)

### CONDENSED STATEMENT OF INCOME

For the Years Ended December 31, 2005, 2004 and 2003

(In thousands)

|   | 2005            | 2004            | 2003            |
|---|-----------------|-----------------|-----------------|
| Income:   |                 |                 |                 |
| Dividends declared by subsidiary - eliminated in consolidation    | \$ -            | \$ 593          | \$ -            |
| Other income  | 1               | -               | 42              |
| Total income  | <u>1</u>        | <u>593</u>      | <u>42</u>       |
| Expenses:   |                 |                 |                 |
| Professional fees   | 106             | 96              | 62              |
| Other expenses  | 500             | 378             | 184             |
| Total expenses  | <u>606</u>      | <u>474</u>      | <u>246</u>      |
| Income (loss) before equity in undistributed income of subsidiary | (605)           | 119             | (204)           |
| Equity in undistributed net income of subsidiary                  | <u>6,438</u>    | <u>3,419</u>    | <u>3,532</u>    |
| Income before income taxes  | 5,833           | 3,538           | 3,328           |
| Income tax benefit  | <u>211</u>      | <u>157</u>      | <u>44</u>       |
| Net income  | <u>\$ 6,044</u> | <u>\$ 3,695</u> | <u>\$ 3,372</u> |

### CONDENSED STATEMENT OF CASH FLOWS

For the Years Ended December 31, 2005, 2004 and 2003

(In thousands)

|   | 2005            | 2004          | 2003          |
|---|-----------------|---------------|---------------|
| Cash flows from operating activities:   |                 |               |               |
| Net income  | \$ 6,044        | \$ 3,695      | \$ 3,372      |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                 |               |               |
| Undistributed net income of subsidiary  | (6,438)         | (3,419)       | (3,532)       |
| Decrease (increase) in other assets   | 792             | (316)         | (47)          |
| (Decrease) increase in liabilities  | <u>(51)</u>     | <u>47</u>     | <u>(22)</u>   |
| Net cash provided by (used in) operating activities   | <u>347</u>      | <u>7</u>      | <u>(229)</u>  |
| Cash flows used in investing activities:  |                 |               |               |
| Investment in subsidiary  | (309)           | (2,000)       | -             |
| Cash flows from financing activities:   |                 |               |               |
| Proceeds from borrowings  | -               | 2,500         | -             |
| Share repurchase and retirement   | -               | (213)         | (81)          |
| Proceeds from exercise of stock options   | 458             | 317           | 245           |
| Cash paid for dividends   | <u>-</u>        | <u>(263)</u>  | <u>(258)</u>  |
| Net cash provided by (used in) financing activities   | <u>458</u>      | <u>2,341</u>  | <u>(94)</u>   |
| Increase (decrease) in cash and cash equivalents  | 496             | 348           | (323)         |
| Cash and cash equivalents at beginning of year  | <u>709</u>      | <u>361</u>    | <u>684</u>    |
| Cash and cash equivalents at end of year  | <u>\$ 1,205</u> | <u>\$ 709</u> | <u>\$ 361</u> |
| Non-cash investing activities:  |                 |               |               |
| Net change in unrealized (loss) gain on available-for-sale investment securities            | \$ (1,407)      | \$ (1,090)    | \$ (1,080)    |
| Fair market value of common stock issued in acquisition of subsidiary                       | \$ 6,079        | \$ -          | \$ -          |
| Non-cash financing activities:  |                 |               |               |
| Tax benefit from stock options exercised  | \$ 173          | \$ 143        | \$ 78         |

# Management's Discussion and Analysis

## of Financial Condition and Results of Operations

### Unaudited Quarterly Statement of Operations Data

(Dollars in thousands, except per share data)

|  | Q4<br>2005 | Q3<br>2005 | Q2<br>2005 | Q1<br>2005 | Q4<br>2004 | Q3<br>2004 | Q2<br>2004 | Q1<br>2004 |
|--|------------|------------|------------|------------|------------|------------|------------|------------|
| Net interest income                      | \$ 5,945   | \$ 5,592   | \$ 5,357   | \$ 5,037   | \$ 4,170   | \$ 3,821   | \$ 3,465   | \$ 3,365   |
| Provision for loan and lease losses      | 500        | 10         | -          | -          | -          | -          | -          | -          |
| Non interest income                      | 933        | 960        | 1,012      | 855        | 852        | 842        | 900        | 1,343      |
| Non-interest expenses                    | 3,811      | 3,953      | 3,978      | 4,051      | 3,496      | 3,151      | 3,102      | 3,370      |
| Income before provision for income taxes | 2,567      | 2,589      | 2,391      | 1,841      | 1,526      | 1,512      | 1,263      | 1,338      |
| Provision for income taxes               | 899        | 940        | 858        | 647        | 485        | 544        | 438        | 477        |
| Net income                               | \$ 1,668   | \$ 1,649   | \$ 1,533   | \$ 1,194   | \$ 1,041   | \$ 968     | \$ 825     | \$ 861     |
| Per share:                               |            |            |            |            |            |            |            |            |
| Basic earnings per share                 | \$ 0.28    | \$ 0.28    | \$ 0.26    | \$ 0.21    | \$ 0.20    | \$ 0.18    | \$ 0.16    | \$ 0.17    |
| Diluted earnings per share               | \$ 0.25    | \$ 0.26    | \$ 0.24    | \$ 0.19    | \$ 0.18    | \$ 0.16    | \$ 0.15    | \$ 0.15    |

### MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis should be read in conjunction with the Company's audited Consolidated Financial Statements and the Notes thereto, at pages 8 through 24.

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

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

### INTRODUCTION

Central Valley Community Bancorp (NASDAQ: CVCY) (the "Company") was incorporated on February 7, 2000. The formation of the holding company offered the Company more flexibility in meeting the long-term needs of customers, shareholders, and the communities it serves. The Company currently has one bank subsidiary. The Company's market area includes the central valley area from Sacramento, California to Bakersfield, California. To garner public acceptance beyond the Clovis-Fresno area, the Company made a decision in the first half of 2002 to change the name of its one subsidiary, Clovis Community Bank, to Central Valley Community Bank (the "Bank").

During 2005, the Company focused on assuring competitive products and services to our clients were made available while adjusting to the many new laws and regulations that affect the banking industry. The Bank opened a full service retail office in the Fresno downtown area on February 13, 2006.

After the close of business on December 31, 2004, the Company completed the merger with Bank of Madera County (BMC). The Madera and Oakhurst branches of BMC were merged into the Bank bringing the total number of branches to nine. For details of the merger, refer to Note 2 to the Company's audited Consolidated Financial Statements at page 14.

### ECONOMIC CONDITIONS

Fresno County's economy has been relatively stable for the past three to four years; however, some minor evidence of a slow down has been evident in the fourth quarter of 2005. Most industries in the County are either stable or contracting very modestly. Fresno County's double-digit unemployment is one of the highest rates in California and the nation; however in the fourth quarter of 2005, the County reported single digit unemployment for the first time in many years. This high level is a hindrance to strong growth in the County. Agriculture and agricultural related businesses remain a critical part of the County's economy. The County's agricultural production is widely diversified producing cotton, nuts, vegetables, fruit, cattle, and dairy products. Due to low land costs, relative to the rest of the state, Fresno's economy has been significantly affected by the real estate construction segment in the past 5 years. Several new and planned developments in the foothill area of the County may assist the industry in maintaining its growth. However, there are indications of a slowing in the housing market; residential permits have been declining in 2005.

Fresno County also offers lower living costs compared with metropolitan areas to the North and South of the County. Fresno County's home appreciation has averaged 20% annually over the past four years. While affordability has declined as a result, the area is still considered more

# Selected Financial Data

## Years Ended December 31, (In thousands, except per share amounts)

| Operations for the year:                               | 2005      | 2004      | 2003      | 2002      | 2001      |
|--|-----------|-----------|-----------|-----------|-----------|
| Total interest income                                  | \$ 26,070 | \$ 16,799 | \$ 14,970 | \$ 14,536 | \$ 14,577 |
| Total interest expense                                 | 4,139     | 1,978     | 2,290     | 2,728     | 4,138     |
| Net interest income before provision for credit losses | 21,931    | 14,821    | 12,680    | 11,808    | 10,439    |
| Provision for credit losses                            | 510       | -         | -         | -         | 623       |
| Net interest income after provision for credit losses  | 21,421    | 14,821    | 12,680    | 11,808    | 9,816     |
| Non-interest income                                    | 3,760     | 3,937     | 4,546     | 4,212     | 4,692     |
|  | 25,181    | 18,758    | 17,226    | 16,020    | 14,508    |
| Non-interest expense                                   | 15,793    | 13,119    | 12,355    | 11,988    | 10,855    |
| Income before provision for income taxes               | 9,388     | 5,639     | 4,871     | 4,032     | 3,653     |
| Provision for income taxes                             | 3,344     | 1,944     | 1,499     | 1,248     | 1,275     |
| Net income   | \$ 6,044  | \$ 3,695  | \$ 3,372  | \$ 2,784  | \$ 2,378  |
| Basic earnings per share                               | \$ 1.03   | \$ 0.71   | \$ 0.65   | \$ 0.54   | \$ 0.46   |
| Diluted earnings per share                             | \$ 0.94   | \$ 0.64   | \$ 0.60   | \$ 0.51   | \$ 0.45   |
| Cash dividends declared per common share               | \$ -      | \$ 0.05   | \$ 0.05   | \$ 0.03   | \$ -      |

## December 31, (In thousands)

| Balances at end of year:   | 2005       | 2004       | 2003       | 2002      | 2001      |
|--|------------|------------|------------|-----------|-----------|
| Investment securities, Federal funds<br>sold and deposits in other banks | \$ 136,340 | \$ 127,895 | \$ 107,300 | \$ 95,901 | \$ 64,746 |
| Net loans  | 298,463    | 206,582    | 183,849    | 156,293   | 130,797   |
| Total deposits   | 430,989    | 326,186    | 290,565    | 246,337   | 192,132   |
| Total assets   | 483,677    | 368,147    | 327,930    | 283,006   | 219,067   |
| Shareholders' equity   | 41,523     | 29,606     | 26,720     | 24,099    | 20,828    |
| Earning assets   | 440,646    | 338,032    | 292,494    | 251,895   | 196,374   |

| Average balances:  | 2005       | 2004       | 2003       | 2002      | 2001      |
|--|------------|------------|------------|-----------|-----------|
| Investment securities, Federal funds<br>sold and deposits in other banks | \$ 135,679 | \$ 115,069 | \$ 101,222 | \$ 74,111 | \$ 70,326 |
| Net loans  | 274,348    | 192,658    | 172,310    | 146,264   | 110,293   |
| Total deposits   | 407,188    | 307,453    | 270,159    | 212,629   | 183,189   |
| Total assets   | 455,680    | 346,217    | 306,384    | 248,948   | 206,522   |
| Shareholders' equity   | 38,691     | 28,203     | 25,484     | 22,604    | 20,181    |
| Earning assets   | 414,257    | 311,456    | 275,846    | 222,067   | 182,418   |

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## **OVERVIEW** (Continued)

### Asset Quality - (continued)

compared to none as of December 31, 2004 and \$634,000 as of December 31, 2003. Two (2) loans comprised the \$616,000 in non-performing loans, and as of December 31, 2005, both loans were on nonaccrual. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on non-accrual status until such time as management has determined that the loans are likely to remain current in future periods. In December 2005, we charged off two (2) commercial loans in which the company had suffered a fire in one of their facilities. The event had a material impact on the operations of the company, which has subsequently filed for Chapter 7 protection. Recovery potential on these two loans is uncertain. As a result of the charge-off, we also increased our provision for credit losses to \$510,000 for 2005 compared to no provision in 2004 and 2003. Non-performing loans as a percentage of gross loans were 0.2% as of December 31, 2005 compared to none at December 31, 2004 and 0.3% at December 31, 2003. The Company did not have any other real estate owned at December 31, 2005, 2004 or 2003.

### Asset Growth

As revenues from both net interest income and non-interest income are a function of asset size, the continued growth in assets has a direct impact in increasing net income and therefore ROE and ROA. The majority of our assets are loans and investment securities, and the majority of our liabilities are deposits, and therefore the ability to generate deposits as a funding source for loans and investments is fundamental to our asset growth. Total assets increased 31.4% during 2005 to \$483,677,000 as of December 31, 2005 from \$368,147,000 as of December 31, 2004. Total gross loans increased 44.2% to \$301,802,000 as of December 31, 2005, compared to \$209,279,000 at December 31, 2004. Total investment securities increased 6.7% to \$105,592,000 as of December 31, 2005 compared to \$98,983,000 as of December 31, 2004 as deposit growth exceeded loan growth. Total deposits increased 32.1% to \$430,989,000 as of December 31, 2005 compared to \$326,186,000 as of December 31, 2004. We continue to under perform in our loan to deposit ratio compared to our peers. Our loan to deposit ratio at December 31, 2005 was 70.0% compared to 64.2% at December 31, 2004. The loan to deposit ratio of our peers was 89.6% at September 30, 2005.

### Operating Efficiency

Operating efficiency is the measure of how efficiently earnings before taxes are generated as a percentage of revenue. The Bank's efficiency ratio (non-interest expenses divided by net interest income plus non-interest income, excluding realized gain on sale of securities) improved to 58.7% for 2005 compared to 69.2% for 2004 and 72.6% at 2003. The improvement in the efficiency ratio is due to the increase in revenues exceeding the increase in operating expenses. The Bank's net interest income before provision for credit losses plus non-interest income increased 40.9% to \$25,753,000 in 2005 compared to \$18,273,000 in 2004 and \$16,678,000 in 2003, while operating expenses increased 19.5% in 2005 and 4.6% in 2004 and 3.7% in 2003. The increase in operating expenses in 2005 can be partially attributed to the merger.

## **RESULTS OF OPERATIONS**

### **NET INCOME**

Net income increased to \$6,044,000 in 2005 compared to \$3,695,000 and \$3,372,000 in 2004 and 2003, respectively. Basic earnings per share were \$1.03, \$0.71 and \$0.65 for 2005, 2004 and 2003, respectively. Diluted earnings per share were \$0.94, \$0.64 and \$0.60 for 2005, 2004 and 2003, respectively. ROE was 15.63% for 2005 compared to 13.10% for 2004, and 13.23% for 2003. ROA for 2005 was 1.33% compared to 1.07% and 1.10% for 2004 and 2003, respectively.

The increase in net income and profitability for 2005 compared to the same period in 2004 was mainly due to the increases in net interest income and was partially offset by decreases in non-interest income and increases in the provision for credit losses and non-interest expenses. Net interest income increased due to an increase in average interest earning assets provided by our organic growth, the merger, and the positive effect of our asset sensitive position expanding our net interest margin in response to the thirteen increases in the Federal funds interest rate since June 30, 2004. Non-interest income in 2005 included a realized gain from the sale of investments of \$92,000 compared to the gain from the sale of investments of \$483,000 in 2004 and \$506,000 in 2003. Non-interest expenses increased primarily due to salaries and benefits and equipment and occupancy expenses that were all affected by the BMC merger.

### **INTEREST INCOME AND EXPENSE**

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

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

Interest and fee income from loans increased 59.6% in 2005 compared to the same period of 2004. Interest and fee income increased 9.9% from 2003 to 2004. As stated above, the combination of the increased volume of loans from the merger with BMC, our organic growth from the focus on building relationships, and the thirteen interest rate increases that have occurred since June 30, 2004, were the major components of the \$7,888,000 increase. Average total loans for 2005 were \$277,855,000 compared to \$195,223,000 and \$174,708,000 for the same periods of 2004 and 2003. The yield on loans for 2005 was 7.63% compared to 6.78% and 6.92% for the same periods of 2004 and 2003, respectively.

Interest income from total investments, (total investments include investment securities, Federal funds, interest bearing deposits with other banks, and other securities) not on a fully tax equivalent basis, increased \$1,383,000 in 2005 compared to 2004, mainly due to the 17.9% increase in average balances of these investments and the thirteen interest rate increases that have occurred since June 30, 2004. In 2004, total investment income increased \$611,000 from 2003. We sold \$14,624,000 in investment securities in 2005 due to funding several new loans and some portfolio restructuring. The realized gain from sales of available for sale investments is discussed in non-interest income below. Due to our low loan to deposit ratio, a significant contributor to interest income is the investment portfolio, which represents 22.6% and 24.1% of net interest income before provision for credit losses for 2005 and 2004, respectively.

In an effort to increase yields, without accepting unreasonable risk, a significant portion of the investment purchases have been in high quality mortgage-backed securities ("MBS") and collateralized mortgage obligations ("CMOs"). At December 31, 2005, we held \$48,431,000 or 45.9% of the total market value of the investment portfolio in MBS and CMOs with an average yield of 3.65%. We understand the interest rate risks and prepayment risks associated with MBS and CMOs. In a declining interest rate environment, prepayments from MBS and CMOs could be expected to increase and the expected life of the investment could be expected to shorten. Conversely, if interest rates increase, prepayments could be expected to decline and the average life of the MBS and CMOs could be expected to extend. Additionally, changes in interest rates are reflected in the market value of the investment portfolio. During declining interest rates, the investment portfolio could be expected to have market value gains and in increasing rate environments, the market value could be expected to decline. The net of tax-effect of the change in market value of the available for-sale investment portfolio

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## **ECONOMIC CONDITIONS** (Continued)

affordable than other places in California. Residential construction, while slowing somewhat, still appears to be strong. The local economy benefited from growth in housing and construction fueled by record low long-term interest rates, demand for new housing and refinance activity.

## **STOCK SPLIT**

On September 21, 2005 the Company's Board of Directors approved a two-for-one stock split for shareholders of record at the close of business on October 5, 2005 and effective on October 31, 2005. All share and per share data in the consolidated financial statements and the following management's discussion and analysis have been retroactively restated to give effect to the stock split.

## **OVERVIEW**

We are extremely pleased to report that both our 2005 operations and the completed merger, which included the data system conversion of Bank of Madera County (BMC), were accretive to our diluted earnings per share (EPS). Diluted EPS for the year ended December 31, 2005 was \$0.94 compared to \$0.64 and \$0.60 for years ended December 31, 2004 and 2003. The increase in EPS from 2004 to 2005 was generated even after the 8% dilutive impact of the additional 522,106 shares of common stock issued as a result of the BMC merger. Net income for 2005 was \$6,044,000 compared to \$3,695,000 and \$3,372,000 for the same period in 2004 and 2003, respectively. In 2005, the \$6,044,000 in earnings included a gain of \$92,000 from the sale of securities compared to \$483,000 and \$506,000 in 2004 and 2003, respectively. Additionally, we increased the provision for credit loss to \$510,000 in 2005 compared to none in 2004 and 2003. Further discussion of operations and the effects of the merger are discussed below.

Return on average equity for 2005 was 15.63% compared to 13.10% and 13.23% for the same periods of 2004 and 2003, respectively. Goodwill and core deposit intangible, resulting from the BMC merger, at December 31, 2005 was \$8,955,000 and \$1,286,000, respectively. The Company did not have any goodwill or intangibles at December 31, 2004. Total equity was \$41,523,000 at December 31, 2005 compared to \$29,606,000 at December 31, 2004.

Total loans continued to grow at a double digit pace in 2005. Average total loans increased \$82,632,000 or 42.3% in 2005 compared to 2004 of which \$45,779,000 can be attributed to the BMC merger. Asset quality continues to be strong. However in 2005, we recorded a provision for credit losses for the first time in three years. The Company had two (2) non-accrual loans at December 31, 2005 totaling \$616,000 compared to none at December 31, 2004. In December 2005, we charged off two loans totaling \$688,000. Net charge-offs for 2005 were \$619,000 compared to net recoveries of \$272,000 in 2004 and net charge-offs of \$8,000 in 2003; refer to "Asset Quality" below for further information. We had no other real estate owned at December 31, 2005 and 2004.

### **Key Factors in Evaluating Financial Condition and Operating Performance**

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

- Return to our stockholders;
- Return on average assets;
- Development of core revenue streams, including net interest income and non-interest income;
- Asset quality;
- Asset growth; and
- Operating efficiency.

## **Return to Our Stockholders**

Our return to our stockholders is measured in the form of return on average equity ("ROE"). Our net income for December 31, 2005 increased \$2,349,000 compared to increases of \$323,000 and \$588,000 for 2004 and 2003, respectively. Net income increased mainly due to an increase in net interest income provided by the increase in interest rates and the additional loan volume from the BMC merger and our own organic growth. This increase was partially offset by an increase in interest expenses, addition to the provision for credit losses, operating expenses and a decrease in non interest income. Basic EPS increased to \$1.03 for the year ended 2005 compared to \$0.71 and \$0.65 for years ended 2004 and 2003, respectively. Diluted EPS increased to \$0.94 for the year ended 2005 compared to \$0.64 and \$0.60 for years ended 2004 and 2003, respectively. The increase in EPS was due primarily to the increase in net income, partially offset by the increase in average shares outstanding as a result of the merger and the exercise of stock options. Our ROE was 15.63% for the year ended 2005 compared to 13.10% and 13.23% for the years ended 2004 and 2003, respectively. The increase in ROE is due to the increase in income partially offset by the increase in average equity outstanding, as a result of the BMC merger.

## **Return on Average Assets**

Our return on average assets ("ROA") is a measure we use to compare our performance with other banks and bank holding companies. Our ROA for the year ended 2005 increased to 1.33% compared to 1.07% and 1.10% for the years ended December 31, 2004 and 2003. The 2005 increase in ROA is due to the increase in net income relative to our increase in average assets. ROA for our peer group was 1.47% at September 30, 2005. Peer group from SNL Financial data includes all holding companies in California with assets from \$300M to \$500M and not subchapter S.

## **Development of Core Earnings**

Over the past several years, we have focused on not only improving net income, but improving the consistency of our revenue streams in order to create more predictable future earnings and reduce the effect of changes in our operating environment on our net income. Specifically, we have focused on net interest income through a variety of processes, including increases in average interest earning assets as a result of the merger, loan generation and retention and improved net interest margin by focusing on core deposit growth and managing the cost of funds. As a result, our net interest income before provision for credit losses increased \$7,110,000 or 48.0% to \$21,931,000 for the year ended 2005 compared to \$14,821,000 and \$12,680,000 for the years ended 2004 and 2003, respectively. Our net interest margin has also improved 55 basis points to 5.46% for the year ended 2005 compared to 4.91% and 4.75% for the years ended 2004 and 2003, respectively.

Our non-interest income is generally made up of service charges and fees on deposit accounts and fee income from loan placements and gain on sale from investment securities. Non-interest income in 2005 decreased \$177,000 or 4.5% to \$3,760,000 compared to \$3,937,000 and \$4,546,000 in 2004 and 2003, respectively. Non-interest income in 2005 included gains from the sale of investments of \$92,000 compared to \$483,000 in 2004 and \$506,000 in 2003. Additionally, in 2004 and 2003, the Company recorded income from equipment leased to others for which it recognized income of \$38,000 and \$485,000, respectively. The Company exited that activity in 2004. Customer service charges increased slightly to \$2,414,000 in 2005 compared to \$2,340,000 and \$2,215,000 in 2004 and 2003, respectively, mainly due to an increase in the number of transaction accounts. Further detail on non-interest income is provided below.

## **Asset Quality**

For all banks and bank holding companies, asset quality has a significant impact on the overall financial condition and results of operations. Asset quality is measured in terms of percentage of total loans and total assets, and is a key element in estimating the future earnings of a company. Non-performing loans totaled \$616,000 as of December 31, 2005

# Management's Discussion and Analysis

## of Financial Condition and Results of Operations

### INTEREST INCOME AND EXPENSE (Continued)

was the result of our own organic growth and the approximate \$45,779,000 in loans and \$19,250,000 in investments as the result of the merger of BMC.

Interest expense on deposits in 2005 increased \$2,093,000 or 116.7% to \$3,886,000 compared to \$1,793,000 and \$2,004,000 in 2004 and 2003, respectively. The increase in 2005 compared to 2004 was due to the repricing of interest-bearing deposits, which increased 52 basis points to 1.37% in 2005 from .85% in 2004, as a result of the increases in the Federal funds interest rate and the \$72,770,000 increase in volume of average interest bearing deposits from 2004 to 2005. The decrease in 2004 compared to 2003 was due to the change in mix of the interest bearing deposits and the repricing of those deposits. Rates paid on interest bearing deposits decreased 20 basis points from 1.05% in 2003 while the volume of average interest bearing deposits increased \$19,448,000 from 2003 to 2004. Average interest-bearing deposits were \$283,013,000 for 2005 compared to \$210,243,000 and \$190,795,000 for 2004 and 2003, respectively. The increase was the result of our own internal growth and the addition of approximately \$44,596,000 in interest-bearing deposits in 2005 as the result of the merger of BMC.

Average other borrowings decreased to \$6,725,000 with an effective rate of 3.76% for 2005 compared to \$7,311,000 with an effective rate of 2.53% for 2004. In 2003 the average other borrowings were \$8,230,000 with an effective rate of 3.48%. Included in other borrowings are advances from the Federal Home Loan Bank (FHLB) and a loan from a major bank, in late 2004, primarily to provide additional capital for the Bank in conjunction with the merger with BMC. We borrowed funds from the Federal Home Loan Bank during a period of low interest rates. The effective rate of the FHLB advances was 2.36% for 2005 compared to 2.53% for 2004 and 3.48% for 2003.

In partial offset to the increase in the cost of interest bearing deposits and other borrowings, the increase in non-interest bearing demand deposits has contributed significantly to the overall cost of funds. Average demand deposits increased 27.7% from an average \$97,210,000 for 2004 to \$124,175,000 for 2005. The merger with BMC added approximately \$19,173,000 in non-interest bearing deposits to our portfolio. The cost of all of our interest bearing liabilities increased 52 basis points to 1.43% for 2005 compared to 0.91% for 2004 and 1.15% for 2003. Average transaction accounts (including interest bearing checking, money market accounts and non-interest bearing demand deposits) increased 28.1% to \$293,609,000 for 2005 compared to \$229,249,000 for 2004 and \$193,556,000 for 2003.

### NET INTEREST INCOME BEFORE PROVISION FOR CREDIT LOSSES

Net interest income before provision for credit losses for 2005 increased \$7,110,000 or 48.0% to \$21,931,000 compared to \$14,821,000 for 2004 and \$12,680,000 for 2003. This increase in 2005 compared to 2004 was primarily due to the increase in the net interest margin, combined with an increase in average interest earning assets partially offset by the increase in average interest bearing liabilities. Average interest earning assets were \$414,257,000 for 2005 with a net interest margin of 5.46% compared to \$311,456,000 with a net interest margin of 4.91% in 2004. The increase in 2004 compared to 2003 was primarily due to the increase in the net interest margin, combined with an increase in average interest earning assets. Average interest-earning assets were \$275,846,000 with a net interest margin of 4.75% for 2003. For a discussion of the repricing of our assets and liabilities, see Quantitative and Qualitative Disclosure about Market Risk on page 37.

### PROVISION FOR CREDIT LOSSES

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

The establishment of an adequate credit allowance is based on both an accurate risk rating system and loan portfolio management tools. The Board has established initial responsibility for the accuracy of credit risk grades with the individual credit officer. The grading is then submitted to the Chief Credit Administrator ("CCA"), who reviews the grades for accuracy and makes recommendations to Credit Review who gives final approval. The risk grading and reserve allocation is analyzed annually by a third party credit reviewer and by various regulatory agencies.

Quarterly, the CCA sets the specific reserve for all adversely risk-graded credits. This process includes the utilization of loan delinquency reports, classified asset reports, and portfolio concentration reports to assist in accurately assessing credit risk and establishing appropriate reserves. Reserves are also allocated to credits that are not adversely graded. Historical loss experience within the portfolio along with peer bank loss experiences are used in determining the level of the reserves held.

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

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

| Loan Type<br>(Dollars in thousands)   | December 31,<br>2005 |                     | December 31,<br>2004 |                     |
|---|----------------------|---------------------|----------------------|---------------------|
|   | \$                   | % of Total<br>Loans | \$                   | % of Total<br>Loans |
| Commercial & industrial   | 1,325                | 27.5%               | 786                  | 27.5%               |
| Real estate   | 1,138                | 41.0%               | 898                  | 35.9%               |
| Real estate<br>- construction,<br>land development<br>and other<br>land loans | 378                  | 15.4%               | 197                  | 16.9%               |
| Equity lines<br>of credit   | 175                  | 7.8%                | 136                  | 8.9%                |
| Agricultural  | 198                  | 2.5%                | 151                  | 7.6%                |
| Consumer<br>& installment   | 120                  | 5.8%                | 178                  | 3.1%                |
| Other   | 1                    | 0.0%                | 51                   | 0.1%                |
| Non-specific reserve  | 4                    |                     | 300                  |                     |
|   | <u>\$ 3,339</u>      |                     | <u>\$ 2,697</u>      |                     |

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

The provision for credit losses in 2005 was \$510,000. There were no provisions made in 2004 and 2003. The increase in 2005 is primarily the result of our assessment of the adequacy of the allowance for credit losses after giving effect to the charge-off in December 2005 of two (2) commercial loans. The borrower suffered a fire in one of their facilities. The event had a material impact on the operations of the company which has subsequently filed for Chapter 7 protection. Recovery potential on these two loans is uncertain. Non-performing loans as a percentage of gross loans was 0.2% as of December 31, 2005 compared to none at December 31, 2004 and 0.3% at December 31, 2003. Non-performing loans as of December 31, 2005 totaled \$616,000 and were comprised of one real



# Management's Discussion and Analysis

## of Financial Condition and Results of Operations

### INTEREST INCOME AND EXPENSE (Continued)

| SCHEDULE OF AVERAGE BALANCES<br>AND AVERAGE YIELDS AND RATES<br>(Dollars in thousands) | For The Year Ended December 31, 2005 |                  |                             | For The Year Ended December 31, 2004 |                  |                             |
|--|--------------------------------------|------------------|-----------------------------|--------------------------------------|------------------|-----------------------------|
|  | Average<br>Balance                   | Interest         | Average<br>Interest<br>Rate | Average<br>Balance                   | Interest         | Average<br>Interest<br>Rate |
| <b>ASSETS</b>  |                                      |                  |                             |                                      |                  |                             |
| Interest-earning deposits in other banks   | \$ 2,136                             | \$ 59            | 2.76%                       | \$ 2,192                             | \$ 37            | 1.69%                       |
| Securities:  |                                      |                  |                             |                                      |                  |                             |
| Taxable securities   | 86,857                               | 3,002            | 3.46%                       | 77,734                               | 2,462            | 3.17%                       |
| Non-taxable securities (1)   | 25,096                               | 1,806            | 7.20%                       | 18,833                               | 1,271            | 6.75%                       |
| Total investment securities  | 111,953                              | 4,808            | 4.29%                       | 96,567                               | 3,733            | 3.87%                       |
| Federal funds sold   | 21,590                               | 702              | 3.25%                       | 16,310                               | 234              | 1.43%                       |
| Total  | 135,679                              | 5,569            | 4.10%                       | 115,069                              | 4,004            | 3.48%                       |
| Loans (2) (3)  | 276,957                              | 21,115           | 7.63%                       | 195,187                              | 13,227           | 6.78%                       |
| Federal Home Loan Bank stock   | 1,621                                | 68               | 4.19%                       | 1,200                                | 41               | 3.42%                       |
| <b>Total interest-earning assets</b>   | <u>414,257</u>                       | <u>\$ 26,752</u> | <u>6.46%</u>                | <u>311,456</u>                       | <u>\$ 17,272</u> | <u>5.55%</u>                |
| Allowance for credit losses  | (3,507)                              |                  |                             | (2,565)                              |                  |                             |
| Non-accrual loans  | 898                                  |                  |                             | 36                                   |                  |                             |
| Cash and due from banks  | 19,365                               |                  |                             | 23,567                               |                  |                             |
| Bank premises and equipment  | 3,004                                |                  |                             | 2,863                                |                  |                             |
| Other non-earning assets   | 21,663                               |                  |                             | 10,860                               |                  |                             |
| <b>Total average assets</b>  | <u>\$ 455,680</u>                    |                  |                             | <u>\$ 346,217</u>                    |                  |                             |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                                      |                  |                             |                                      |                  |                             |
| Interest-bearing liabilities:  |                                      |                  |                             |                                      |                  |                             |
| Savings and NOW accounts   | \$ 83,781                            | \$ 149           | 0.18%                       | \$ 67,099                            | \$ 118           | 0.18%                       |
| Money market accounts  | 111,519                              | 1,500            | 1.35%                       | 84,178                               | 660              | 0.78%                       |
| Time certificates of deposit, under \$100,000  | 50,841                               | 1,017            | 2.00%                       | 37,082                               | 550              | 1.48%                       |
| Time certificates of deposit, \$100,000 and over                                       | 36,872                               | 1,220            | 3.31%                       | 21,884                               | 465              | 2.12%                       |
| Total interest-bearing deposits  | 283,013                              | 3,886            | 1.37%                       | 210,243                              | 1,793            | 0.85%                       |
| Other borrowed funds   | 6,725                                | 253              | 3.76%                       | 7,311                                | 185              | 2.53%                       |
| Federal funds purchased  | -                                    | -                | -                           | 2                                    | -                | -                           |
| <b>Total interest-bearing liabilities</b>  | <u>289,738</u>                       | <u>\$ 4,139</u>  | <u>1.43%</u>                | <u>217,556</u>                       | <u>\$ 1,978</u>  | <u>0.91%</u>                |
| Non-interest bearing demand deposits   | 124,175                              |                  |                             | 97,210                               |                  |                             |
| Other liabilities  | 3,076                                |                  |                             | 3,248                                |                  |                             |
| Shareholders' equity   | 38,691                               |                  |                             | 28,203                               |                  |                             |
| <b>Total average liabilities and shareholders' equity</b>                              | <u>\$ 455,680</u>                    |                  |                             | <u>\$ 346,217</u>                    |                  |                             |
| Interest income and rate earned on average earning assets                              |                                      | \$ 26,752        | <u>6.46%</u>                |                                      | \$ 17,272        | <u>5.55%</u>                |
| Interest expense and interest cost related to average interest-bearing liabilities     |                                      | <u>4,139</u>     | <u>1.43%</u>                |                                      | <u>1,978</u>     | <u>0.91%</u>                |
| <b>Net interest income and net interest margin (4)</b>                                 |                                      | <u>\$ 22,613</u> | <u>5.46%</u>                |                                      | <u>\$ 15,294</u> | <u>4.91%</u>                |

(1) Calculated on a fully tax equivalent basis, which includes Federal tax benefits relating to income earned on municipal bonds totaling \$614 and \$932 in 2005 and 2004, respectively.

(2) Loan interest income includes loan fees of \$964 in 2005 and \$808 in 2004.

(3) Average loans do not include non-accrual loans.

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

is also reflected in the Company's equity. At December 31, 2005, the average life of the investment portfolio was 4.5 years and the market value reflected a pre-tax loss of \$845,000.

A component of the Company's strategic plan has been to use its investment portfolio to offset, in part, its interest rate risk relating to variable rate loans. At December 31, 2005, an immediate rate increase of 200 basis points would result in an estimated decrease in the market value of the investment portfolio by approximately \$7,519,000. Conversely, with an immediate rate decrease of 200 basis points, the estimated increase in the market value of the investment portfolio is \$6,460,000. The modeling environment assumes management would take no action during an immediate shock of 200 basis points. The likelihood of immediate changes of 200 basis points is contrary to expectation, as evidenced by the changes in interest rates in the past year, which were in 25 basis point increments. However, the Company uses those increments to measure its interest rate risk in accordance with regulatory requirements and to measure the possible future risk in the investment portfolio. For further discussion

of the Company's market risk, refer to Quantitative and Qualitative Disclosures about Market Risk on page 37.

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

Total interest income in 2005 increased \$9,271,000, to \$26,070,000 compared to \$16,799,000 in 2004 and \$14,970,000 in 2003. The 55.2% increase in 2005 was due to the 33.0% increase in the average balance of interest earning assets, combined with the 91 basis point increase in the yield on those assets. Average interest-earning assets increased to \$414,257,000 for 2005 compared to \$311,456,000 for 2004, and \$275,846,000 for 2003. The yield on interest earning assets increased to 6.46% for 2005 compared to 5.55% and 5.58% for 2004 and 2003, respectively. The \$102,801,000 increase in average earning assets in 2005



# Management's Discussion and Analysis of Financial Condition and Results of Operations

## PROVISION FOR CREDIT LOSSES (Continued)

estate secured loan for \$591,000 and one commercial loan for \$25,000. We do not anticipate a loss on either loan. The Company did not have any other real estate owned at December 31, 2005 or 2004.

For 2005 we had a net charge off ratio of 0.223%. For 2004, we had a net recovery ratio of 0.139%, and a net charge-off ratio of 0.005% for 2003. The potential for a future net recovery position is not likely as we have been very successful in collection of those loans charged off in prior years. Refer to the allowance for credit losses section for further discussion of credit quality.

The completion of the merger of BMC into the Bank provided an additional \$751,000 to the allowance for credit losses. Based on information currently available, management believes that the allowance for credit losses should be adequate to absorb estimated probable losses in the portfolio. However, no assurance can be given that we may not sustain charge-offs which are in excess of the allowance in any given period. Refer to "Allowance for Credit Losses" below for further information of the allowance for credit losses.

## NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES

Net interest income after the \$510,000 addition to provision for credit losses was \$21,421,000 for 2005 compared to \$14,821,000 and \$12,680,000 for 2004 and 2003, respectively.

## NON-INTEREST INCOME

Non interest income is comprised of customer service charges, loan placement fees, gain on sales of investments and other income. Non-interest income was \$3,760,000 in 2005 compared to \$3,937,000 and \$4,546,000 in 2004 and 2003, respectively. The \$177,000 decrease in non-interest income comparing 2005 to 2004 was primarily due to the decrease in gain realized on sale of investment securities of \$391,000. The decrease from 2004 to 2003 was mainly due to the \$447,000 decrease in rentals from equipment leased to others. We have allowed the volume of leases to run-off and have not replaced them as we have exited that activity.

Customer service charges increased \$74,000 to \$2,414,000 in 2005 compared to \$2,340,000 in 2004 and \$2,215,000 in 2003. The increase in both years is mainly due to an increase in the activity level as the average number of transaction accounts has increased and the increase in fees generated by the overdraft protection program which began in 2003.

We earn loan placement fees from the brokerage of single-family residential mortgage loans provided for the convenience of our customers. Loan placement fees increased \$60,000 in 2005 to \$390,000 compared to \$330,000 for 2004 and decreased in 2004 by \$158,000 from \$488,000 in 2003. The increase in 2005 is primarily due to the continued relative strength of normal home sales due to "moving up" or relocating as Fresno and Madera counties continue to reflect affordable housing compared to other parts of California. The decrease in 2004 compared to 2003 is mainly due to the impact of the increases in mortgage rates and less refinancing opportunities.

Appreciation in cash surrender value of bank owned life insurance (BOLI) increased \$15,000 mainly due to \$440,000 in BOLI purchased in 2005. The Bank purchased the additional insurance in connection with increases to the split-dollar life insurance policies related to salary continuation benefits for four key executives. Offsetting the increase in volume was a decrease in the interest rate received. Appreciation in 2004 compared to 2003 decreased \$103,000 as a result of the decrease in the yields earned. This interest rate is reviewed annually by the Board of Directors. Salary continuation and the related BOLI are used as a retention tool for directors and key executives of the Bank.

The Bank holds stock from the Federal Home Loan Bank in relationship with the borrowing capacity and generally receives quarterly dividends. We currently hold \$1,659,000 in FHFB stock of which \$172,000 was the result of the merger with BMC compared to \$1,420,000 at December 31, 2004. Dividends in 2005 increased to \$68,000 compared to \$41,000 in 2004 and \$28,000 in 2003.

Other income increased to \$581,000 in 2005 compared to \$505,000 and \$521,000 in 2004 and 2003, respectively. The \$76,000 increase comparing 2005 to 2004 can be attributed to an increase in merchant fees from bankcards, an increase in overall fees charged for miscellaneous services due to increases in volume, and fees from investment services provided by a third party. 2003 included \$485,000 from lease rental income from equipment leased to others compared to none in 2005 and \$38,000 in 2004. The decrease is a result of the Company's decision to no longer participate in operating lease arrangements.

## NON-INTEREST EXPENSES

Salaries and employee benefits, occupancy and equipment, professional services, and data processing are the major categories of non-interest expenses. Non-interest expenses increased \$2,674,000 to \$15,793,000 in 2005 compared to \$13,119,000 in 2004 which increased \$764,000 in 2004 from \$12,355,000 in 2003.

The Bank's efficiency ratio, measured as the percentage of non-interest expenses to net interest income before provision for credit losses plus non-interest income (excluding gains on sales of investments), improved to 58.7% for 2005 compared to 69.2% for 2004 and 72.6% for 2003.

Salaries and employee benefits increased \$1,639,000 or 21.7% to \$9,178,000 in 2005 compared to \$7,539,000 in 2004 and \$7,152,000 in 2003. The increase in salaries and employee benefits in 2005 compared to 2004 can be attributed to normal cost increases for salaries and benefits and incentive based compensation due to increased loan and deposit production, profitability, and the additional personnel costs from the merger with BMC which includes the salary of one former BMC executive officer retained by the Company following the merger. The \$387,000 increase in 2004 compared to 2003 is primarily related to general salary and benefit increases and additional staffing. Commissions paid for loan placements in 2005 increased \$49,000 comparing 2005 to 2004. Commissions were \$199,000 for 2005 compared to \$150,000 in 2004 and \$229,000 in 2003.

Occupancy and equipment expense increased \$512,000 to \$2,133,000 in 2005 compared to \$1,621,000 in 2004 and \$1,576,000 in 2003. The 31.6% increase in occupancy expense in 2005 compared to 2004 was due mainly to the addition of the two branches resulting from the merger, normal increases in rent on existing leaseholds, and other occupancy related expenses. The 2.9% increase in 2004 compared to 2003 was due to increased depreciation costs related to remodeling of offices.

Other non-interest expenses increased \$561,000 or 14.3% in 2005 compared to 2004. Contributing to the 2005 increase in other non-interest expense was an additional \$100,000 write down to the Company's investment in CATEX Holding Corporation, formerly known as Diversified Capital Holdings, the parent company of a title and escrow insurance company that was sold in July 2005. To date, the Company has written down a total of \$250,000 of the original \$500,000 investment. The Company has received \$176,000 from the sale and anticipates full recovery of the remaining balance of \$74,000. Other non-interest expenses increased \$496,000 or 14.5% in 2004 compared to 2003. Contributing to the 2004 increase was a \$150,000 write down to the Company's investment described above, \$95,000 in expenses associated with the BMC merger and data processing conversion, and \$127,000 reversal of previously recorded state tax benefits relating to the Company's REIT.

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## LOANS (Continued)

### Allowance for Credit Losses - (continued)

- General valuation allowances ("GVA"): This element relates to assets with no well-defined deficiency or weakness (i.e. assets classified pass) and takes into consideration losses that are imbedded within the portfolio but have not yet been recognized. Generally, borrowers are impacted by events well in advance of a lender's knowledge that may ultimately result in loan default and eventual loss. An example of such a loss-causing event would be the loss of a major tenant in the case of commercial real estate loan. General valuation allowances are determined through consideration of past loss experience.
- GVA is calculated by applying loss factors to outstanding loans, in each case based on the internal risk grade of pass of such loans and commercial leases. Changes in risk grades affect the amount of the allowance. Loss factors are based on our historical loss experience and may be adjusted for significant factors that, in management's judgment, affect the collectibility of the portfolio as of the evaluation date.
- Loss factors are developed in the following ways:
  - pass graded loss factors for commercial, financial, and industrial loans along with real estate construction (participated, commercial or consumer) derive from a migration model that tracks historical losses over a period (usually the last thirty six calendar months) which we believe captures the inherent losses in our loan portfolio;
  - pass graded loss factors for commercial real estate loans are based on the average annual net charge-off rate over a period reflective of a full economic cycle; the past seven years.

We believe that an economic cycle is a period in which both upturns and downturns in the economy have been reflected. We calculate a loss factor over a time interval that spans what we believe constitutes a complete and representative economic cycle.

- Criticized and classified allowance: At the time of credit analysis and risk determination, credits, which have been determined to contain a weakness higher than management's overall risk appetite, are graded as criticized or classified. Once validated that the credit is not impaired, a risk of loss is calculated and applied.
- The CCA identifies credits that have a risk level of special mention or worse, however not inclusive of Impaired Assets. The calculation uses the credit's expected default frequency (EDF) as estimated by Moody's risk for private companies. In each case use of the loan maturity defines if the one or five year default component is employed. Default is defined by Moody's as a statistical probability that the credit will either miss or delay interest and/or principal payment, bankruptcy or receivership will occur, or exchange security where the exchange has the apparent purpose of helping the borrower avoid default. The exception to use of the EDF is found in the watch credits whereby the loan has an automatic 1% reserve held on outstanding balance. If the EDF has not been calculated, the Bank maintains an allocation equal to the sum of:

100% of those loans classified loss  
50% of those loans classified doubtful  
15% of those loans classified substandard  
5% of those loans classified special mention  
1% of those loans classified watch

- Pool loan allowance ("PLA"): Our residential and consumer loans and leases are relatively homogeneous with no single loan individually significant in terms of its size or potential risk of loss.

Therefore, we review our residential and consumer portfolios by analyzing their performance as a pool of loans. Generally, borrowers become impacted by events well in advance of a lender's knowledge that may ultimately result in loan default and eventual loss. Examples of such loss-causing events would be borrower job loss, divorce or medical crisis in the case of single family residential and consumer loans.

- Risk grade is not a component of this computation.
- Loss factors are developed in the following ways:
  - Pooled loan loss factors (not individually graded loans) are based on expected net charge-offs for one year. Pooled loans are loans that are homogeneous in nature, such as consumer installment, home equity, residential mortgage loans and consumer leases.
  - Large borrower risk allowance ("LBA"): CVCB has a number of borrowers with large loan balances which may create an additional risk if one or two of these borrowers were to unexpectedly default. Therefore an additional allowance for this risk is analyzed and applied.
  - LBA identifies those credits with outstandings exceeding the house lending limit.
  - Q factor allowances ("QFA"): The methodology applied in all other allowance sections does not account for both quantitative and qualitative factors and documentation. Any methodology falls subject to some uncertainties. All loans and commercial leases contain, in management's judgment, factors where loss recognition exists due to effects of the national and local economies, trends in nature and volume, changes in mix, consumer credit score migration, loan administration, concentrations, changes in internal lending policies, and collection practices to mention just a few.
  - QFA is subjective by definition. The factors reflect management's overall estimate of the additional rate of loss over the next four quarters that differ from either the historical loss experience or other valuations. The factors ever evolve and expectation of change from quarter to quarter is expected, both in inclusion and in value. As multiple factors exist which may be evaluated in connection with this allowance, topics noted below are examples only:
    - general economic and business conditions affecting our key lending areas;
    - credit quality trends (including trends in nonperforming loans expected to result from existing conditions);
    - collateral values;
    - loan volumes and concentrations;
    - seasoning of the loan portfolio;
    - specific industry conditions within portfolio segments;
    - recent loss experience in particular segments of the portfolio;
    - duration of the current economic cycle;
    - government regulation
    - bank regulatory examination results; and
    - findings of our internal and external credit reviewers.

Model risk allowance ("MRA"): The allowance methodologies noted above are by definition imprecise. Any methodology is subject to some uncertainties. Estimating future losses inherent in a loan portfolio will vary with each method. Therefore, one applies a model risk component to determine a loss provision. This allowance is also used to establish a minimum floor by which the provision for credit loss would not decline below 1% of total gross loans.

# Management's Discussion and Analysis

## of Financial Condition and Results of Operations

### LOANS (Continued)

We believe that our commercial real estate loan underwriting policies and practices result in prudent extensions of credit, but recognize that our lending activities result in relatively high reported commercial real estate lending levels. Commercial real estate loans include certain loans which represent low to moderate risk and certain loans with higher risks.

The Board of Directors reviews and approves concentration limits and exceptions to limitations of concentration are reported to the Board of Directors at least quarterly.

**Non-performing Assets** Non-performing assets consist of non-performing loans, other real estate owned ("OREO") and repossessed assets. Non-performing loans are those loans which have (i) been placed on non-accrual status, (ii) been subject to troubled debt restructuring, (iii) been classified as doubtful under our asset classification system, or (iv) become contractually past due 90 days or more with respect to principal or interest and have not been restructured or otherwise placed on non-accrual status. A loan is classified as non-accrual when 1) it is maintained on a cash basis because of deterioration in the financial condition of the borrower, 2) payment in full of principal or interest under the original contractual terms is not expected, or 3) principal or interest has been in default for a period of 90 days or more unless the asset is both well secured and in the process of collection.

At December 31, 2005 and December 31, 2004, we had no OREO, repossessed assets or restructured loans. At December 31, 2005, we had two non-accrual loans totaling \$616,000 compared to no non-accrual loans at December 31, 2004. At December 31, 2005, we estimated the potential for any losses from these credits would have a minimal impact on the allowance for credit losses.

A summary of non-accrual, restructured, and past due loans at December 31, 2005 and December 31, 2004 is set forth below. The Company had no restructured loans and no accruing loans past due more than 90 days at December 31, 2005 and December 31, 2004. Management is not aware of any potential problem loans, which were current and accruing at December 31, 2005, where serious doubt exists as to the ability of the borrower to comply with the present repayment terms. Management can give no assurance that non-accrual and other non-performing loans will not increase in the future.

#### Composition of Non-accrual, Past Due and Restructured Loans

| (Dollars in thousands)                                       | December 31, 2005 | December 31, 2004 |
|--|-------------------|-------------------|
| Non-accrual loans  |                   |                   |
| Commercial & industrial loans                                | \$ 25             | \$ -              |
| Real Estate  | 591               | -                 |
| Total non-accrual  | 616               | -                 |
| Accruing loans past due 90 days or more                      | -                 | -                 |
| Restructured loans   | -                 | -                 |
| Total non-performing loans                                   | \$ 616            | \$ -              |
| Non-accrual loans to total loans                             | 0.20%             | 0.0%              |
| Ratio of non-performing loans to allowance for credit losses | 18.5%             | 0.0%              |
| Loans considered to be impaired                              | \$ 616            | \$ -              |
| Related allowance for credit losses on impaired loans        | \$ -              | \$ -              |

We measure our impaired loans by using the fair value of the collateral if the loan is collateral-dependent and the present value of the expected future cash flows discounted at the loan's effective interest rate if the loan is not collateral-dependent. As of December 31, 2005, we had \$616,000 in impaired loans. We place loans on non-accrual status that are delinquent 90 days or more or when a reasonable doubt exists as to the collectibility of interest and principal. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on

non-accrual status until such time as management has determined that the loans are likely to remain current in future periods.

**Classified Assets** From time to time, management has reason to believe that certain borrowers may not be able to repay their loans within the parameters of the present repayment terms, even though, in some cases, the loans are current at the time. These loans are graded in the classified loan grades of "substandard," "doubtful," or "loss" and include non-performing loans. Each classified loan is monitored monthly. Classified assets, consisting of non-accrual loans, loans graded as substandard or lower, other real estate owned and repossessed assets, (all net of government guarantees), totaled \$2,598,000 as of December 31, 2005 compared to \$1,564,000 as of December 31, 2004.

**Allowance for Credit Losses** We have established a methodology for the determination of the allowance for credit losses. The methodology is set forth in a formal policy and takes into consideration the need for an overall allowance for credit losses as well as specific allowances that are tied to individual loans. Our methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance and a specific allowance for identified problem loans.

In originating loans, we recognize that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the collateral securing the loan. The allowance is increased by provisions charged against earnings and reduced by net loan charge offs. Loans are charged off when they are deemed to be uncollectible, or partially charged off when portions of a loan are deemed to be uncollectible. Recoveries are generally recorded only when cash payments are received.

The allowance for credit losses is maintained to cover losses inherent in the loan portfolio. The responsibility for the review of our assets and the determination of the adequacy lies with management and our Audit Committee. They delegate the authority to the CCA to determine the loss reserve ratio for each type of asset and reviews, at least quarterly, the adequacy of the allowance based on an evaluation of the portfolio, past experience, prevailing market conditions, amount of government guarantees, concentration in loan types and other relevant factors.

The allowance for credit losses is an estimate of the losses that may be sustained in our loan and lease portfolio. The allowance is based on two principles of accounting: (1) Statement of Financial Accounting Standards (SFAS) No. 5, "Accounting for Contingencies," which requires that losses be accrued when they are probable of occurring and estimable; and (2) SFAS No. 114, "Accounting by Creditors for Impairment of a Loan" and SFAS No. 118, "Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures," which requires that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

The Company under SFAS No. 5 establishes reserves. Credit Administration adheres to an internal asset review system and loss allowance methodology designed to provide for timely recognition of problem assets and adequate valuation allowances to cover expected asset losses. The Bank's asset monitoring process includes the use of asset classifications to segregate the assets, largely loans and real estate, into various risk categories. The Bank uses the various asset classifications as a means of measuring risk and determining the adequacy of valuation allowances by using a nine-grade system to classify assets. All credit facilities exceeding 90 days of delinquency require classification.

The allowance for credit losses has seven components: the general valuation allowance, criticized and classified allowance, the specific valuation allowance, large borrower risk allowance, pool loan allowance, Q factor allowance and the model risk allowance. Each of these components is determined based upon estimates that can and do change when the actual events occur.

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## CAPITAL (Continued)

The following table presents the Company's and the Bank's capital ratios as of December 31, 2005 and December 31, 2004.

| Ratio | (Dollars in thousands) |      |
|-------|------------------------|------|
|       | 2005                   | 2004 |

| Tier 1 Leverage Ratio                                  |           |        |
|--|-----------|--------|
| Central Valley Community Bancorp and Subsidiary        | \$ 31,767 | 6.84%  |
| Minimum regulatory requirement                         | \$ 18,572 | 4.00%  |
| Central Valley Community Bank                          | \$ 32,493 | 7.00%  |
| Minimum requirement for "Well-Capitalized" institution | \$ 23,204 | 5.00%  |
| Minimum regulatory requirement                         | \$ 18,563 | 4.00%  |
| Tier 1 Risk-Based Capital Ratio                        |           |        |
| Central Valley Community Bancorp and Subsidiary        | \$ 31,767 | 9.26%  |
| Minimum regulatory requirement                         | \$ 13,719 | 4.00%  |
| Central Valley Community Bank                          | \$ 32,493 | 9.48%  |
| Minimum requirement for "Well-Capitalized" institution | \$ 20,572 | 6.00%  |
| Minimum regulatory requirement                         | \$ 13,715 | 4.00%  |
| Total Risk-Based Capital Ratio                         |           |        |
| Central Valley Community Bancorp and Subsidiary        | \$ 35,106 | 10.24% |
| Minimum regulatory requirement                         | \$ 27,437 | 8.00%  |
| Central Valley Community Bank                          | \$ 35,832 | 10.45% |
| Minimum requirement for "Well-Capitalized" institution | \$ 34,287 | 10.00% |
| Minimum regulatory requirement                         | \$ 27,429 | 8.00%  |

## LIQUIDITY

Liquidity management involves our ability to meet cash flow requirements arising from fluctuations in deposit levels and demands of daily operations, which include funding of securities purchases, providing for customers' credit needs and ongoing repayment of borrowings. Our liquidity is actively managed on a daily basis and reviewed periodically by our management and Directors' Asset/Liability Committee. This process is intended to ensure the maintenance of sufficient funds to meet our needs, including adequate cash flow for off-balance sheet commitments.

Our primary sources of liquidity are derived from financing activities which include the acceptance of customer and, to a lesser extent, broker deposits, federal funds facilities and advances from the Federal Home Loan Bank of San Francisco. These funding sources are augmented by payments of principal and interest on loans, the routine maturities and paydowns of securities from the securities portfolio, the stability of our core deposits and the ability to sell investment securities. Primary uses of funds include withdrawal of and interest payments on deposits, origination and purchases of loans, purchases of investment securities, and payment of operating expenses.

As a means of augmenting our liquidity, we have established Federal funds lines with correspondent banks. At December 31, 2005 our available borrowing capacity includes approximately \$14,100,000 in Federal funds lines with our correspondent banks and \$2,311,000 in unused TILB advances. We believe our liquidity sources to be stable and adequate. At December 31, 2005, we were not aware of any information that was reasonably likely to have a material effect on our liquidity position.

## OFF-BALANCE SHEET ITEMS

In the ordinary course of business, the Company is a party to financial instruments with off-balance risk. These financial instruments include commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The balance of commitments to extend credit on undischarged construction and other loans and letters of credit was \$133,956,000 as of December 31, 2005 compared to \$107,816,000 as of December 31, 2004. For a fuller discussion of these financial instruments, see Note 10 - Commitments and Contingencies to the Company's audited consolidated financial statements on page 18.

In the ordinary course of business, the Company is party to various operating leases. For a fuller discussion of these financial instruments, see Note 10 - Commitments and Contingencies to the Company's audited consolidated financial statements on page 18.

The liquidity of the parent company, Central Valley Community Bancorp is primarily dependent on the payment of cash dividends by its subsidiary, Central Valley Community Bank, subject to limitations imposed by the regulations.

| Credit Lines  | (In thousands)    |                   |
|---|-------------------|-------------------|
|   | December 31, 2005 | December 31, 2004 |
| Unsecured (Credit Lines (interest rate varies with market))                         | \$14,100          | \$ -              |
| Federal Home Loan Bank Collateral pledged   | \$6,680           | \$9,668           |
| Fair Value of Collateral at prevailing interest rate                                | \$6,598           | \$9,822           |
| Federal Reserve Bank Collateral pledged (interest rate at prevailing interest rate) | \$3,350           | \$3,504           |
| Fair Value of Collateral  | \$3,252           | \$3,456           |
| Collateral pledged  | \$4,000           | \$6,000           |
| Fair Value of Collateral  | \$9,822           | \$6,000           |

The following table reflects the Company's credit lines, balances outstanding, and pledged collateral at December 31, 2005 and December 31, 2004:

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## LOANS (Continued)

### Allowance for Credit Losses - (continued)

The following table sets forth information regarding our allowance for credit losses at the dates and for the periods indicated:

| (Dollars in thousands)                                       | For the Years Ending December 31, |          |
|--|-----------------------------------|----------|
|  | 2005                              | 2004     |
| Balance, beginning of the year                               | \$ 2,697                          | \$ 2,425 |
| Addition from merger with BMC                                | 751                               | -        |
| Provision charged to operations                              | 510                               | -        |
| Losses charged to the allowance                              | (787)                             | (24)     |
| Recoveries on loans previously charged off                   | 168                               | 296      |
| Balance, end of period                                       | \$ 3,339                          | \$ 2,697 |
| Ratio of non-performing loans to allowance for credit losses | 18.5%                             | N/A      |
| Allowance for credit losses to total loans                   | 1.11%                             | 1.29%    |

As of December 31, 2005 the balance in the allowance for credit losses was \$3,339,000 compared to \$2,697,000 as of December 31, 2004. The increase result from the incorporation of the allowance for credit losses from the merger with BMC into the Bank's allowance and the \$510,000 additional provision, offset by net charge-offs totaling \$619,000. The balance of commitments to extend credit on undisbursed construction and other loans and letters of credit was \$133,956,000 as of December 31, 2005 compared to \$107,816,000 as of December 31, 2004. Risks and uncertainties exist in all lending transactions, and even though there have historically been no charge offs on construction and other loans that have not been fully disbursed, our management and Directors' Loan Committee have established reserve levels based on historical losses as well as economic uncertainties and other risks that exist as of each reporting period.

As of December 31, 2005 the allowance was 1.11% of total gross loans compared to 1.29% as of December 31, 2004. Some shift occurred in the concentration of real estate loans without an offsetting increase in the allocated allowance. However, based on the Company's historical low rate of real estate charge offs, management feels the current allocation is adequate. Assumptions regarding the collateral value of various under performing loans may affect the level and allocation of the allowance for credit losses in future periods. The allowance may also be affected by trends in the amount of charge offs experienced or expected trends within different loan portfolios. The allowance for credit losses as a percentage of non-performing loans was 542% as of December 31, 2005. There were no non-performing loans as of December 31, 2004. Management believes the allowance at December 31, 2005 is adequate based upon its ongoing analysis of the loan portfolio, historical loss trends and other factors. However, no assurance can be given that the Company may not sustain charge-offs which are in excess of the allowance in any given period.

## DEPOSITS AND BORROWINGS

Total deposits increased \$104,803,000 or 32.1% to \$430,989,000 as of December 31, 2005 compared to \$326,186,000 as of December 31, 2004. Interest bearing deposits increased \$57,034,000 or 25.8% to \$277,985,000 as of December 31, 2005 compared to \$220,951,000 as of December 31, 2004. Non-interest bearing deposits increased \$47,769,000 or 45.4% to \$153,004,000 as of December 31, 2005 compared to \$105,235,000 as of December 31, 2004. The increase in deposits attributable to the BMC merger is approximately \$63,769,000. The remaining growth is consistent with our strategy to grow our core deposit base and has occurred because of growth in our retail banking offices. In the merger with BMC we acquired 2 branches located in Oakhurst and Madera, California. We plan to open an additional branch in the first quarter of 2006 in downtown Fresno, California.

The composition of the deposits and average interest rates paid at December 31, 2005 and December 31, 2004 is summarized in the table below.

|                        | December 31, 2005      |                           |                | December 31, 2004 |                          |                |
|------------------------|------------------------|---------------------------|----------------|-------------------|--------------------------|----------------|
|                        | Dollars                | Percent of Total Deposits | Effective Rate | Dollars           | Percent of Total Deposit | Effective Rate |
|                        | (Dollars in thousands) |                           |                |                   |                          |                |
| NOW accounts           | \$ 56,991              | 13.2%                     | 0.10%          | \$ 52,571         | 16.1%                    | 0.10%          |
| MMA accounts           | 108,024                | 25.1%                     | 1.35%          | 89,904            | 27.5%                    | 0.78%          |
| Time deposits          | 88,581                 | 20.5%                     | 2.55%          | 57,958            | 17.8%                    | 1.72%          |
| Savings deposits       | 24,389                 | 5.7%                      | 0.34%          | 20,518            | 6.3%                     | 0.35%          |
| Total Interest-bearing | 277,985                | 64.5%                     | 1.37%          | 220,951           | 67.7%                    | 0.85%          |
| Non-interest bearing   | 153,004                | 35.5%                     |                | 105,235           | 32.3%                    |                |
| Total deposits         | \$430,989              | 100.0%                    |                | \$326,186         | 100.0%                   |                |

Short-term borrowings totaled \$3,250,000 as of December 31, 2005 compared to \$2,000,000 as of December 31, 2004. Short term borrowings include \$1,250,000 in principal payments coming due in 2006 on the loan with a major bank (described below) and \$2,000,000 in FHLB advances maturing in the next twelve months. We maintain a line of credit with the FHLB collateralized by commercial loans and government securities. Refer to Liquidity below for further discussion of FHLB advances.

Long-term debt, which consisted of payments coming due in 2007 on a loan with a major bank, described below, and \$2,000,000 in FHLB advances maturing in 2007, totaled \$3,250,000 as of December 31, 2005 compared to \$6,500,000 as of December 31, 2004.

On December 17, 2004, the Company entered into a non-revolving loan agreement with a major bank under which the Company borrowed \$2,500,000 and contributed \$2,000,000 of additional capital to the Bank. The loan bears interest indexed to prime or LIBOR, at the Company's election. Further terms and conditions of the loan agreement were outlined in Report on Form 8-K filed on December 22, 2004. The purpose of the borrowing was to ensure the Bank's capital ratios remain at or above well capitalized after the effective date of the merger with BMC. Refer to Note 8 to the audited Consolidated Financial Statements on page 17.

## CAPITAL

Our stockholders' equity increased to \$41,523,000 as of December 31, 2005 compared to \$29,606,000 as of December 31, 2004. The increase in stockholders' equity is a result of net income of \$6,014,000 for 2005 combined with the increase in common stock from the merger with BMC, and proceeds from the exercise of stock options.

During the period the Company's borrowings remains outstanding, which is expected to be until approximately 2007, the Bank does not anticipate paying dividends to the Company except for dividends that are necessary to meet the ordinary and usual operating expenses of the Company provided that the Bank would not pay any dividend that would cause it to be deemed not "well capitalized" under applicable banking laws and regulations.

Management considers capital requirements as part of its strategic planning process. The strategic plan calls for continuing increases in assets and liabilities, and the capital required may therefore be in excess of retained earnings. The ability to obtain capital is dependent upon the capital markets as well as our performance. Management regularly evaluates sources of capital and the timing required to meet its strategic objectives.

# Management's Discussion and Analysis of Financial Condition and Results of Operations

## CRITICAL ACCOUNTING POLICIES (Continued)

presented in Note 1 of the audited Consolidated Financial Statements require management to make difficult, subjective or complex judgements or estimates.

### Use of Estimates

The preparation of these financial statements requires management to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. On an ongoing basis, management evaluates the estimates used. Estimates are based upon historical experience, current economic conditions and other factors that management considers reasonable under the circumstances.

These estimates result in judgements regarding the carrying values of assets and liabilities when these values are not readily available from other sources, as well as assessing and identifying the accounting treatments of contingencies and commitments. Actual results may differ from these estimates under different assumptions.

### Accounting Principles Generally Accepted in the United States of America

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP").

We follow accounting policies typical to the commercial banking industry and in compliance with various regulation and guidelines as established by the Public Company Accounting Oversight Board ("PCAOB"), Financial Accounting Standards Board ("FASB"), the American Institute of Certified Public Accountants ("AICPA"), and the Bank's primary federal regulator, the FDIC. The following is a brief description of our current accounting policies involving significant management judgements.

### Allowance for Credit Losses

Our most significant management accounting estimate is the appropriate level for the allowance for credit losses. The allowance for credit losses is established to absorb known and inherent losses attributable to loans outstanding. The adequacy of the allowance is monitored on an ongoing basis and is based on our management's evaluation of numerous factors. These factors include the quality of the current loan portfolio, the trend in the loan portfolio's risk ratings, current economic conditions, loan concentrations, loan growth rates, past-due and non-performing trends, evaluation of specific loss estimates for all significant problem loans, historical charge-off and recovery experience and other pertinent information.

The calculation of the allowance for credit losses is by nature inexact, as the allowance represents our management's best estimate of the losses inherent in our credit portfolios at the reporting date. These credit losses will occur in the future, and as such cannot be determined with absolute certainty at the reporting date.

### Amortization of Premiums on Investments

We invest in Collateralized Mortgage Obligations ("CMO") and Mortgage Backed Securities, ("MBS") as part of the overall strategy to increase our net interest margin. CMOs and MBS by their nature react to changes in interest rates. In a declining rate environment, prepayments from MBS and CMOs would be expected to increase and the expected life of the investment would be expected to shorten. Conversely, if interest rates increase, prepayments would be expected to decline and the average life of the MBS and CMOs would be expected to extend. Premium amortization of these investments affects our net interest income. Our management monitors the prepayment speed of these investments and adjusts premium amortization based on several factors. These factors include the type of investment, the investment structure, interest rates, interest rates on new mortgage loans, expectation of interest rate changes, current economic conditions, level of principal remaining on the bond, the bond coupon rate, the bond origination date, and volume of available

bonds in market. The calculation of premium amortization is by nature inexact, and represents management's best estimate of principal paydowns inherent in the total investment portfolio.

### Goodwill

Business combinations involving the Company's acquisition of the equity interests or net assets of another enterprise or the assumption of net liabilities in an acquisition of branches constituting a business may give rise to goodwill. Goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed in transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Company's ability to generate net earnings after the acquisition. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed for impairment at a reporting unit level at least annually. While the Company believes all assumptions utilized in its assessment of goodwill for impairment are reasonable and appropriate, changes could cause the Company to record impairment in the future.

### Stock Based Compensation

Under Accounting Practice Bulletin No.25, compensation cost for stock options is measured as the excess, if any, of the fair market value of our stock at the date of the grant over the amount required to be paid to the Company by the optionee upon exercising the option. Because our stock option plan provides for the issuance of options at a price of no less than the fair market value at the date of the grant, no compensation cost is required to be recognized for the stock option plan on the date of the grant. See Note 1 to the audited Consolidated Financial Statements for further information on pages 12 through 14.



# Management's Discussion and Analysis

## of Financial Condition and Results of Operations

### CONTRACTUAL OBLIGATIONS

The following summarizes the Company's long-term contractual obligations at December 31, 2005:

| (In thousands)  | Less than |           |           |            |           |
|---|-----------|-----------|-----------|------------|-----------|
|   | 1 year    | 1-3 years | 3-5 years | Thereafter | Total     |
| Time deposits   | \$ 70,615 | \$ 13,549 | \$ 4,417  | \$ -       | \$ 88,581 |
| FHLB Advances   | 2,000     | 2,000     | -         | -          | 4,000     |
| Other long-term debt                                    | 1,250     | 1,250     | -         | -          | 2,500     |
| Deferred Compensation Liability (1)                     | 1,366     | 81        | -         | -          | 1,447     |
| Salary Continuation Liability                           | 1,293     | -         | -         | -          | 1,293     |
| Obligations reflected on Consolidated Balance Sheet     | \$ 70,524 | \$ 16,880 | \$ 4,417  | \$ -       | \$ 97,821 |
| Operating lease obligations                             | \$ 600    | \$ 997    | \$ 672    | \$ 624     | \$ 2,893  |
| Obligations not reflected on Consolidated Balance Sheet | \$ 600    | \$ 997    | \$ 672    | \$ 624     | \$ 2,893  |

(1) These amounts represent the current accrual for payment to participants under the Company's deferred compensation and salary continuation plans. See Note 13 to the audited Consolidated Financial Statements on page 20 for additional information related to the Company's deferred compensation and salary continuation plans.

### QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest rate risk ("IRR") and credit risk constitute the two greatest sources of financial exposure for insured financial institutions. IRR represents the impact that changes in absolute and relative levels of market interest rates may have upon our net interest income ("NII"). Changes in the NII are the result of changes in the net interest spread between interest-earning assets and interest-bearing liabilities (timing risk), the relationship between various rates (basis risk), and changes in the shape of the yield curve.

We realize income principally from the differential or spread between the interest earned on loans, investments, other interest-earning assets and the interest incurred on deposits and borrowings. The volumes and yields on loans, deposits and borrowings are affected by market interest rates. As of December 31, 2005, 82% of our loan portfolio was tied to adjustable rate indices. The majority of these adjustable rate loans are tied to prime and reprice within 90 days. The majority of our time deposits have a fixed rate of interest. As of December 31, 2005, 80% of our time deposits mature within one year or less. As of December 31, 2005, \$2,000,000 of our long term debt was fixed rate with an average remaining term of 1.1 years and \$1,250,000 of long term debt reprices on a quarterly basis.

Changes in the market level of interest rates directly and immediately affect our interest spread, and therefore profitability. Sharp and significant changes to market rates can cause the interest spread to shrink or expand significantly in the near term, principally because of the timing differences between the adjustable rate loans and the maturities (and therefore repricing) of the deposits and borrowings.

Our management and Board of Director's Asset/Liability Committees ("ALCO") are responsible for managing our assets and liabilities in a manner that balances profitability, IRR and various other risks including liquidity. The ALCO operates under policies and within risk limits prescribed by, reviewed and approved by the Board of Directors.

The ALCO seeks to stabilize our NII by matching rate-sensitive assets and liabilities through maintaining the maturity and repricing of these assets and liabilities at appropriate levels given the interest rate environment. When the amount of rate-sensitive liabilities exceeds rate-sensitive assets within specified time periods, NII generally will be negatively impacted by an increasing interest rate environment and positively impacted by a decreasing interest rate environment. Conversely, when the amount of rate-sensitive assets exceeds the amount of rate-sensitive liabilities within specified time periods, net interest income will

generally be positively impacted by an increasing interest rate environment and negatively impacted by a decreasing interest rate environment. The speed and velocity of the repricing of assets and liabilities will also contribute to the effects on our NII, as will the presence or absence of periodic and lifetime interest rate caps and floors.

Simulation of earnings is the primary tool used to measure the sensitivity of earnings to interest rate changes. Earnings simulations are produced using a software model that is based on actual cash flows and repricing characteristics for all of our financial instruments and incorporate market-based assumptions regarding the impact of changing interest rates on current volumes of applicable financial instruments.

Interest rate simulations provide us with an estimate of both the dollar amount and percentage change in NII under various rate scenarios. All assets and liabilities are normally subjected to up to 300 basis point increases and decreases in interest rates in 100 basis point increments. Under each interest rate scenario, we project our net interest income. From these results, we can then develop alternatives in dealing with the tolerance thresholds.

Approximately 82% of our loan portfolio is tied to adjustable rate indices and 61% of our loan portfolio reprices within 90 days. As of December 31, 2005, we had 136 commercial and real estate loans totaling \$35,630,000 with floors ranging from 1% to 8% and ceilings ranging from 8% to 25%. In the current rate environment, the number of loans affected by floors and ceilings is minimal.

The following table shows the effects of changes in projected net interest income for the twelve months ending December 31, 2006 under the interest rate shock scenarios stated. The table was prepared as of December 31, 2005, at which time prime interest rate was 7.25%.

### Sensitivity analysis of impact on interest income of rate changes

| Hypothetical Change In Rates | Projected Net Interest Income | \$ Change From Rates At Dec. 31, 2005 | % Change From Rates At Dec. 31, 2005 |
|------------------------------|-------------------------------|---------------------------------------|--------------------------------------|
| (Dollars in thousands)       |                               |                                       |                                      |
| UP 300 bp                    | \$30,594                      | \$4,948                               | 19.29%                               |
| UP 200 bp                    | 28,297                        | 2,652                                 | 10.34%                               |
| UP 100 bp                    | 26,450                        | 804                                   | 3.13%                                |
| UNCHANGED                    | 25,646                        | -                                     | -                                    |
| DOWN 100 bp                  | 24,464                        | (1,181)                               | -4.61%                               |
| DOWN 200 bp                  | 22,582                        | (3,063)                               | -11.95%                              |
| DOWN 300 bp                  | 20,670                        | (4,976)                               | -19.40%                              |

Assumptions are inherently uncertain, and, consequently, the model cannot precisely measure net interest income or precisely predict the impact of changes in interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude and frequency of interest rate changes, as well as changes in market conditions and management strategies which might moderate the negative consequences of interest rate deviations. In the model above, the simulation shows that the Company is neutral over the one-year horizon. If interest rates increase or decline, there will be similar positive and negative impact to net interest income.

There is no material change in our current market risk exposure from the market risk exposure we experienced in 2005.

### CRITICAL ACCOUNTING POLICIES

The Securities and Exchange Commission ("SEC") issued disclosure guidance for "critical accounting policies". The SEC defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgements, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods.

Our accounting policies are integral to understanding the results reported. Our significant accounting policies are described in detail in Note 1 of the Company's audited Consolidated Financial Statements, pages 12 through 14. Not all of the significant accounting policies

# Board of Directors

**Daniel N. Cunningham**  
Chairman of the Board  
Vice President and Director  
Quinn Properties, Inc.  
Director, Quinn Group, Inc.

**Sidney B. Cox**  
Owner  
Cox Communications

**Edwin S. Darden, Jr.**  
President  
Edwin S. Darden Associates

**Daniel J. Doyle**  
President and CEO  
Central Valley Community Bancorp,  
Central Valley Community Bank

**Steven D. McDonald**  
President  
McDonald Properties, Inc.

**Louis McMurray**  
President  
Charles McMurray Co.

**Wanda L. Rogers**  
President  
Rogers Helicopters, Inc.

**William Smittcamp**  
President/Owner  
Wawona Frozen Foods

**Joseph B. Weirick**  
Investments

*Leadership*

*Integrity*

*Loyalty*

*Caring*

*Teamwork*

*Trustworthy Business*



**Edwin Darden**

**Wanda L. Rogers**

**Steven D. McDonald**

**Louis McMurray**

**Sidney B. Cox**

**Joseph B. Weirick**

**William Smittcamp**

## Stock Price Information

## Exceptional Employees

### STOCK PRICE INFORMATION

The Company's common stock is listed for trading on the NASDAQ SmallCap Market under the ticker symbol CVCY. As of February 28, 2006 the Company had approximately 390 shareholders of record.

The following table shows the high and low bid prices for the common stock for each quarter as reported by NASDAQ. The prices have been adjusted to reflect a two-for-one stock split on October 31, 2005.

Sales Prices for  
the Company's Common Stock

| Quarter Ended      | Low      | High     |
|--------------------|----------|----------|
| March 31, 2004     | \$ 10.25 | \$ 13.50 |
| June 30, 2004      | 11.50    | 12.50    |
| September 30, 2004 | 11.00    | 15.00    |
| December 31, 2004  | 11.38    | 13.43    |
| March 31, 2005     | 11.25    | 13.12    |
| June 30, 2005      | 11.06    | 16.36    |
| September 30, 2005 | 11.00    | 14.98    |
| December 31, 2005  | 13.95    | 16.00    |

On October 31, 2005, we effected a two-for-one stock split. The Company did not pay any cash dividends in 2005. The Company paid \$0.05 per share cash dividends in 2004 and 2003.

#### Market Makers

Inquiries on Central Valley Community Bancorp stock can be made by calling Troy Norlander with The Seidler Companies at (800) 288-2811, Jeffrey Mayer with The Seidler Companies at (559) 449-2777, Joey Warmenhoven with Wedbush Morgan Securities at (503) 675-3100, or Dave Bonaccorso at Hoelzer & Arnett at (800) 346-5544 ext. 223. Central Valley Community Bancorp stock can also be purchased through any licensed stockbroker.

#### Shareholder Inquiries

Inquiries regarding Central Valley Community Bancorp's accounting, internal controls or auditing concerns should be directed to Steven D. McDonald, chairman of the Board of Directors' Audit Committee, at [steve.mcdonald@cvcb.com](mailto:steve.mcdonald@cvcb.com), anonymously at [www.ethicspoint.com](http://www.ethicspoint.com) or call Ethics Point, Inc. at (866) 294-9588.

General inquiries about the Company or the Bank should be directed to Cathy Ponte, Assistant Corporate Secretary at (800) 298-1775.

### EXCEPTIONAL EMPLOYEES

Central Valley Community Bank could not continue to achieve unprecedented growth and financial success without an outstanding team of employees. We pride ourselves on the strength of our team and are proud of its continued commitment and dedication to providing superior customer service and community support.

Each year Central Valley Community Bank's top-performing employees are recognized in the Circle of Excellence, and from that group, the best are designated to the Circle of Elite.

The 2005 Circle of Elite included:

Jacque Ashjian  
*Vice President, Credit Administration*

Donna Bridges  
*Customer Service Supervisor*

Terry Crawford  
*Vice President, Agribusiness Loan Officer*

Dawn Crusinberry  
*Assistant Vice President, Assistant Controller*

Jean Ornelas  
*Vice President, Senior Construction Loan Officer*

Carol Van Ness  
*Customer Service Representative*

Jeannine Welton  
*Vice President, Branch Manager*

Central Valley  
**Community  
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**Fig Garden Village**

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(559) 221-2760

**Foothill**

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Prather, CA 93651  
(559) 855-4100

**Fresno Downtown**

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Fresno, CA 93721  
(559) 268-6806

**Herndon & Fowler**

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(559) 323-2200

**Kerman**

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Kerman, CA 93630  
(559) 842-2265

**Madera**

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(559) 673-0395

**Oakhurst**

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Oakhurst, CA 93644  
(559) 642-2265

**River Park**

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(559) 447-3350

**Sacramento**

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Gold River, CA 95670  
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**SBA Lending**

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(559) 323-3384

**Agribusiness**

8375 North Fresno Street  
Fresno, CA 93720  
(559) 439-3989

**Real Estate**

795 Pollasky Avenue  
Clovis, CA 93612  
(559) 323-3365

## Our Mission

### *As a Full Service Bank We Are Committed To:*

Providing the full range of financial products and services required by our customers

Contributing to the quality of life throughout the Central Valley communities we serve

Providing superior customer service to be delivered in a highly professional, but very personal, manner that promotes trust and confidence

Maintain a positive work environment for our team members

Continuing to maximize shareholder value

Being the Best we can be!

### **Independent Auditors**

Perry-Smith LLP, Sacramento, CA

### **Counsel**

Downey Brand LLP, Sacramento, CA

### **Holding Company and Bank Officers:**

Daniel J. Doyle  
President and Chief Executive Officer

Gayle Graham  
Senior Vice President, Chief Financial Officer

Thomas L. Sommer  
Senior Vice President, Credit Administrator

## Bank Officers:

Gary Quisenberry  
Senior Vice President,  
Commercial and  
Business Banking

Shirley Wilburn  
Senior Vice President,  
Consumer and  
Retail Banking

Shelle Abbott  
Vice President,  
Branch Manager

Jan Bowman  
Vice President,  
Branch Support Manager

Cyndi Carmichael  
Vice President,  
Compliance Officer

Vicki Casares  
Vice President,  
Branch Manager

Cathy Chatoian  
Vice President,  
Retail Banking Sales

Terry Crawford  
Vice President,  
Commercial Loan Officer

Stan Davis  
Vice President,  
Commercial Loan Officer

Ken Dodderer  
Vice President,  
Commercial Loan Officer

Steve Freeland  
Vice President,  
Special Assets Officer

Rod Geist  
Vice President,  
Branch Manager

Barbara Gillmore  
Vice President,  
Human Resources Director

Diane Hump  
Vice President,  
Loan Servicing Manager

Tim Harris  
Vice President,  
Private Banking Manager

Charles Jones  
Vice President,  
Branch Manager

Bernie Kraus  
Vice President,  
Commercial Loan Officer

Lesley Lang-Lopez  
Vice President,  
Manager SBA Department

Rona Melkus  
Vice President,  
Controller

Don Mendenhall  
Vice President,  
Commercial Loan Officer

Sheryl Michael  
Vice President,  
Branch Manager

Steve Morales  
Vice President,  
Manager Information Services

Jean Ornelas  
Vice President,  
Real Estate Construction  
Loan Officer

Jeff Pace  
Vice President,  
Manager Real Estate Division

Teresa Palsgaard  
Vice President,  
Business Development Officer

John Royal  
Vice President,  
Commercial Loan Officer

Elizabeth Salas  
Vice President,  
Branch Manager

Gerald Sullivan  
Vice President,  
Commercial Loan Officer

Theodore Thome  
Vice President,  
Private Banking Officer

Robert Walker  
Vice President,  
Commercial Loan Officer

Jeannine Welton  
Vice President,  
Branch Manager

Jennette Williams  
Vice President,  
Business Development Officer

Carol Worstein  
Vice President,  
Branch Manager

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