FEDERAL DEPOSIT INSURANCE CORPORATION

Washington, D.C. 20429

FORM 10-K

Mark One

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

For the fiscal year ended December 31, 2004

or

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

For the transition period from to .

PREFERRED BANK

(Exact name of registrant as specified in its charter)

California	33539	95-4340199
(State or other jurisdiction of incorporation or organization)	(FDIC Certificate Number)	(I.R.S. Employer Identification No.)

601 S. Figueroa Street, 20th Floor, Los Angeles, California	90017
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (213) 891-1188

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
NONE	NONE

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, No Par Value

(Title of class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☐ No ☒

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 or Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The aggregate market value of the registrant's common stock held by non-affiliates is approximately $162,330,926 (based on the March 29, 2005 closing price of the registrant's Common Stock of $38.23 per share on the Nasdaq National Market).

As of March 29, 2005, 6,637,404 shares of Preferred Bank Common Stock were outstanding.

The following documents are incorporated by reference herein:

Document Incorporated By Reference	Part of Form 10-K Into Which Incorporated
Definitive Proxy Statement for the Annual Meeting of Shareholders which will be filed within 120 days of the fiscal year ended December 31, 2004	Part III

TABLE OF CONTENTS

PART I		**1**
ITEM 1.	BUSINESS	1
ITEM 2.	PROPERTIES	31
ITEM 3.	LEGAL PROCEEDINGS	32
ITEM 4.	SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS	32
PART II		**33**
ITEM 5.	MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS	33
ITEM 6.	SELECTED FINANCIAL DATA	35
ITEM 7.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	37
ITEM 7A.	QUANTITATIVE AND QUALITATIVE DISCLOSURES OF MARKET RISKS	68
ITEM 8.	FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	68
ITEM 9.	CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	68
ITEM 9A.	CONTROLS AND PROCEDURES	68
ITEM 9B.	OTHER INFORMATION	68
PART III		**69**
ITEM 10.	DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT	69
ITEM 11.	EXECUTIVE COMPENSATION	69
ITEM 12.	SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS	69
ITEM 13.	CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS	69
ITEM 14.	PRINCIPAL ACCOUNTANT FEES AND SERVICES	69
PART IV		**70**
ITEM 15.	EXHIBITS AND FINANCIAL STATEMENT SCHEDULES	70
SIGNATURES		**96**

PART I

Certain matters discussed in this Annual Report on Form 10-K may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "1933 Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and as such, may involve risks and uncertainties. These forward-looking statements relate to, among other things, expectations of the environment in which the Bank operates and projections of future performance. The Bank's actual results, performance, or achievements may differ significantly from the results, performance, or achievements expected or implied in such forward-looking statements. For discussion of some of the factors that might cause such differences, see "Item 1. BUSINESS—Risk Factors That May Affect Future Results."

ITEM 1. BUSINESS

General

We are one of the largest independent commercial banks in California focusing on the Chinese-American market. We consider the Chinese-American market to encompass individuals born in the United States of Chinese ancestry, ethnic Chinese who have immigrated to the United States and ethnic Chinese who live abroad but conduct business in the United States.

We commenced operations in December 1991 in Los Angeles, California with initial capital of $20 million. At December 31, 2004, we had total assets of approximately $907.3 million, loans and leases of approximately $616.0 million, deposits of approximately $801.5 million and shareholders' equity of approximately $76.8 million. Net income per share on a fully diluted basis was $1.92 for the year ended December 31 as compared to $1.58 per share for the year ended December 31, 2003.

We provide personalized deposit services as well as real estate finance, commercial loans and trade finance to small and mid-sized businesses and their owners, entrepreneurs, real estate developers and investors, professionals and high net worth individuals. We believe we have benefited, and will continue to benefit from the significant migration to Southern California of ethnic Chinese from China and other areas of East Asia. We estimate that at December 31, 2004, approximately 68% of our non-governmental deposits and 31% of our loans were with customers from the Chinese-American market. While our business is not solely dependent on the Chinese-American market, it represents an important element of our operating strategy, especially for our branch network and deposit products and services.

On February 17, 2005, we completed our initial public offering ("IPO") of 2,438,000 shares of our common stock at $38.00 per share in a firm commitment underwritten offering. The number of shares sold included 318,000 shares sold pursuant to the underwriters' exercise of their over-allotment option. Of the 2,438,000 shares sold, Preferred Bank sold 985,622 shares and 1,452,378 shares were sold by certain selling shareholders. The net proceeds to us from our IPO of common stock were approximately $35 million (before expenses).

We plan to use the net proceeds from this offering for general corporate purposes, working capital, financing internal growth, possible future acquisitions of financial institutions, branch offices and loan portfolios; and establishing new branches and loan production offices.

Our main office is located at 601 S. Figueroa Street, 20th Floor, Los Angeles, CA 90017 and our telephone number is (213) 891-1188. Our internet address is *www.preferredbank.com*. On our website *www.preferredbank.com*, we post the following filings as soon as reasonably practicable after they are filed with or furnished to the Federal Deposit Insurance Corporation: our annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, our proxy statement related to our annual stockholders' meeting and any amendments to those reports or statements filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. All such filings on our website are available free of charge. The reference to our website address does not constitute

incorporation by reference of the information contained in the website and should not be considered part of this document. A copy of our Code of Personal and Business Conduct, including any amendments thereto or waivers thereof and Board Committee Charters can also be accessed on our website. We will provide, at no cost, a copy of our Code of Personal and Business Conduct and Board Committee Charters upon request by phone or in writing at the above phone number or address, attention: Chris Chan, Senior Vice President and Chief Financial Officer.

Our Customers

We provide a range of deposit and loan products and services to customers primarily within the following categories:

- *Real Estate Finance*—consisting of investors and developers within the real estate industry and of owner-occupied properties in Southern California. We provide construction loans and mini-perm loans for residential, commercial, industrial and other income producing properties. A portion of our real estate loans are to borrowers who are also international trade finance customers.
- *Middle Market Business*—consisting of manufacturing, service and distribution companies with annual sales of approximately $5 million to $100 million and with borrowing requirements of up to approximately $12 million. We offer a range of lending products to customers in this market, including working capital loans, equipment financing and commercial real estate loans. Additionally, we provide a full range of deposit products and related services including safe deposit boxes, account reconciliation, courier service and cash management services.
- *International Trade Finance*—consisting of importers and exporters based in the U.S. requiring both borrowing and operational products. We offer a full range of products to international trade finance customers, including commercial and standby letters of credit, acceptance financing, documentary collections, foreign draft collections, international wires and foreign exchange.
- *Private Banking*—consisting of wealthy individuals residing in the Pacific Rim area with residences, real estate investments or businesses in Southern California. We offer all of our banking products and services to this segment through our multi-lingual team of professionals knowledgeable in the business environment and financial affairs of Pacific Rim countries. We believe our language capabilities provide us with a competitive advantage.
- *Professionals*—consisting generally of physicians, accountants, attorneys, business managers and talent agents and other professionals associated with the entertainment industry. We provide specialized personal banking services to customers in this segment including courier service, several types of specialized deposit accounts and personal and business loans as well as lines of credit.

Our Market

From our main office in downtown Los Angeles, California and full-service branch banking offices in Los Angeles and Orange Counties, we market our services and conduct our business primarily in Los Angeles, Orange, Ventura, Riverside and San Bernardino counties, focusing on the areas with growing Chinese-American communities.

We believe that Chinese-Americans continue to be the largest Asian ethnic group in Los Angeles County. According to the U.S. Census 2000, between 1990 and 2000, the Chinese-American population in the United States grew by approximately 48% with 40% of all Chinese-Americans living in California. During this same period, it is estimated that the Chinese-American population in Los Angeles grew by 34%. According to the U.S. Census Bureau, as of 2003, 364,469 or approximately 30% of Asian-Americans living in Los Angeles County were Chinese-Americans (excluding Taiwanese).

As of 2003, Asian-Americans have attractive demographics with a higher nationwide median household income than all other groups ($55,262 vs. $43,318). According to the Bureau of Labor Statistics, in 2003, Asian-Americans have the highest percentage of college education of any group and the lowest unemployment rate of any ethnic group at 6.0%.

We believe that continuing consolidation of banks generally in Southern California, and among the banks serving the Chinese-American market in particular, has created an underserved market of small and mid-sized businesses, real estate developers and investors and high net worth depositors that we can continue to attract as customers.

We believe we are well positioned to compete effectively with the smaller Chinese-American community banks, the larger commercial banks and major publicly listed and foreign bank-owned Chinese banks operating in Southern California by offering the following:

- deposit and cash management services to high net worth depositors with a high degree of personal service and responsiveness;
- experienced, multi-lingual management team and staff who we believe can provide sophisticated credit solutions faster and more efficiently and with a higher degree of personal service than what is provided by our competition; and
- loan products to customers requiring credit of a size in excess of what can be provided by our competitors.

Our Strategy

We strive to continue operating as a high performing community bank for the long-term benefit of our shareholders, customers and employees. The key elements of our growth and operating strategy are to:

Growth Strategies

- *Continue to grow our real estate lending activities* by providing competitive commercial real estate loans, construction loans and other real estate loans. With the additional capital provided by this offering, we will have the ability to originate larger loans to new and existing customers.
- *Expand our franchise* by establishing new branches in Southern California. We plan to open two additional branches by the end of 2005.
- *Expand our commercial lending relationships* in an effort to increase our noninterest bearing deposit accounts and our noninterest income. We expect to enhance our commercial loan portfolio by expanding existing customer relationships, as well as by devoting additional marketing resources to the Chinese-American business community in Southern California.
- *Expand our portfolio of products and services to high net worth customers* who we believe prefer to address their deposit and credit needs in a personal manner with experienced, efficient and service-oriented bank officers.
- *Hire and retain experienced and qualified employees* to support our planned expansion of our business activities.

Operating Strategies

- *Maintain high asset quality* independent of production goals by continuing to utilize rigorous loan underwriting standards and credit risk management policies.
- *Access capital markets* as needed and enhance our equity-based compensation programs through the increased liquidity provided by being a public company.
- *Increase revenue opportunities* by increasing our investments in higher yielding floating rate loans and investment securities and reducing the percentage of our investments in federal funds sold and other overnight investments.

- *Increase our operating leverage* by:
- increasing our loan to deposit ratio by growing our loan portfolio;
- expanding sources of funding in addition to deposits to fund our loan and securities portfolios, such as borrowings from the Federal Home Loan Bank system;
- changing the mix of our securities and loan portfolios to reduce the effect of regulatory asset risk weighting consistent with our yield parameters to permit additional asset growth without requiring additional capital; and
- potentially reorganizing our corporate structure to form a bank holding company so that we may have greater access to the capital markets and benefit from the incremental operating flexibility provided by a bank holding company structure.

Our Lending Activities

We originate a variety of types of loans, most of which fall into the following four categories:

- Real estate mini-perm loans;
- Real estate construction loans;
- Commercial loans; and
- Trade finance.

In addition to these loan types, we make a small amount of consumer loans principally as an accommodation to our business customers. We also utilize our relationships within the banking industry to purchase and sell participations in syndicated loans that meet our underwriting criteria. During the year ended December 31, 2004, we purchased $80.6 million and sold $25.7 million in non-recourse loan participations. We manage our loan portfolio to provide for an adequate return, but also to provide a diversification of risk.

We originate our loans from our nine banking offices in Los Angeles and Orange counties. For mini-perm and construction loans, we rely on referrals from existing clients who are real estate investors and developers as well as our network of loan brokers. For our commercial and trade finance lending, we seek referrals from existing banking clients as well as referrals from professionals, such as certified public accountants, attorneys and business managers.

At December 31, 2004, 88% of our loans carried interest rates that adjust with changes in the Prime Rate, 10% carried interest rates tied to LIBOR or other indices and 2% carried a fixed rate. At December 31, 2004, $47.5 million of our loans had interest rate floors, which means that even if the Prime Rate falls below the contractual limit, the borrower is required to pay interest at the higher floor rate. At December 31, 2004, $43.7 million of our loans had interest rate ceilings, which means that even if the Prime Rate rises above the contractual limit, the borrower is only required to pay interest at the lower ceiling rate.

The following table sets forth information regarding our four major loan categories:

	At December 31, 2004
	(Dollars in thousands)
Real Estate Mini-Perm	
Portfolio size	$358,221
Number of loans	211
Average loan size	$ 1,698
Average LTV[1]	59.80%
Average DCR[2]	1.90%
Weighted average rate	6.19%
Real Estate Construction	
Portfolio size	$112,002
Number of loans	63
Average loan size	$ 1,778
Average LTV[1]	58.14%
Average DCR[2]	1.92%
Weighted average rate	6.27%
Commercial Loans	
Portfolio size	$ 98,547
Number of loans	465
Average loan size	$ 212
Weighted average rate	5.64%
Trade Finance	
Portfolio size	$ 45,951
Number of loans	123
Average loan size	$ 374
Weighted average rate	5.68%

(1) Average loan-to-value, or LTV, is calculated based upon a weighted average of outstanding principal loan balances (for mini-perm loans) or commitment (for construction loans) divided by the most recent third party appraisal reports. Third party appraisal reports are only an estimate of the value of the property at the time the appraisal is made.

(2) Average debt coverage ratio, or DCR, is calculated based upon the net operating income of the property divided by the debt service.

We had 109 loans with outstanding principal balances between $1 million to $5 million, 22 loans between $5 million and $10 million, and 6 loans over $10 million as of December 31, 2004.

Real Estate Mini-Perm Loans

Real estate mini-perm loans secured by retail, office and residential properties have been the fastest growing segment of our loan portfolio and comprise 58% of our loan portfolio as of December 31, 2004. We believe the primary reason for this growth is strong demand for commercial and residential real estate in Southern California. We also have focused our marketing efforts on this loan type, especially since we believe competitive sources of such financing have reduced their participation for this type of loan due to the declining rate environment. We seek diversification through maintaining a broad base of borrowers and monitoring our exposure to various property types.

The following table sets forth the breakdown of our real estate mini-perm portfolio by property type:

Property Type	At December 31, 2004 Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial/Office	$ 76,820	12.47%
Industrial	53,882	8.75
Retail	106,716	17.33
Apartment 4+	38,967	6.33
Residential 1-4	34,654	5.63
Other	47,182	7.65
Total	$358,221	58.16%

The following table sets forth the maturity of our real estate mini-perm loan portfolio:

At December 31, 2004						
Less than					More than	Total Outstanding
1-Year	2-Years	3-Years	4-Years	5-Years	5-Years	Balance
(In thousands)						
$65,571	$60,493	$38,756	$47,243	$66,994	$79,164	$358,221

Loan Origination. The loan origination process for mini-perm loans begins by a loan officer collecting preliminary property information and financial data from a prospective borrower. After a preliminary deal sheet is prepared and approved by management, the loan officer collects the necessary third party reports such as appraisals, credit reports, environmental assessments and preliminary title reports as well as detailed financial information. We utilize third party appraisers from an appraiser list approved by our Board of Directors' loan committee. From that list, appraisers for loans under $1.2 million are selected by the individual loan officer, appraisers for loans between $1.2 million and $3.0 million are selected by the loan officer with the concurrence of the Chief Credit Officer and appraisers for loans over $3.0 million are selected by the Chief Credit Officer.

All appraisals for loans over $1 million are reviewed by an additional outside appraiser. Appraisals for loans under that amount are reviewed by internal staff. A credit memorandum is then prepared by summarizing all third party reports and preparing an analysis of the adequacy of primary and secondary repayment sources; namely the property DCR and LTV as well as the outside financial strength and cash flow of the borrower or guarantor(s). This completed credit memorandum is then submitted to an officer or committee having the appropriate authority for approval. For further information on our different levels of authority, see "—Loan Authorizations" below.

Once a loan is approved by the appropriate authority level, loan documents are drawn by our note department, which also funds the loan when approval conditions are met. On larger, relatively complex transactions, loan documents are prepared or reviewed by outside legal counsel.

Underwriting Standards. Our principal underwriting standards for real estate mini-perm loans are as follows:

- Maximum LTV of 80%-85%, depending on the property type. However, our practice is to lend at more conservative levels.
- Minimum DCR of 1.2-1.25, depending on the property type.
- Requirements of personal guarantees from the principals of closely-held entity.

Monitoring. We monitor our mini-perm portfolio in different ways. First, on loans over $2 million, we conduct site inspections and gather rent rolls and operating statements on the subject properties at least annually. Using this information, we evaluate a given property's ability to service present payment requirements, and we perform "stress testing" to evaluate the property's ability to service debt at higher debt levels. Second, on an annual basis, we request updated financial information from our borrowers and/or guarantors to monitor their financial capacity.

The vast majority of our mini-perm loans carry a five year maturity. However, it has been our practice to renew these loans for additional five-year periods based on a satisfactory payment record and an updated underwriting profile.

Real Estate Construction

We are an active construction lender with construction loans comprising 18% of the total loan portfolio as of December 31, 2004. Construction loans are typically short-term loans of up to 18 months for the purpose of funding the costs of constructing a building. Outstanding construction loans by property type are summarized as follows:

	At December 31, 2004	
Property Type	**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**
	(Dollars in thousands)	
Office	$ 19,593	3.18%
Retail	23,255	3.78
Industrial	4,203	.68
For sale attached residential	42,671	6.93
For sale detached residential	16,198	2.63
Apartment	5,757	.93
Special purpose	325	.05
Total	$112,002	18.18%

Loan Origination. The origination process for construction loans is identical to our real estate mini-perm origination process described above under "—Real Estate Mini-Perm Loans—Loan Origination," but with an additional step. We generally require a third party review of the developer's proposed building costs.

Underwriting Standards. Our underwriting standards for construction loans are identical to those described above under "—Real Estate Mini-Perm Loans—Underwriting Standards." For the for-sale-housing projects, however, the DCR requirement is not applicable. In addition, we require that the construction loan applicant has proven experience in the type of project we are considering. Finally, notwithstanding the maximum 80%-85% LTV discussed above under "—Real Estate Mini-Perm Loans—Underwriting Standards," we generally require a maximum 80% LTV for construction loans.

Monitoring. The monitoring of construction loans is accomplished under the supervision of our Chief Credit Officer. We engage third-party inspectors to report on the percentage of project completion as well as to evaluate whether the project is proceeding at an acceptable pace. The third-party inspector also recommends whether we should approve or disapprove disbursement request amounts. The third-party inspector produces monthly reports on each project that contain the evaluation and recommendation for each project. The Chief Credit Officer reviews each report and makes a final determination regarding the disbursement requests. All approved disbursements are funded by the note department.

Commercial Loans

We offer a variety of commercial loan products including lines of credit for working capital, term loans for capital expenditures and commercial and stand-by letters of credit. As of December 31, 2004, we had $98.5 million of commercial loans outstanding, which represented 16% of our overall loan portfolio. Lines of credit typically have

a 12 month commitment and are secured by the borrower's assets. In cases of larger commitments, an updated certificate from the borrower may be required to determine eligibility at the time of any given advance. Term loans seldom exceed 60 months, but in no case exceed the depreciable life of the tangible asset being financed.

Loan Origination. A commercial loan begins with a loan officer obtaining preliminary financial information from the borrower and guarantors and summarizing the loan request in a deal sheet. The deal sheet is then reviewed by senior management and/or those who have the loan authority to approve the credit. Following preliminary approval, the loan officer undertakes a formal underwriting analysis, including third party credit reports and asset verifications. From this information and analysis, a credit memorandum is prepared and submitted to an officer or committee having the appropriate approval authority for review. After approval, the note department prepares loan documentation reflecting the conditions of approval and funds the loan when those conditions are met.

Underwriting Standards. Our underwriting standards for commercial loans are designed to identify, measure and quantify the risk inherent in these types of credits. Our underwriting process and standards help us identify the primary and secondary repayment sources. The following are our major underwriting guidelines:

- Cash flow is our primary underwriting criteria. We require a minimum 1.5:1 DCR for our commercial loans. We also review trends in the borrower's sales levels, gross profit and expenses.
- We evaluate the borrower's financial statements to determine whether a given borrower's balance sheet provides for appropriate levels of equity and working capital.
- Since most of our borrowers are closely held companies, we require the principals to guarantee the company debt. Our underwriting process, therefore, includes an evaluation of the guarantor's net worth, income and credit history. Where circumstances warrant, we usually require guarantees be secured by collateral (generally with real estate).
- Where there is a reliance on the accounts receivable and inventory of a company, we evaluate their condition, which may include third party onsite audits.

Monitoring. For those borrowers whose credit availability is tied to a formula based on advances as a percentage of accounts receivable and inventory (typically 80% and 25%, respectively), we review monthly borrowing base certificates for both availability and turnover trends. Periodically, we also conduct third party onsite audits, the frequency of which is dependent on the individual borrower. On a quarterly basis, we monitor the financial performance of a borrower by analyzing the borrower's financial statements for compliance with financial covenants.

Trade Finance Credits

Our trade finance portfolio totaled $46.0 million, or approximately 7% of our total loan portfolio as of December 31, 2004. Of this amount, virtually all loans were made to U.S. based importers who are also our current borrowers or depositors. We also provide standby letters of credit and foreign exchange services to our clients. Our new trade finance credit relationships result from contacts and relationships with existing clients, CPAs and trade facilitators such as customs brokers. In many cases, the ability to generate new trade finance business is also a result of cultivated social contacts and extended family.

We offer the following services to importers:

- Commercial letters of credit;
- Import lines of credit;
- Documentary collections;
- International wire transfers; and
- Acceptances / trust receipt financing.

We offer the following services to exporters:

- Export letters of credit;
- Export finance;
- Documentary collections;
- Bills purchase program; and
- International wire transfers.

Loan Origination. Our trade finance origination process is equivalent to our commercial loan process. Since we lend only to U.S. based companies, our due diligence process is equivalent to that of our commercial loan process with an emphasis on evaluating and verifying the assets of the borrowers and principals.

Underwriting Standards. Trade finance underwriting standards are based on our commercial loan standards. Typically, these loans are secured by receivables and inventories with advance rates similar to that of commercial loans. In many cases, we also require real estate or cash as partial collateral to further enhance our collateral position. However, in underwriting these credits, we also analyze the borrower's working capital requirements with a greater focus on the trade cycle and seasonality of the inventory being imported. Often an importer needs to order product months in advance, which requires us to structure the credit to accommodate the issuance of letters of credit early in the season and to carry accounts receivable after shipping.

Monitoring. We monitor trade finance credits by reviewing monthly borrowing base certificates of accounts receivable and inventory for both availability and turnover trends and tracking loan covenants on a quarterly basis. To supplement our review of borrowing bases, we utilize the services of third party accounts receivable and inventory auditors for certain credits. Finally, it is accepted trade finance practice to fund the payment of letters of credit on a "tenor" basis. That means that an advance under the trade finance line has a maturity (commonly 90 days). This serves as a self-monitoring mechanism because a matured and unpaid advance is a possible indicator of poor accounts receivable and/or inventory turnover.

Loan Concentrations

As of December 31, 2004 and December 31, 2003, we had a concentration of loans secured by real estate. At those dates, real estate-related loans comprised 76% and 69%, respectively, of total loans. A substantial decline in the performance of the economy in general, or a decline in real estate values in the bank's primary market areas, in particular, could have an adverse impact on collectibility, increase the level of real estate-related non-performing loans or have other adverse effects which alone or in the aggregate could have a material adverse effect on our business, financial condition, results of operations and cash flows.

Our real estate loans by type of collateral are as follows:

	At December 31, 2004	
Property Type	**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**
	(Dollars in thousands)	
Office	$ 96,413	15.65%
Retail(1)	129,970	21.10
Industrial	58,085	9.43
1-4 family	93,523	15.18
Multi-family	44,724	7.26
Land/Special purpose(2)	47,508	7.72
Total	$470,223	76.34%

(1) Includes shopping centers, strip malls or stand-alone properties which house retailers.

(2) Examples, other than land, include hospitality and self-storage.

To manage the risks inherent in this concentration in our loan portfolio, we have adopted a number of policies and procedures. For example, we have adopted regulatory loan-to-value standards that must be met at the time of origination, which are summarized below:

Collateral Type	LTV Maximum
Occupied 1-4	90%
Unimproved land	65%
Land development	75%
Improved properties	85%
Construction	80-85%
Commercial construction	80%
1-4 SFR construction	85%

Our underwriting practice, however, is to lend at lower LTV's. At December 31, 2004, the weighted average LTV of our real estate portfolio based on LTVs at the time of origination was 59.10%.

Our practice is to require DCR's on commercial real estate loans of 1.2 to 1.25x, depending on the property type. We also underwrite our commercial real estate loans using a rate that is 1-2% greater than the proposed interest rate on the loan.

In addition, we have established certain concentration limits for our real estate lending activities by property type. Our other real estate loan limitations include out of area (California) lending at no more than 15% of our portfolio. At December 31, 2004, 3% of our real estate portfolio was secured by real estate located outside of California.

Loan Maturities

In addition to measuring and monitoring concentrations in our loan portfolio, we also monitor the maturities and interest rate structure of our portfolio. The following table shows the amounts of loans and leases outstanding as of December 31, 2004 which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. The table also presents, for loans and leases with maturities over one year, an analysis with respect to fixed interest rate loans and leases and floating interest rate loans and leases.

	At December 31, 2004				Rate Structure for Loans Maturing over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
	(In thousands)					
Real estate mini-perm	$ 65,565	$213,485	$79,170	$358,220	$13,844	$278,811
Real estate construction	77,362	34,640	—	112,002	—	34,640
Commercial	68,152	30,012	384	98,548	117	30,279
Trade finance	42,929	3,022	—	45,951	—	3,022
Consumer	2	63	—	65	—	63
Leases receivable and other	462	713	—	1,175	713	—
Total	$254,472	$281,935	$79,554	$615,961	$14,674	$346,815

The following table shows the amounts of loans and leases outstanding as of December 31, 2003, which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. Demand or other loans having no stated maturity and no stated schedule of repayments are reported as due in one year or less. The table also presents, for loans and leases with maturities over one year, an analysis with respect to fixed interest rate loans and leases and floating interest rate loans and leases.

	At December 31, 2003				Rate Structure for Loans Maturing over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
			(In thousands)			
Real estate mini-perm	$ 53,952	$146,603	$50,438	$250,993	$16,590	$180,451
Real estate construction	67,156	27,660	—	94,816	—	27,660
Commercial	92,347	24,869	390	117,606	142	25,117
Trade finance	37,699	130	—	37,829	—	130
Consumer	25	97	—	122	9	88
Leases receivable and other	808	879	1,000	2,687	1,879	0
Total	$251,987	$200,238	$51,828	$504,053	$18,620	$233,446

As reflected in this data, the maturity of our portfolio is divided generally between loans maturing within one year or less and loans maturing between one and five years. Most of our shorter maturity loans are commercial, construction and trade finance loans. Most of the loans that have maturities between one and five years are real estate-mini perm loans. Regardless of maturity, most of our loans have interest rates that adjust with changes in the Prime Rate.

Loan Authorizations

- *Individual Authorities*. Individual loan officers have approval authority up to $750,000 for loans secured by first trust deeds or cash and up to $500,000 for unsecured transactions. The Chief Executive Officer and the Chief Credit Officer have combined approval authority up to $6.0 million for secured loans and up to $3.75 million for unsecured loans.
- *Management Loan Committee*. The Management Loan Committee consists of the Chief Executive Officer, the Chief Credit Officer and senior commercial and real estate lending officers. It has approval authority up to $10.0 million for secured loans and up to $6.0 million for unsecured loans.
- *Board of Directors Loan Committee*. Our Board of Directors loan committee consists of three members of the board of directors. It has approval authority up to our legal lending limit, which was approximately $20.0 million for secured loans and $12.0 million for unsecured loans at December 31, 2004. The Board of Directors loan committee also reviews all loan commitments granted in excess of $1 million on a quarterly basis for the preceding quarter.

All loan individual authorities are granted by the loan committee of our board of directors and are based on the individual's demonstrated credit judgment and lending experience.

If a credit falls outside of the guidelines set forth in our lending policies, the loan is not approved until it is reviewed by a higher level of credit approval authority. Credit approval authority has three levels, as listed above from lowest to highest level. Policy exceptions for cash flow, waiver of guarantee, excessive LTV or bad credit require approval of the President or Chief Credit Officer regardless of size.

We believe that the current authority levels provide satisfactory management and a reasonable percentage of secondary review. Any conditions placed on loans in the approval process must be satisfied before our Chief

Credit Officer will release loan documentation for execution. Our Chief Credit Officer and his staff work entirely independent of loan production and have full responsibility for all loan disbursements.

Loan Grading and Loan Review

We seek to quantify the risk in our lending portfolio by maintaining a loan grading system consisting of eight different categories (Grades 1-8). The grading system is used to determine, in part, the provision for loan losses. The first four grades in the system are considered satisfactory. The other four grades range from a "special mention" category to a "loss" category. These four grades are further discussed below under the section subtitled "classified assets."

The originating loan officer initially assigns a grade to each credit as part of the loan approval process. Such grade may be changed as a loan application moves through the approval process.

Prior to funding, all new loans of $1.0 million or over are reviewed by our Chief Credit Officer who may assign a different grade to the credit. The grade on each individual loan is reviewed at least annually by the loan officer responsible for monitoring the credit. The board of directors reviews monthly the aggregate amount of all loans graded as special mention, substandard or doubtful, and each individual loan that has a grade within such range. Additionally, changes in the grade for a loan may occur through any of the following means:

- monthly reviews by the Chief Credit Officer of a sample of loans approved under individual loan authority;
- annual reviews conducted by an outside loan reviewer of certain categories of loans determined by the Board of Directors' audit committee. In 2003 and 2004, the outside loan reviewer reviewed all loans to insiders in excess of $400,000, watch list credits in excess of $400,000 and a sample of larger loans in our loan portfolio;
- bank regulatory examinations; and
- monthly action plans submitted to the Chief Credit Officer by the responsible lending officers for each credit graded 5-8.

Loan Delinquencies. When a borrower fails to make a committed payment, we attempt to cure the deficiency by contacting the borrower to seek payment. Habitual delinquencies and loans delinquent 30 days or more are reviewed for possible changes in grading.

Classified Assets. Federal regulations require that each insured bank classify its assets on a regular basis. In addition, in connection with examinations of insured institutions, examiners have authority to identify problem assets, and, if appropriate, classify them. We use grades 5-8 of our loan grading system to identify potential problem assets. There were $4.5 million, $3.9 million and $6.5 million and $8.4 million in classified loans at December 31, 2004, December 31, 2003 and December 31, 2002, respectively.

The following describes grades 5-8 of our loan grading system:

- *Special Mention—Grade 5*. Generally these are assets that display negative trends or other causes for concern. This grade is regarded as a transition category. We will either upgrade the credit if meaningful progress is evident within six months, or downgrade the credit to a more severe grade as appropriate.
- *Substandard—Grade 6*. These are assets that in management's judgment have potential weaknesses that may result in deterioration of the repayment prospects and, therefore, deserve the attention of management. Usually, these assets are long-term problems that are likely to remain and require management action plans. These loans exhibit an increasing reliance on collateral for repayment.
- *Doubtful—Grade 7*. These assets are inadequately protected by the current worth and paying capacity of the borrower or of the collateral pledged, if any. Although loss may not be imminent, if the weaknesses are not corrected, there is a good possibility that we will sustain some loss.

- *Loss—Grade 8*. Assets classified as "loss" are considered uncollectible and of such little value in the near term that their continuance as active assets is not warranted. This does not mean they have no recovery or salvage value.

Deposit Products and Other Sources of Funds

Our primary sources of funds for use in our lending and investment activities consist of:

- deposits and related services;
- maturities and principal and interest payments on loans and securities; and
- other borrowings.

We closely monitor rates and terms of competing sources of funds and utilize those sources we believe to be the most cost effective, consistent with our asset and liability management policies.

Deposits and Related Services. We have historically relied primarily upon, and expect to continue to rely primarily upon, deposits to satisfy our needs for sources of funds. An important balance sheet component impacting our net interest margin is the composition and cost of our deposit base. We can improve our net interest margin to the extent that growth in deposits can be focused in the less volatile and somewhat more traditional core deposits, or total deposits less CDs greater than $100,000, commonly referred to as Jumbo CDs.

We provide a wide array of deposit products. We offer regular checking, savings, NOW and money market deposit accounts; fixed-rate, fixed maturity retail certificates of deposit ranging in terms from 14 days to five years; and individual retirement accounts and non-retail certificates of deposit consisting of Jumbo CDs. We attempt to price our deposit products in order to promote deposit growth and satisfy our liquidity requirements. We provide courier service to pick up non-cash deposits, and for those customers that use large amounts of cash, we arrange for armored car and vault service.

We provide a high level of personal service to our high net worth individual customers who have significant funds available to invest. Based on balances as of December 31, 2004, 46% of our deposit portfolio was from Jumbo CDs, as compared to 43% at December 31, 2003. We believe our Jumbo CDs are a stable source of funding because they are based primarily on service and personal relationships with senior bank officers rather than interest rate. Further, 6% of these Jumbo CDs are pledged as collateral for loans from us to the depositor or the depositor's affiliated business or family member. We monitor interest rates offered by our competitors and pay a rate we believe is competitive with the range of rates offered by such competitors.

We also receive a significant amount of our deposits from governmental agencies. At December 31, 2004, we had $59.0 million in government agency deposits, or 7% of our total deposits at that date. Generally, a condition to holding some of these deposits is that we must pledge qualifying government securities in the amount of 110% of the deposit we hold. At December 31, 2004, we had $46.1 million of government securities pledged for the benefit of our government agency deposits.

From time to time, we also access the deposit broker market for deposits to meet short-term liquidity requirements. At December 31, 2004, we held $25.0 million of deposits obtained in this manner. There were no significant rate differences between the rates on these deposits as compared to our internally generated Jumbo CDs.

We intend to focus our efforts on attracting deposits from our business lending relationships in order to reduce our cost of funds and improve our net interest margin. Also, we believe that we have the ability to attract sufficient additional funding by re-pricing the yields on our CDs in order to meet loan demands during times that growth rates in core deposits differ from loan growth rates.

In addition to the marketing methods listed above, we seek to attract new clients and deposits by:

- expanding long-term business customer relationships, including referrals from our customers, and
- building deposit relationships through our branch relationship officers.

Other Borrowings. We may occasionally use our federal funds lines of credit to support liquidity needs created by seasonal deposit flows, to temporarily satisfy funding needs from increased loan demand and for other short-term purposes. We have three federal funds lines with other financial institutions pursuant to which we can borrow up to $47.0 million on an unsecured basis. These lines may be terminated by the respective lending institutions at any time. At December 31, 2004, we had $0 outstanding under these federal funds lines.

We also borrow from the Federal Home Loan Bank, or FHLB, pursuant to an existing commitment based on the value of the collateral pledged (either loans or securities). FHLB borrowings have been only occasional and based upon pricing opportunities. We may utilize this source of funding in the future to a greater extent than we have in the past.

Our Investment Activities

Our investment strategy is designed to be complementary to and interactive with our other strategies (*i.e.*, cash position; borrowed funds; quality, maturity, stability and earnings of loans; nature and stability of deposits; capital and tax planning). The target percentage for our investment portfolio is between 10% to 40% of total assets. Our general objectives with respect to our investment portfolio are to:

- achieve an acceptable asset/liability mix;
- provide a suitable balance of quality and diversification to our assets;
- provide liquidity necessary to meet cyclical and long-term changes in the mix of assets and liabilities;
- provide a stable flow of dependable earnings;
- maintain collateral for pledging requirements;
- manage and mitigate interest rate risk;
- comply with regulatory and accounting standards; and
- provide funds for local community needs.

Investment securities consist primarily of U.S. agency issues, investment grade corporate notes, municipal bonds and mortgage-backed securities. In addition, for bank liquidity purposes, we use (1) overnight federal funds, which are temporary overnight sales of excess funds to correspondent banks and (2) interest-bearing deposits at other financial institutions, which consist of certificates of deposit spread over many financial institutions to take advantage of 100% FDIC insured coverage.

All of our investment securities are classified as "available-for-sale" pursuant to SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Available for sale securities are reported at fair value, with unrealized gains and losses excluded from earnings and instead reported as a separate component of stockholders' equity. Held to maturity securities would be securities that we have both the intent and the ability to hold to maturity. These securities would be carried at cost adjusted for amortization of premium and accretion of discount.

Our securities portfolio is managed in accordance with guidelines set by our investment policy. Specific day-to-day transactions affecting the securities portfolio are managed by our Chief Financial Officer. In accordance with our written investment policy, all executions also require the prior written approval of the President. These securities activities are reviewed periodically, as needed, by our investment committee and are reported to our board of directors.

Our investment policy addresses strategies, types and levels of allowable investments and is reviewed and approved annually by our board of directors. It also limits the amount we can invest in various types of securities, places limits on average life and duration of securities, and limits the securities dealers with whom we can conduct business.

Our Concentrations / Customers

Except as described below, no individual or single group of related accounts is considered material in relation to our assets or deposits or in relation to our overall business. Approximately 77% of our loan portfolio at December 31, 2004 consisted of real estate-secured loans, including commercial loans secured by real estate, construction loans and real estate mini-perm loans. Moreover, our business activities are focused in Southern California. Consequently, our business is dependent on the trends of this regional economy, and in particular, the commercial real estate markets. At December 31, 2004, we had 137 loans in excess of $1 million each, totaling $477.3 million. These loans comprise approximately 18% of our loan portfolio by number of loans and 77% by total loans outstanding. Not including credit card and consumer overdraft lines, our average loan size is $793,170.

Excluding government deposits, brokered deposits and deposits as direct collateral for loans, 10 depositors held a total of $101.3 million in deposits or 12.6% of our total deposits. At December 31, 2004, besides these 10 depositors, we had 19 depositors who held in excess of $3.0 million for a total of $76.9 million or 9.6% of our total deposits.

Our Competition

The banking and financial services business in Southern California is highly competitive. Within the Chinese-American market, where we have a particular focus, competition is also intense. This increasingly competitive environment is a result primarily of growth in community banks, changes in regulation, changes in technology and product delivery systems, and the accelerating pace of consolidation among financial services providers. We compete for loans, deposits and customers with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions and other nonbank financial service providers. Many of these competitors are much larger in total assets and capitalization, have greater access to capital markets and offer a broader range of financial services than we can offer.

We also compete with three publicly listed Chinese-American banks, and subsidiary banks and branches of foreign banks, from countries such as Taiwan and China, many of which have greater lending limits, and a wider variety of products and services than us. We also compete with smaller Chinese-American community banks for both deposits and loans.

Competition for deposit and loan products remains strong from both banking and non-banking firms and this competition directly affects the rates of those products and the terms on which they are offered to consumers.

Technological innovation continues to contribute to greater competition in domestic and international financial services markets. Many customers now expect a choice of several delivery systems and channels, including telephone, mail, internet and ATMs.

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

Regulation and Supervision

The following discussion of statutes and regulations affecting banks is only a summary and does not purport to be complete. This discussion is qualified in its entirety by reference to such statutes and regulations. No assurance can be given that such statutes or regulations will not change in the future.

General

As a California state-chartered bank whose accounts are insured by the FDIC up to a maximum of $100,000 per depositor, we are subject to regulation, supervision and regular examination by the California Commissioner and the FDIC. In addition, while we are not a member of the Federal Reserve System, we are subject to certain regulations of the Federal Reserve Board, or the FRB. The regulations of these agencies govern most aspects of our business, including the making of periodic reports by us, and our activities relating to dividends, investments, loans, borrowings, capital requirements, certain check-clearing activities, branching, mergers and acquisitions, reserves against deposits and numerous other areas. Supervision, legal action and examination of us by the FDIC is generally intended to protect depositors and is not intended for the protection of shareholders.

Our earnings and growth are largely dependent on our ability to maintain a favorable differential or "spread" between the yield on our interest-earning assets and the rate paid on our deposits and other interest-bearing liabilities. As a result, our performance is influenced by general economic conditions, both domestic and foreign, the monetary and fiscal policies of the federal government, and the policies of the regulatory agencies, particularly the FRB. The FRB implements national monetary policies (such as seeking to curb inflation and combat recession) by its open-market operations in United States government securities, by adjusting the required level of reserves for financial institutions subject to its reserve requirements and by varying the discount rate applicable to borrowings by banks which are members of the Federal Reserve System. The actions of the FRB in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans deposits. The nature and impact of any future changes in monetary policies cannot be predicted.

The bank is also subject to the requirements and restrictions of various consumer laws, regulations and the Community Reinvestment Act, or CRA.

Capital Standards

The FDIC has risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets, and transactions, such as letters of credit and recourse arrangements, which are reported as off-balance-sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by one of several risk adjustment percentages, which range from 0.0% for assets with low credit risk, such as certain U.S. government securities, to 100.0% for assets with relatively higher credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets and off-balance-sheet items. The regulators measure risk-adjusted assets and off-balance-sheet items against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. Tier 1 capital consists of common stock, retained earnings, noncumulative perpetual preferred stock and minority interests in certain subsidiaries. Tier 2 capital may consist of a limited amount of the allowance for loan and lease losses and certain other instruments with some characteristics of equity. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies. Since December 31, 1992, the FDIC has required a minimum ratio of qualifying total capital to risk-adjusted assets and off-balance-sheet items of 8.0%, and a minimum ratio of Tier 1 capital to risk-adjusted assets and off-balance-sheet items of 4.0%. In addition, to be considered "well capitalized," an institution must maintain a minimum ratio of qualifying total capital to risk-adjusted assets and off-balance-sheet items of 10%, and a minimum ratio of Tier 1 capital to risk-adjusted assets and off-balance-sheet items of 6.0%.

In addition to the risk-based guidelines, the FDIC requires banking organizations to maintain a minimum amount of Tier 1 capital to average total assets, referred to as the leverage ratio. For a banking organization rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio is 3.0%. It is improbable, however, that an institution with a 3.0% leverage ratio would receive the highest rating by the regulators since a strong capital position is a significant part of the regulators' ratings. For all banking organizations not rated in the highest category, the minimum leverage ratio is at least 100 to 200 basis points above the 3.0% minimum. Thus, the effective minimum leverage ratio, for all practical purposes, is at least 4.0% or 5.0%. In addition, to be considered "well capitalized," an institution must maintain a minimum leverage ratio of 5.0%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the FDIC has the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

A bank that does not achieve and maintain the required capital levels may be issued a capital directive by the FDIC to ensure the maintenance of required capital levels. As discussed above, we are required to maintain certain levels of capital. The regulatory capital guidelines as well as our actual capitalization as of December 31, 2004 is as follows:

Leverage Ratio	
Preferred Bank	9.30%
Minimum requirement for "Well-Capitalized" institution	5.00%
Minimum regulatory requirement	4.00%
Tier 1 Risk-Based Capital Ratio	
Preferred Bank	9.33%
Minimum requirement for "Well-Capitalized" institution	6.00%
Minimum regulatory requirement	4.00%
Total Risk-Based Capital Ratio	
Preferred Bank	10.15%
Minimum requirement for "Well-Capitalized" institution	10.00%
Minimum regulatory requirement	8.00%

Prompt Corrective Action

Federal banking agencies possess broad powers to take corrective and other supervisory action to resolve the problems of insured depository institutions, including those institutions that fall below one or more prescribed minimum capital ratios described above. An institution that, based upon its capital levels, is classified as well capitalized, adequately capitalized or undercapitalized may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions.

In addition to measures taken under the prompt corrective action provisions, commercial banking organizations may be subject to potential enforcement actions by the federal regulators for unsafe or unsound practices in conducting their businesses or for violations of any law, rule or regulation or any condition imposed in writing by the agency or any written agreement with the agency. Enforcement actions may include the imposition of a conservator or receiver, the issuance of a cease-and-desist order that can be judicially enforced, the termination of insurance of deposits (in the case of a depository institution), the imposition of civil money penalties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the issuance of removal and prohibition orders against institution-affiliated parties and the enforcement of such actions through injunctions or restraining orders based upon a judicial determination that the agency would be harmed if such equitable relief was not granted.

Premiums for Deposit Insurance

Through the Bank Insurance Fund, or BIF, the FDIC insures our customer deposits up to prescribed limits for each depositor. The amount of FDIC assessments paid by each BIF member institution is based on its relative risk of default as measured by regulatory capital ratios and other factors. Specifically, the assessment rate is based on the institution's capitalization risk category and supervisory subgroup category. An institution's capitalization risk category is based on the FDIC's determination of whether the institution is well capitalized, adequately capitalized or less than adequately capitalized. An institution's supervisory subgroup category is based on the FDIC's assessment of the financial condition of the institution and the probability that FDIC intervention or other corrective action will be required.

FDIC-insured depository institutions pay an assessment rate equal to the rate assessed on deposits insured by the Savings Association Insurance Fund.

The assessment rate currently ranges from zero to 27 cents per $100 of domestic deposits. The FDIC may increase or decrease the assessment rate schedule on a semi-annual basis. Due to continued growth in deposits and some recent bank failures, the BIF is nearing its minimum ratio of 1.25% of insured deposits as mandated by law. If the ratio drops below 1.25%, it is likely the FDIC will be required to assess premiums on all banks. Any increase in assessments or the assessment rate could have a material adverse effect on our business, financial condition, results of operations or cash flows, depending on the amount of the increase. Furthermore, the FDIC is authorized to raise insurance premiums under certain circumstances.

The FDIC is authorized to terminate a depository institution's deposit insurance upon a finding by the FDIC that the institution's financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices or has violated any applicable rule, regulation, order or condition enacted or imposed by the institution's regulatory agency. The termination of our deposit insurance would have a material adverse effect on our business, financial condition, results of operations or cash flows.

All FDIC-insured depository institutions must pay an annual assessment to provide funds for the payment of interest on bonds issued by the Financing Corporation, a federal corporation chartered under the authority of the Federal Housing Finance Board. The bonds, commonly referred to as FICO bonds, were issued to capitalize the Federal Savings and Loan Insurance Corporation. The FDIC established the FICO assessment rates effective for the fourth quarter of 2004 at approximately 1.54 cents for each $100 of assessable deposits. The FICO assessments are adjusted quarterly to reflect changes in the assessment bases of the FDIC's insurance funds and do not vary depending on a depository institution's capitalization or supervisory evaluations.

Federal Home Loan Bank System

We are a member of the Federal Home Loan Bank of San Francisco, or FHLB-SF. Among other benefits, each Federal Home Loan Bank, or FHLB, serves as a reserve or central bank for its members within its assigned region. Each FHLB is financed primarily from the sale of consolidated obligations of the FHLB system. Each FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the board of directors of the individual FHLB. As an FHLB member, we are required to own capital stock in an FHLB in an amount equal to the greater of:

- 1% of its aggregate outstanding principal amount of its residential mortgage loans, home purchase contracts and similar obligations at the beginning of each calendar year; or
- 5% of its FHLB advances or borrowings.

A new capital plan of the FHLB-SF was approved by the Federal Housing Finance Board and was implemented on April 1, 2004. The new capital plan incorporates a single class of stock with a par value of $100

per share, and may be issued, exchanged, redeemed and repurchased only at par value. Each member is required to own stock in an amount equal to the greater of:

- a membership stock requirement with an initial cap of $25 million (100% of "membership asset value" as defined); or
- an activity based stock requirement (based on percentage of outstanding advances).

The new capital stock is redeemable on five years' written notice, subject to certain conditions.

Federal Reserve System

The FRB requires all depository institutions to maintain noninterest bearing reserves at specified levels against their transaction accounts (primarily checking, NOW and Super NOW checking accounts) and non-personal time deposits. At December 31, 2004, we were in compliance with these requirements.

Impact of Monetary Policies

Our earnings and growth are subject to the influence of domestic and foreign economic conditions, including inflation, recession and unemployment. Our earnings are affected not only by general economic conditions but also by the monetary and fiscal policies of the United States and federal agencies, particularly the FRB. The FRB can and does implement national monetary policy, such as seeking to curb inflation and combat recession, by its open market operations in United States government securities and by its control of the discount rates applicable to borrowings by banks from the FRB. The actions of the FRB in these areas influence the growth of bank loans and leases, investments and deposits and affect the interest rates charged on loans and leases and paid on deposits. The FRB's policies have had a significant effect on the operating results of commercial banks and are expected to continue to do so in the future. The nature and timing of any future changes in monetary policies are not predictable.

Extensions of Credit to Insiders and Transactions with Affiliates

The Federal Reserve Act and FRB Regulation O, which is applicable to us, place limitations and conditions on loans or extensions of credit to:

- a bank's executive officers, directors and principal shareholders (*i.e.*, in most cases, those persons who own, control or have power to vote more than 10% of any class of voting securities);
- any company controlled by any such executive officer, director or shareholder; or
- any political or campaign committee controlled by such executive officer, director or principal shareholder.

Loans and leases extended to any of the above persons must comply with loan-to-one-borrower limits, require prior full board approval when aggregate extensions of credit to the person exceed specified amounts, must be made on substantially the same terms (including interest rates and collateral) as, and follow credit-underwriting procedures that are not less stringent than, those prevailing at the time for comparable transactions with non-insiders, and must not involve more than the normal risk of repayment or present other unfavorable features. In addition, Regulation O provides that the aggregate limit on extensions of credit to all insiders of a bank as a group cannot exceed the bank's unimpaired capital and unimpaired surplus. Regulation O also prohibits a bank from paying an overdraft on an account of an executive officer or director, except pursuant to a written pre-authorized interest-bearing extension of credit plan that specifies a method of repayment or a written pre-authorized transfer of funds from another account of the officer or director at the bank.

Consumer Protection Laws and Regulations

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

The CRA is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank's record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution's record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of "outstanding" to a low of "substantial noncompliance." In its last examination for CRA compliance, as of October 15, 2002, we were rated "Satisfactory."

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

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

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

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

Finally, the Real Estate Settlement Procedures Act, or RESPA, requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties. Due to heightened regulatory concern related to compliance with the CRA, TILA, FH Act, ECOA, HMDA and RESPA generally, we may incur additional compliance costs or be required to expend additional funds for investments in our local community.

Recent and Proposed Legislation

Our operations are subject to extensive regulation by federal, state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on

part or all of their respective operations. Because our business is highly regulated, the laws, rules and regulations applicable to us are subject to regular modification and change.

From time to time, legislation is enacted which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial institutions. Proposals to change the laws and regulations governing the operations and taxation of banks and other financial institutions are frequently made in Congress, in the California legislature and before various bank regulatory agencies.

Sarbanes-Oxley Act. On July 30, 2002, the President signed into law SOX, implementing legislative reforms intended to address corporate and accounting fraud. In general, SOX applies to publicly reporting companies, that is, companies (including banks) that have a class of securities registered under Section 12 of the Exchange Act. Upon commencement of the offering, we will become subject to the provisions of SOX, as well as the rules and regulations adopted by the SEC to implement SOX. In addition to the establishment of a new accounting oversight board which will enforce auditing, quality control and independence standards and will be funded by fees from all publicly traded companies, the bill restricts provision of both auditing and consulting services by accounting firms. To maintain auditor independence, any non-audit services being provided to an audit client will require pre-approval by our audit committee members. In addition, the audit partners must be rotated.

SOX also requires chief executive officers and chief financial officers, or their equivalent, to certify to the accuracy of periodic reports filed, subject to civil and criminal penalties if they knowingly or willfully violate this certification requirement. In addition, under SOX and implementing regulations of the SEC, legal counsel is required to report evidence of a material violation of the securities laws or a breach of fiduciary duty by a company to its chief executive officer or its chief legal officer, and, if such officer does not appropriately respond, to report such evidence to the audit committee or other similar committee of the board of directors or the board itself.

Longer prison terms and increased penalties will also be applied to corporate executives who violate federal securities laws, the period during which certain types of suits can be brought against a company or its officers has been extended and bonuses issued to top executives prior to restatement of a company's financial statements are now subject to disgorgement if such restatement was due to corporate misconduct. Executives are also prohibited from insider trading during retirement plan "blackout" periods, and loans to company executives are restricted. The Act accelerates the time frame specified for disclosures by public companies. Directors and executive officers must also provide information for most changes in ownership in a company's securities within two business days of the change.

SOX also prohibits any officer or director of a company or any other person acting under their direction from taking any action to fraudulently influence, coerce, manipulate or mislead any independent public or certified accountant engaged in the audit of our financial statements for the purpose of rendering the financial statements materially misleading. SOX and implementing regulations of the SEC require inclusion of an internal control report and assessment by management in the annual report to shareholders. In addition, SOX requires that each financial report required to be prepared in accordance with (or reconciled to) accounting principles generally accepted in the United States of America and filed with the SEC reflect all material correcting adjustments that are identified by the independent auditors in accordance with accounting principles generally accepted in the United States of America and the rules and regulations of the SEC.

Following the effective date of our registration statement under the Exchange Act, as directed by Section 302(a) of SOX, our chief executive officer and chief financial officer each will be required to provide certification relating to the contents of our annual and quarterly reports and our disclosure controls and procedures and our internal control over financial reporting.

USA PATRIOT Act. In the wake of the tragic events of September 11th, on October 26, 2001, the President signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and

Obstruct Terrorism Act of 2001, referred to as the USA PATRIOT Act. Under the USA PATRIOT Act, financial institutions are subject to prohibitions regarding specified financial transactions and account relationships as well as enhanced due diligence and "know your customer" standards in their dealings with foreign financial institutions and foreign customers. For example, the enhanced due diligence policies, procedures, and controls generally require financial institutions to take reasonable steps:

- To conduct enhanced scrutiny of account relationships to guard against money laundering and report any suspicious transaction;
- To ascertain the identity of the nominal and beneficial owners of, and the source of funds deposited into, each account as needed to guard against money laundering and report any suspicious transactions;
- To ascertain for any foreign bank, the shares of which are not publicly traded, the identity of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner; and
- To ascertain whether any foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related due diligence information.

Under the USA PATRIOT Act, financial institutions were given 180 days from enactment to establish anti-money laundering programs. The USA PATRIOT Act sets forth minimum standards for these programs, including:

- The development of internal policies, procedures, and controls;
- The designation of a compliance officer;
- An ongoing employee training program; and
- An independent audit function to test the programs.

On February 17, 2004, our board of directors adopted comprehensive policies and procedures to address the requirements of the USA PATRIOT Act.

Financial Services Modernization Legislation. On November 12, 1999 the Gramm-Leach-Bliley Act of 1999, also known as the Financial Services Modernization Act, was signed into law. The Financial Services Modernization Act is intended to modernize the banking industry by removing barriers to affiliation among banks, insurance companies, the securities industry and other financial service providers. It provides financial organizations with the flexibility of structuring such affiliations through a holding company structure or through a financial subsidiary of a bank, subject to certain limitations. The Financial Services Modernization Act establishes a new type of bank holding company known as a financial holding company that may engage in an expanded list of activities that are financial in nature, which include securities and insurance brokerage, securities underwriting, insurance underwriting and merchant banking.

The Financial Services Modernization Act also sets forth a system of functional regulation that makes the FRB the "umbrella supervisor" for holding companies, while providing for the supervision of the holding company's subsidiaries by other federal and state agencies. A bank holding company may not become a financial holding company if any of its subsidiary financial institutions are not well-capitalized or well-managed. Further, each bank subsidiary of the holding company must have received at least a satisfactory CRA rating. The Financial Services Modernization Act also expands the types of financial activities a national bank may conduct through a financial subsidiary, addresses state regulation of insurance, provides privacy protection for nonpublic customer information of financial institutions, modernizes the FHLB system and makes miscellaneous regulatory improvements. The FRB and the Secretary of the Treasury must coordinate their supervision regarding approval of new financial activities to be conducted through a financial holding company or through a financial subsidiary of a bank. While the provisions of the Financial Services Modernization Act regarding activities that may be conducted through a financial subsidiary directly apply only to national banks, those provisions indirectly apply to state-chartered banks.

In addition, we are subject to other provisions of the Financial Services Modernization Act, including those relating to CRA, privacy and safe-guarding confidential customer information, regardless of whether we elect to establish a holding company and become a financial holding company or to conduct activities through a financial subsidiary.

We do not believe that the Financial Services Modernization Act will have a material adverse effect on our operations in the near term. However, to the extent that it permits banks, securities firms and insurance companies to affiliate, the financial services industry will continue to experience further consolidation. The Financial Services Modernization Act is intended to grant to community banks certain powers as a matter of right that larger institutions have accumulated on an ad hoc basis. Nevertheless, this act may have the result of increasing the amount of competition that we face from larger institutions and other types of companies offering financial products, many of which may have substantially more financial resources than us.

Safety and Soundness Standards. The Federal Deposit Insurance Corporation Improvement Act, or FDICIA, imposes certain specific restrictions on transactions and requires federal banking regulators to adopt overall safety and soundness standards for depository institutions related to internal control, loan underwriting and documentation and asset growth. Among other things, FDICIA limits the interest rates paid on deposits by undercapitalized institutions, restricts the use of brokered deposits, limits the aggregate extensions of credit by a depository institution to an executive officer, director, principal shareholder or related interest and reduces deposit insurance coverage for deposits offered by undercapitalized institutions for deposits by certain employee benefits accounts. The federal banking agencies may require an institution to submit to an acceptable compliance plan as well as have the flexibility to pursue other more appropriate or effective courses of action given the specific circumstances and severity of an institution's noncompliance with one or more standards.

California Financial Information Privacy Act. The California Financial Information Privacy Act, or CFIPA, which was enacted in August 2003, imposes stricter limits on the use of consumers' nonpublic personal information by financial institutions beyond those imposed by the Financial Services Modernization Legislation. CFIPA applies to any financial institution doing business in California, but only with respect to the individual consumers of the institution that reside in California.

Under CFIPA, and subject to certain specified exceptions, a financial institution must now obtain a consumer's written consent before disclosing the consumer's nonpublic personal information to any nonaffiliated third party. Before releasing a consumer's nonpublic personal information to an affiliate, the financial institution must give the consumer the opportunity to direct that his or her information not be disclosed. This "opt-out" requirement also applies to information a financial institution discloses in connection with (1) certain joint marketing agreements with other financial institutions and (2) agreements with "affinity partners" in whose name the financial institution issues credit cards or other financial products. A financial institution that meets certain conditions may, however, share nonpublic personal information with its wholly owned financial institution subsidiaries or sister companies engaged in the same line of business.

CFIPA provides a statutory form of "opt-out" notice that a financial institution may use to offer consumers the opportunity to communicate their privacy preferences. A financial institution may satisfy CFIPA's notice requirements by sending out this form annually. Alternatively, a financial institution may use its own form, subject to specific requirements and limitations.

Since these provisions are more restrictive than the privacy provisions of the Financial Services Modernization Act, CFIPA would require us to adopt new policies, procedures and disclosure documentation. The cost of complying with this legislation is not predictable at this time.

Fair and Accurate Transactions Act. In December 2003, the U.S. Congress adopted, and the President signed, the Fair and Accurate Transactions Act, referred to as the FACT Act. One of the provisions of the FACT Act provides that, when the implementing regulations have been issued and become effective, the FACT Act will preempt elements of the California Financial Information Privacy Act. The FACT Act requires the FRB and the

Federal Trade Commission to issue final regulations within nine months of the effectiveness of the FACT Act, and that those regulations must become effective within six months of issuance. The provisions of the regulations that will implement the FACT Act, and the timing of their effect on us, cannot be determined at this time.

Other. Various other legislation, including proposals to overhaul the bank regulatory system and to limit the investments that a depository institution may make with insured funds, is introduced into Congress or the California Legislature from time to time. We cannot determine the ultimate effect that any potential legislation, if enacted, or regulations promulgated thereunder, would have upon our business, financial condition, results of operations or cash flows.

Employees

As of December 31, 2004, the Bank had a total of 111 full-time employees and three part-time employees. None of the employees are represented by a union or collective bargaining group. The management of the Bank believes that their employee relations are satisfactory.

Available Information

We are subject to the reporting and other requirements of the Securities Exchange Act of 1934, as amended. In accordance with Sections 12, 13 and 14 of the Exchange Act and as a bank that is not a member of the Federal Reserve System, we file certain reports, proxy materials, information statements and other information with the FDIC, copies of which can be inspected and copied at the public reference facilities maintained by the FDIC, at the Public Reference Section, Room F-6043, 550 17th Street, N.W., Washington, DC 20429. Requests for copies may be made by telephone at (202) 898-8913 or by fax at (202) 898-3909.

Risk Factors That May Affect Future Results

In addition to other information contained in this report, the following discusses certain factors which may affect our financial results and operations and should be considered in evaluating us:

Changes in economic conditions, and in particular a prolonged economic slowdown in the State of California, could hurt our business materially.

Our business is directly affected by factors such as economic, political and market conditions, broad trends in industry and finance, legislative and regulatory changes, changes in governmental monetary and fiscal policies and inflation, all of which are beyond our control. We are particularly susceptible to conditions and changes affecting the State of California and Southern California in view of the concentration of our operations and the collateral securing our loan portfolio in Southern California. In 2003, the negative effects of weak national and international economic recoveries, the threat of terrorism and the uncertainty associated with the impact of the war in Iraq on California’s economy were exacerbated by the state’s budget crisis and the recent hike in energy prices, the recall of its governor and wildfires in Southern California. Deterioration in economic conditions, in California and Southern California in particular, could result in the following consequences, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flows:

- problem assets and foreclosures may increase;
- loan delinquencies may increase;
- demand for loans and our other products and services may decline;
- deposits may decrease or become more expensive; and
- collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers’ borrowing power or capacity to repay, and reducing the value of assets and collateral associated with our existing loans.

In addition, because we make loans to small to medium-sized businesses, many of our customers may be particularly susceptible to economic slowdowns or recessions and may be unable to make scheduled principal or interest payments during these periods.

Most of our loans are secured by real estate, and a downturn in the California real estate market could have a material adverse effect on our business, financial condition, results of operations and cash flows.

A downturn in the California real estate market could hurt our business because most of our loans are secured by real estate located in California. As of December 31, 2004, approximately 73% of our loan portfolio consisted of loans collateralized by various types of California real estate. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other laws, regulations and policies and acts of nature. In addition, real estate values in California could be affected by, among other things, earthquakes and national disasters particular to the state. If real estate prices decline, the value of real estate collateral securing our loans will be reduced. As a result, we may experience greater charge-offs and, similarly, our ability to recover on defaulted loans by foreclosing and selling the real estate collateral would then be diminished and we would be more likely to suffer losses on defaulted loans.

We rely heavily on our senior management team and other employees, the loss of whom could significantly harm our business.

Our success depends heavily on the abilities and continued service of our executive officers, especially Li Yu, our founder, Chairman, President and Chief Executive Officer, and Walter Duchanin, our Executive Vice President. These two individuals, who have worked together since our founding, are integral to implementing our business plan. We currently do not have employment agreements or non-competition agreements with Messrs. Yu or Duchanin. If we lose the services of any of our executive officers, especially Mr. Yu or Mr. Duchanin, our business, financial condition, results of operations and cash flows may be adversely affected. Furthermore, attracting suitable replacements may be difficult and may require significant management time and resources.

We also rely to a significant degree on the abilities and continued service of our private banking, loan origination, underwriting, administrative, marketing and technical personnel. Competition for qualified employees in the banking industry is intense and there are a limited number of qualified persons with knowledge of, and experience in, the California community banking industry. The process of recruiting personnel with the combination of skills and attributes required to carry out our strategies is often lengthy. If we fail to attract and retain the necessary deposit generation, loan origination, underwriting, administrative, marketing and technical personnel, our business, financial condition, results of operations and cash flows may be materially adversely affected.

A natural disaster or recurring energy shortage, especially in California, could harm our business.

Historically, Southern California has been vulnerable to natural disasters. Therefore, we are susceptible to the risks of natural disasters, such as earthquakes, wildfires, floods and mudslides. Natural disasters could harm our operations directly through interference with communications, as well as through the destruction of facilities and our operational, financial and management information systems. Uninsured or underinsured disasters may reduce a borrower’s ability to repay mortgage loans. Disasters may also reduce the value of the real estate securing our loans, impairing our ability to recover on defaulted loans. Southern California has also experienced energy shortages which, if they recur, could impair the value of the real estate in those areas affected. The occurrence of natural disasters or energy shortages in Southern California could have a material adverse effect on our business, financial condition, results of operations and cash flows.

Our business is subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

Market interest rates are affected by many factors that are beyond our control and are hard to predict, including inflation, recession, performance of the stock markets, a rise in unemployment, tightening money supply, exchange rates, monetary and other policies of various governmental and regulatory agencies, domestic and international disorder and instability in domestic and foreign financial markets.

Changes in the interest rate environment may reduce our profits. Changes in interest rates will influence not only the interest we receive on our loans and investment securities and the amount of interest we pay on deposits, it will also affect our ability to originate loans and obtain deposits and our costs in doing so.

We expect that we will continue to realize a substantial portion of our income from the differential or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Because interest rates are based on the maturity, repricing and other characteristics of an instrument, conditions that trigger changes in interest rates do not produce equivalent changes in interest income earned on our interest-earning assets and interest expense paid on our interest-bearing liabilities. Accordingly, fluctuations in interest rates could adversely affect our interest rate spread and, in turn, our profitability.

In addition, an increase in the general level of interest rates may adversely affect the ability of some borrowers to pay the interest on and principal of their obligations, which could reduce our cash flows and harm our asset quality.

We face strong competition from financial services companies and other companies that offer banking services, and our failure to compete effectively with these companies could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We conduct our operations primarily in California. Increased competition within California may result in reduced loan originations and deposits. Ultimately, we may not be able to compete successfully against current and future competitors. Many competitors offer the types of loans and banking services that we offer. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including finance companies, brokerage firms, insurance companies, mortgage banks and other financial intermediaries. In particular, our competitors include financial institutions whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous banking locations and mount extensive promotional and advertising campaigns. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions may have larger lending limits which would allow them to serve the credit needs of larger customers. These institutions, particularly to the extent they are more diversified than we are, may be able to offer the same loan products and services we offer at more competitive rates and prices.

We also compete with three publicly listed Chinese-American banks, and subsidiary banks and branches of foreign banks, many of which have greater lending limits, and a wider variety of products and services than us. We also compete with smaller Chinese community banks for both deposits and loans.

We also face competition from out-of-state financial intermediaries that have opened loan production offices or that solicit deposits in our market areas. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits, and our business, financial condition, results of operations and cash flows may be materially adversely affected.

If our underwriting practices are not effective, we may suffer losses in our loan portfolio and our results of operations may be harmed.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Depending on the type of loan, these practices include analysis of a borrower's prior credit history, financial

statements, tax returns and cash flow projections, valuation of collateral based on reports of independent appraisers and verification of liquid assets. Although we believe that our underwriting criteria are appropriate for the types of loans we make, we cannot assure you that they will be effective in mitigating all risks. If our underwriting criteria prove to be ineffective, we may incur losses in our loan portfolio, and these losses may exceed the amounts set aside as reserves in our allowance for loan losses.

If our allowance for loan and lease losses is inadequate to cover actual losses, our financial results would be harmed.

A significant source of risk arises from the possibility that losses could be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans and leases. The underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent unexpected losses that could have a material adverse effect on our business, financial condition, results of operations and cash flows. Unexpected losses may arise for a wide variety of reasons, many of which are beyond our ability to predict, influence or control. Some of these reasons could include a prolonged economic downturn in the State of California, a decline in the California real estate market, changes in the interest rate environment, adverse economic conditions in Asia and natural disasters.

Like all financial institutions, we maintain an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. Our allowance for loan and lease losses may not be adequate to cover actual loan and lease losses, and future provisions for loan and lease losses could materially and adversely affect our business, financial condition, results of operations and cash flows. Our allowance for loan and lease losses reflects our best estimate of the losses inherent in the existing loan and lease portfolio at the relevant balance sheet date and is based on management's evaluation of the collectibility of the loan and lease portfolio, which evaluation is based on historical loss experience and other significant factors. The determination of an appropriate level of loan and lease loss allowance is an inherently difficult process and is based on numerous assumptions. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, that may be beyond our control and these losses may exceed current estimates. While we believe that our allowance for loan and lease losses is adequate to cover current losses, we cannot assure you that we will not increase the allowance for loan and lease losses further or that regulators will not require us to increase this allowance. Either of these occurrences could materially adversely affect our business, financial condition, results of operations and cash flows.

If the risks inherent in construction lending are realized, our net income could be adversely affected.

At December 31, 2004, our construction loans were $112.0 million, or 18% of our total loans and leases held, and the average loan size of our construction loans was $1.8 million. The risks inherent in construction lending include the possibility that contractors may fail to complete, or fail to complete on a timely basis, construction of the relevant properties; substantial cost overruns in excess of original estimates and financing; market deterioration during construction; and a lack of permanent take-out financing. Loans secured by these properties also involve additional risk because the properties have no operating histories. In these loans, funds are advanced upon the security of the project under construction, which is of uncertain value prior to completion of construction, and the estimated operating cash flow to be generated by the completed project. The borrowers' ability to repay their obligations to us and the value of our security interest in the collateral will be materially adversely affected if the projects do not generate sufficient cash flow by being either sold or leased.

If the appraised value of our real property collateral is greater than the proceeds we realize from a sale or foreclosure of the property, we may suffer a loss on our investment.

In considering whether to make a loan on or secured by real property, we generally will require an appraisal. However, an appraisal is only an estimate of the value of the property at the time the appraisal is made. If the appraisal does not reflect the amount that may be obtained upon any sale or foreclosure of the property, we may not realize an amount equal to the indebtedness secured by the property and we may suffer a loss on our investment.

Adverse economic conditions in Asia could impact our business adversely.

We estimate that at December 31, 2004, approximately 68% of our non-governmental deposits and 31% of our loans were with customers from the Chinese-American market. We believe these customers maintain significant ties to many Asian countries and, therefore, could be affected by economic and other conditions in those countries. We cannot predict the behavior of the Asian economies. U.S. economic policies, the economic policies of countries in Asia, domestic unrest and/or military tensions, crises in leadership succession, currency devaluations, cases of Severe Acute Respiratory Syndrome, or SARS, and an unfavorable global economic condition may among other things adversely impact the Asian economies. We generally do not loan to customers or take collateral located outside of Southern California. However, if Asian economic conditions should deteriorate, we could experience an outflow of deposits by our Chinese-American customers. In addition, adverse economic conditions could prevent or delay these customers from meeting their obligations to us. This may adversely impact the recoverability of investments with or loans made to these customers. Adverse economic conditions may also negatively impact asset values and the profitability and liquidity of companies operating in Asia.

We do not believe that the recent Tsunami disaster in Southeast Asia will adversely impact our business or financial condition because our customers do not have significant ties to the particular areas affected by the disaster.

A downturn in international trade could impact our business adversely.

At December 31, 2004, approximately $46.0 million, or 7%, of our loan portfolio consisted of loans made to finance international trade activities. Changes in monetary policy, including changes in interest rates, governmental regulation of international trade activities, currency valuation, price competition, competition from other financial institutions and general economic and political conditions could negatively impact the amount of goods imported to and exported from the United States, the ability of borrowers to repay loans made by us, and the number and extent of importers' and exporters' need for our trade finance activities. It is possible that if the U.S. dollar continues to weaken against other foreign currencies, as it has during 2004, the cost of imported goods will increase, which could have an adverse impact on some of our customers who import goods for resale in the United States. Such factors could have a material adverse effect on our business, financial condition, results of operations and cash flows.

If we cannot attract deposits, our growth may be inhibited.

We plan to increase significantly the level of our assets, including our loan portfolio. Our ability to increase our assets depends in large part on our ability to attract additional deposits at competitive rates. We intend to seek additional deposits by continuing to establish and strengthening our personal relationships with our customers and by offering deposit products that are competitive with those offered by other financial institutions in our markets. We cannot assure you that these efforts will be successful. Our inability to attract additional deposits at competitive rates could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We rely primarily on large certificates of deposits to fund our operations, and the potential volatility of such deposits and the unavailability of any such funds in the future could adversely impact our growth strategy and prospects.

We primarily rely on deposits, in particular certificates of deposit of $100,000 or more, or Jumbo CDs, to fund our operations. At December 31, 2004, we held $368.7 million of Jumbo CDs, representing 46% of total deposits. These deposits are considered volatile and could be subject to withdrawal. Withdrawal of a material amount of such deposits would adversely impact our liquidity, profitability, business, financial condition, results of operations and cash flows.

Our inability to raise additional capital when needed or on favorable terms could inhibit our growth and could harm our operations.

To the extent that our deposits and total assets continue to grow, we may need to increase our capital in order to maintain our compliance with regulatory capital requirements. We may also need additional capital to fund growth in our loan portfolio or in the event we are unable to attract sufficient deposits in order to fund our growth. We cannot predict the timing and amount of our future capital requirements. If our capital needs exceed our earnings, we may seek funding through the capital markets; however, we may not be able to obtain capital when we need to or when it would be advantageous for us to do so. Failure to raise capital when needed could limit or eliminate our ability to grow, or in extreme instances, materially adversely affect our operations. Moreover, even if capital is available, it may be upon terms that are not favorable to existing common shareholders and could dilute their interest.

Our inability to manage our growth could harm our business.

We anticipate that our asset size and deposit base will continue to grow over time, perhaps significantly. To manage the expected growth of our operations and personnel, we will be required to, among other things:

- improve existing and implement new transaction processing, operational and financial systems, procedures and controls;
- maintain effective underwriting guidelines; and
- expand our employee base and train and manage this growing employee base.

If we are unable to manage growth effectively, our business, financial condition, results of operations and cash flows could be materially adversely affected.

We rely on communications, information, operating and financial control systems technology from third-party service providers, and we may suffer an interruption in or break of those systems that may result in lost business and we may not be able to obtain substitute providers on terms that are as favorable if our relationships with our existing service providers are interrupted.

We rely heavily on third-party service providers for much of our communications, information, operating and financial control systems technology, including customer relationship management, general ledger, deposit, servicing and loan origination systems. Any failure or interruption or breach in security of these systems could result in failures or interruptions in our customer relationship management, general ledger, deposit, servicing and/or loan origination systems. We cannot assure you that such failures or interruptions will not occur or, if they do occur, that they will be adequately addressed by us or the third parties on which we rely. The occurrence of any failures or interruptions could have a material adverse effect on our business, financial condition, results of operations and cash flows. If any of our third-party service providers experience financial, operational or technological difficulties, or if there is any other disruption in our relationships with them, we may be required to locate alternative sources of such services, and we cannot assure you that we could negotiate terms that are as favorable to us, or could obtain services with similar functionality as found in our existing systems without the need to expend substantial resources, if at all. Any of these circumstances could have a material adverse effect on our business, financial condition, results of operations and cash flows.

The U.S. government's monetary policies or changes in those policies could have a major effect on our operating results, and we cannot predict what those policies will be or any changes in such policies or the effect of such policies on us.

Our earnings will be affected by domestic economic conditions and the monetary and fiscal policies of the U.S. government and its agencies. The monetary policies of the Federal Reserve Bank, or the FRB, have had, and

will continue to have, an important effect on the operating results of commercial banks and other financial institutions through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession.

The monetary policies of the FRB, effected principally through open market operations and regulation of the discount rate and reserve requirements, have had major effects upon the levels of bank loans, investments and deposits. For example, in 2001, several drops in the discount rate by the Federal Open Market Committee placed tremendous pressure on the profitability of all financial institutions because of the resulting contraction of net interest margins. It is not possible to predict the nature or effect of future changes in monetary and fiscal policies.

We are subject to extensive government regulation, and these regulations may hamper our ability to increase assets and earnings and could result in a decrease in the value of your shares.

Our operations are subject to extensive regulation by federal, state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Because our business is highly regulated, the laws, rules and regulations applicable to us are subject to regular modification and change, which may have the effect of increasing or decreasing the cost of doing business, modifying permissible activities or enhancing the competitive position of other financial institutions. These laws are primarily intended for the protection of consumers, depositors and the deposit insurance funds and not for the protection of shareholders of bank holding companies or banks. There are currently proposed various laws, rules and regulations that, if adopted, would impact our operations. We cannot assure you that these proposed laws, rules and regulations or any other laws, rules or regulations will not be adopted in the future, which could make compliance much more difficult or expensive, restrict our ability to originate, further limit or restrict the amount of commissions, interest or other charges earned on loans originated by us or otherwise adversely affect our business, financial condition, results of operations or cash flows.

We are exposed to risk of environmental liability with respect to properties to which we take title.

In the course of our business, we may foreclose on and take title to properties securing our loans. If hazardous substances were discovered on any of the properties, we may be held liable to governmental entities or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination or may be required to investigate or clean up hazardous or toxic substances or chemical releases at a property. Many environmental laws can impose liability regardless of whether we knew of or were responsible for the contamination. In addition, if we arrange for the disposal of hazardous or toxic substances at another site, we may be liable for the costs of cleaning up and removing those substances from the site, even if we neither own nor operate the disposal site. Environmental laws may require us to incur substantial expenses and may materially limit use of properties we acquire through foreclosure, reduce their value or limit our ability to sell them in the event of a default on the loans they secure. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability.

The threat of terrorism has depressed the economy generally and could worsen, particularly if there are further terrorist events.

The terrorist attacks and international conflicts of recent years have resulted in continued uncertainty regarding the economic outlook of the United States. The possibility of further terrorist attacks, as well as continued terrorist threats, may prolong the depth and length of this economic uncertainty. Future terrorist acts and responses to such activities could adversely affect us in a number of ways, including an increase in delinquencies, bankruptcies or defaults that could result in a higher level of non-performing assets, net charge-offs and provision for loan losses.

Executive Officers of the Bank

The following table sets forth our executive officers, their positions and their ages. Each officer is appointed by our Board of Directors and serves at their pleasure.

Name	Age (1)	Position with Bank
Li Yu	64	Chairman of the Board, President and Chief Executive Officer
Walt Duchanin	51	Executive Vice President and Chief Credit Officer
Chris Chan	43	Senior Vice President and Chief Financial Officer

(1) As of March 28, 2005

Li Yu has been our President and Chief Executive Officer since 1993. From December 1991 to the present, he has served as Chairman of our Board of Directors. From 1987 to 1991, he was involved in several privately held companies of which he was the owner. From 1982 to 1987, he served as Chairman of the Board of California Pacific National Bank, which became a part of Bank of America. Mr. Yu received a Masters of Business Administration, or MBA, from the University of California, Los Angeles. He was also the past President of the National Association of Chinese American Bankers, and is currently a member of the Board of Visitors of UCLA's Anderson Graduate School of Management.

Chris Chan has been our Senior Vice President and Chief Financial Officer since 1997. From 1996 until 1997, he was the Senior Vice President and Chief Financial Officer of First Professional Bank, and from 1989 until 1996, he was Vice President/Finance of First Public Savings Bank. Mr. Chan received a MBA from Pepperdine University and a Bachelors of Science degree in finance from the University of Southern California, or USC.

Walter Duchanin has been our Executive Vice President and Chief Credit Officer since 1995 and our Senior Vice President and Senior Loan Officer from 1992 to 1995. From 1988 to 1992, he was the Senior Vice President and Credit Administrator of Simi Valley Bank, and from 1983 to 1988, he was Group Vice President of Marathon National Bank. Mr. Duchanin's banking experience also includes American International Bank and Bank of America. Mr. Duchanin received a Bachelors of Science degree in finance from USC.

ITEM 2. PROPERTIES

Our corporate headquarters are located at 601 S. Figueroa Street, 20th Floor, Los Angeles, California 90017. The lease for this floor extends until August 31, 2008, with one option for us to extend the term of the lease for five years. We paid $313,000 in lease expenses for 2004 related to this lease.

At December 31, 2004, we maintained eight full-service branch offices in Alhambra, Century City, City of Industry, Torrance, Arcadia, Irvine, Diamond Bar and Valencia, California. We believe that no single lease is material to our operations.

We believe that our present facilities are adequate for our current needs, and that alternative or additional space, if necessary, will be available at market terms to facilitate, among other things, our growth in branches and/or loan production offices. For the year ended December 31, 2003, we paid $976,000 in lease payments. For the year ended December 31, 2004, we paid $1,036,000 in lease payments.

We believe that our existing facilities are adequate for our present purposes. We believe that, if necessary, we could secure alternative facilities on similar terms without adversely affecting our operations.

The following table provides certain information with respect to our leased branch locations.

Location	Address	Current Lease Term Expiration Date	Square Footage	Total Deposits at December 31, 2004
				(In thousands)
Los Angeles County				
Alhambra	325 E. Valley Blvd.	03/31/09	6,000	$158,188
Arcadia	1469 S. Baldwin Avenue	04/30/09	2,600	55,684
Century City	1801 Century Park East, Suite 100	06/09/06	4,416	55,170
City of Industry	17515-A Colima Road	03/31/15	5,610	77,427
Diamond Bar	1373 S. Diamond Bar Blvd.	11/30/09	3,440	46,002
Los Angeles (Head Office & branch)	601 S. Figueroa Street, 20th Floor	08/31/08	15,64	237,146
Santa Monica	524 Wilshire Blvd.	07/31/12	1,355	— (1)
Torrance	3501 Sepulveda Blvd., Suite 107	10/25/06	4,800	135,582
Valencia	24501 Town Center Drive	10/22/11	2,926	7,802
Orange County				
Irvine	2301 Dupont Drive, Suite 150	05/31/06	3,584	28,534

(1) On March 15, 2005, we signed a lease for our new full-service branch office in Santa Monica, California. We anticipate opening this branch in July 2005.

ITEM 3. LEGAL PROCEEDINGS

From time to time we are a party to claims and legal proceedings arising in the ordinary course of business. There are no pending legal proceedings or, to the best of our knowledge, threatened legal proceedings, to which we are a party which may have a material adverse effect upon our financial condition, results of operations and business prospects.

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

There was no submission of matters to a vote of security holders during the fourth quarter of the year ended December 31, 2004.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Market Information

Our Common Stock commenced trading on the Nasdaq National Market on February 15, 2005 under the symbol "PFBC." Prior to being listed on the Nasdaq National Market, our common stock was listed for trading on the OTC Bulletin Board under the symbol "PFBL." While listed for trading on the OTC Bulletin Board, there was limited trading at widely varying prices and on a number of days during, there were no trades at all in our common stock.

The initial public offering price of our common stock on February 14, 2004 was $38.00 per share. Our common stock closed at $38.23 on March 28, 2005 and there were 150 holders of record of the 6,637,404 outstanding shares of our common stock.

The following table sets forth the high and low sales prices for our common stock for the periods indicated as reported by the OTC Bulletin Board, as well as the number of shares sold in each period:

	High	Low	Number of Shares Sold
2002			
First Quarter	$14.25	$13.50	5,200
Second Quarter	N/A	N/A	0
Third Quarter	$16.00	$14.25	15,000
Fourth Quarter	$15.10	$14.75	1,600
2003			
First Quarter	$17.00	$14.75	1,100
Second Quarter	$17.00	$17.00	6,800
Third Quarter	$18.00	$18.00	1,000
Fourth Quarter	N/A	N/A	0
2004			
First Quarter	$22.00	$17.80	22,400
Second Quarter	N/A	N/A	0
Third Quarter	N/A	N/A	0
Fourth Quarter	N/A	N/A	0

The foregoing reflects information available to us and does not necessarily include all trades in our common stock during the periods indicated.

Dividends

The following table sets forth during the periods indicated the dividends declared per share of our common stock.

Calendar Year Ending December 31,	Dividends Declared Per Share
2004	$0.60
2003	$0.24
2002	$0.38
2001	$0.38
2000	$0.30
1999	$0.30
1998	$0.25
1997	$0.25

On February 7, 2005, we paid a dividend of $0.15 per share to shareholders of record on January 31, 2005.

We began paying dividends on a quarterly basis in the first quarter of 2005, subject to regulatory, capital and contractual constraints. Any determination to pay dividends in the future will, however, be at the discretion of our board of directors and will depend upon our earnings, financial condition, results of operations, capital requirements, available investment opportunities, regulatory restrictions, contractual restrictions and other factors that our board of directors may deem relevant. Accordingly, there can be no assurance that any stock or cash dividends will be declared in the future, and if any are declared, what amount they will be.

Because we are a California state-chartered bank, our ability to pay dividends or make distributions to shareholders is subject to restrictions set forth in the California Financial Code. California Financial Code Section 642 restricts the amount available for cash dividends by state-chartered banks to the lesser of: (1) retained earnings; or (2) the bank's net income for its last three fiscal years (less any distributions to shareholders made during such period).

However, Section 643 of the California Financial Code provides that notwithstanding the provisions of Section 642, a state-chartered bank may, with the prior approval of the California Commissioner, make a distribution to its shareholders in an amount not exceeding the greater of:

- retained earnings;
- net income for a bank's last preceding fiscal year; or
- net income of the bank for its current fiscal year.

If the California Commissioner finds that the shareholders' equity of the bank is not adequate or that the payment of a dividend would be unsafe or unsound for the bank, the California Commissioner may order the bank not to pay a dividend to the bank's shareholders.

As of December 31, 2004, we could have paid $17.9 million in dividends without the approval of the California Commissioner.

In addition, under California law, the California Commissioner has the authority to prohibit a bank from engaging in business practices which the California Commissioner considers to be unsafe or injurious to its business or financial condition. It is possible, depending on our financial condition and other factors, that the California Commissioner could assert that the payment of dividends or other payments to our shareholders might under some circumstances be unsafe or injurious to our business or financial condition and prohibit such payment.

The FDIC also has the authority to prohibit a bank from engaging in business practices which the FDIC considers to be unsafe or unsound. It is possible, depending upon our financial condition and other factors, that the FDIC could assert that the payment of dividends or other payments might under some circumstances be such an unsafe or unsound practice and prohibit such payment.

ITEM 6. SELECTED FINANCIAL DATA

The following table shows our selected historical financial data for the periods indicated. You should read our selected historical financial data, together with the notes thereto, in conjunction with the more detailed information in our financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Form 10-K.

Our financial condition data as of December 31, 2004 and 2003 and our statement of income data for the years ended December 31, 2004, 2003 and 2002 have been derived from our audited historical financial statements included elsewhere in this Form 10-K.

The statement of income data for the years ended December 31, 2001 and 2000 and the financial condition data as of December 31, 2002, 2001 and 2000 have been derived from our audited financial statements that are not included in this Form 10-K.

	At or for the Year Ended December 31,				
	2004	2003	2002	2001	2000
	(Dollars in thousands, except per share data)				
Financial Condition Data:					
Total assets	$907,270	$761,825	$706,052	$658,273	$589,059
Total deposits	801,535	662,812	614,868	576,325	501,343
Investments securities available-for sale, at fair value sale, at fair value	164,635	155,869	97,961	114,237	141,927
Loans and leases	615,961	504,053	448,512	374,160	324,611
Cash due from banks	35,212	22,960	24,351	17,568	30,992
Other real estate owned[1]	8,258	8,258	8,188	795	—
Shareholders' equity	76,808	67,736	59,918	57,122	50,891
Statement of Income Data:					
Interest income	$ 38,643	$ 34,376	$ 33,902	$ 40,032	$ 46,176
Interest expense	7,447	8,696	10,718	19,184	22,216
Net interest income	31,196	25,680	23,184	20,848	23,960
Provision for loan and lease losses	1,550	2,100	10,146	900	1,330
Net interest income after provision for loan and lease losses	29,646	23,580	13,038	19,948	22,630
Noninterest income	4,199	4,923	4,514	5,664	2,494
Noninterest expense	15,339	13,774	10,261	12,379	11,094
Income before provision for income taxes	18,506	14,729	7,291	13,233	14,030
Provision for income taxes	7,354	5,696	2,888	5,205	5,803
Net income	$ 11,152	$ 9,033	$ 4,403	$ 8,028	$ 8,227

	At or for the Year Ended December 31,				
	2004	2003	2002	2001	2000
	(Dollars in thousands, except per share data)				
Share Data:					
Net income per share, basic[2]	$ 2.02	$ 1.66	$ 0.82	$ 1.52	$ 1.56
Net income per share, diluted[2]	$ 1.92	$ 1.58	$ 0.77	$ 1.43	$ 1.46
Book value per share[3]	$ 13.83	$ 12.42	$ 11.06	$ 10.66	$ 9.82
Shares outstanding at period end	5,554,182	5,454,982	5,415,282	5,358,782	5,180,280
Weighted average number of shares outstanding, basic[2]	5,518,398	5,440,319	5,398,114	5,272,605	5,265,087
Weighted average number of shares outstanding, diluted[2]	5,809,234	5,715,542	5,724,186	5,622,402	5,620,662
Selected Other Balance Sheet Data[4]:					
Average assets	$ 840,265	$ 752,097	$ 679,185	$ 623,549	$ 565,160
Average earning assets	791,227	707,588	636,053	588,162	535,160
Average shareholders' equity	71,896	63,704	60,285	54,436	47,518
Selected Financial Ratios[4]:					
Return on average assets	1.33%	1.20%	0.65%	1.29%	1.46%
Return on average shareholders equity	15.51%	14.18%	7.30%	14.75%	17.31%
Shareholders' equity to assets[5]	8.47%	8.89%	8.49%	8.68%	8.64%
Net interest margin[6]	3.94%	3.63%	3.65%	3.54%	4.48%
Efficiency ratio[7]	43.34%	45.01%	37.05%	46.69%	41.94%
Selected Asset Quality Ratios:					
Non-performing loans to total loans and leases[8]	0.06%	0.20%	1.43%	1.61%	1.36%
Non-performing assets to total assets[9]	0.95%	1.22%	2.05%	1.04%	0.75%
Allowance for loan and leases losses to total loans and leases	1.09%	1.22%	2.06%	1.31%	1.35%
Allowance for loan and leases losses to non-performing loans	1758.64%	616.80%	144.23%	81.32%	99.16%
Net charge-offs to average loans and leases	0.18%	1.11%	1.38%	0.11%	0.07%

n.m. Not meaningful.

(1) These amounts include all property held by us as a result of foreclosure.

(2) Net income per share, basic is based on the weighted average shares of common stock outstanding during the period. Net income per share, diluted is based on the weighted average shares of common stock plus common stock equivalents determined using the treasury stock method.

(3) Book value per share represents our shareholders' equity divided by the number of shares of common stock issued and outstanding at the end of the period indicated (exclusive of shares exercisable under our stock option plans). Book value per share reflects the impact of a $0.60 per share cash dividend declared on April 21, 2004, which was paid on May 1, 2004 to shareholders of record on April 30, 2004.

(4) Average balances used in this chart and throughout this offering circular are based on daily averages. Percentages as used throughout this offering circular have been rounded to the closest whole number, tenth or hundredth as the case may be.

(5) For a discussion of the components of the capital ratios, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Capital Resources."

(6) Net interest margin is net interest income expressed as a percentage of average total interest-earning assets.

(7) The efficiency ratio is the ratio of noninterest expense divided by the sum of net interest income before the provision for loan and lease losses plus noninterest income.

(8) Non-performing loans consist of loans on nonaccrual and loans past due 90 days or more and restructured debt.

(9) Non-performing assets consist of non-performing loans, restructured debt and other real estate owned. Since 2002, we have had two significant non-performing assets consisting of a leveraged lease to United Airlines which has now been charged off and a single office building property located in San Francisco with a carrying value of $8.3 million. This property currently generates operating income, is appraised for more than its carrying value and has been sold as of March 15, 2005. For more details, see subheadings "Overview," "Results of Operations—The UAL Leveraged Lease" and "Financial Condition—Non-Performing Assets" under "Management's Discussion and Analysis of Financial Condition and Results of Operations."

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of Preferred Bank (the "Bank"). This information is intended to facilitate the understanding and assessment of significant changes and trends related to our financial condition and the results of our operations. This discussion and analysis should be read in conjunction with the Bank's consolidated financial statements and the accompanying notes presented elsewhere herein.

Overview

We are a California chartered, full-service commercial bank focused on the Chinese-American market. We conduct our banking business from our headquarters in Los Angeles, and through our eight full-service branch banking offices located in Alhambra, Century City, City of Industry, Torrance, Arcadia, Irvine, Diamond Bar, and Valencia, California.

We derive our income primarily from interest received on our loan and investment securities portfolios, and fee income we receive in connection with servicing our loan and deposit customers. Our major operating expenses are the interest we pay on deposits and borrowings, and the salaries and related benefits we pay our management and staff. We rely primarily on locally-generated deposits, most of which we receive from the Chinese-American market within Southern California, to fund our loan and investment activities.

One of our strategic goals is to focus on improving profitability while achieving reasonable but controlled asset growth. To attain this goal, we plan to continue to expand our branch network in Southern California. In December 2002, we established a branch office in Diamond Bar and in January 2004, we opened our Valencia branch to further expand our franchise. On March 10, 2005, we signed a lease for our new branch office in Santa Monica, California. We currently anticipate opening our Santa Monica Branch in July 2005. In addition, we currently anticipate opening in 2005 another branch office in Southern California, but we have no commitments, understandings or agreements concerning such branch office.

During the three-year period ended December 31, 2004, our assets, loans and deposits grew by 37.83%, 64.63% and 39.08%, respectively. We market and make loans throughout the Southern California market without regard to the ethnicity of our customers. Most of our loan growth is attributable to increases in the volume of our real estate loan portfolio, especially in mini-perm real estate loans secured by retail, office and 1-4 residential income producing properties. We believe that most of our deposit growth is the result of our successful marketing efforts with high net-worth individuals, primarily within the Chinese-American market we serve through our branch network.

For the three-year period ended December 31, 2004, our net interest income grew by 49.64%. However, our net income grew by only 38.91% during this period. The reason for the lower rate of growth in our net income as compared to our net interest income is partially attributable to the additional provisions in the amount of $9.3 million to our allowance for loan and lease losses due to an investment in a leveraged aircraft lease with United Airlines we originally made in November 1997, or the UAL Leveraged Lease. During 2002, United Airlines declared bankruptcy. As a result, in 2002 we made a $8.6 million provision to our allowance for loan and lease losses, with an additional provision of $700,000 during the first nine months of 2003. See "—Results of Operations—The UAL Leveraged Lease" for additional information on the UAL Leveraged Lease. As a result of this significant provision, our net income was adversely affected. In addition to the additional provision to our allowance for loan and lease losses, in reaction to the uncertainty caused by the UAL Leveraged Lease we restrained the rate of growth of our loan originations, and increased our federal funds sold and investment in short-term, but lower-yielding investment securities during 2002 and the early half of 2003. We charged off $1.0 million, $1.2 million and $1.0 million for the quarters ended September 30, 2003, December 31, 2003 and June 30, 2004, respectively. We have no further exposure to the UAL Leveraged Lease, and we currently have no exposure to any other leveraged lease.

In connection with the complete charge-off of the remaining balance of the UAL Leveraged Lease, and in part in response to changes in interest rates, we changed the mix of our assets by accelerating the growth of our loan originations, especially commercial real estate loans, reducing the amount of federal funds sold and investing in higher-yielding investment securities. Our net income grew at the rate of 23.46% for the year ended December 31, 2004 as compared to the year ended December 31, 2003. We expect to continue to shift our asset mix in this manner for the foreseeable future subject to changes in market conditions and other factors described in this offering circular.

An asset that continues to impact our performance is a property located at 60 Federal Street, San Francisco, California, or 60 Federal. We carry this property under other real estate owned, or OREO, in the amount of $8.3 million. We acquired 60 Federal by foreclosure on September 27, 2002. It consists of a five story, 88,156 square foot adapted warehouse and office building located in the "South of Market" area of San Francisco. 60 Federal currently generates annual operating income of approximately $496,000, which is included as noninterest income. The property was appraised in February 2003 for $8.8 million. We sold 60 Federal on March 15, 2005 for $9.0 million.

Critical Accounting Policies

Our accounting policies are integral to understanding the financial results reported. Our most complex accounting policies require management's judgment to ascertain the valuation of assets, liabilities, commitments and contingencies. We have established detailed policies and control procedures that are intended to ensure valuation methods are well controlled and consistently applied from period to period. In addition, these policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. The following is a brief description of our current accounting policies involving significant management valuation judgments.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses, or ALLL, represents our best estimate of losses inherent in the existing loan and lease portfolio. The allowance for loan and lease losses is increased by the provision for loan and lease losses charged to expense and reduced by loans and leases charged off, net of recoveries.

We evaluate our allowance for loan and lease losses quarterly. We believe that the allowance for loan and lease losses is a "critical accounting estimate" because it is based upon management's assessment of various factors affecting the collectibility of the loans and leases, including current economic conditions, past credit experience, delinquency status, the value of the underlying collateral, if any, and a continuing review of the portfolio of loans and leases.

Like all financial institutions, we maintain an ALLL based on a number of quantitative and qualitative factors. The amount of the allowance is based on management's evaluation of the collectibility of the loan and lease portfolio and that evaluation is based on historical loss experience and other significant factors. These other significant factors include the level and trends in delinquent, non-accrual and adversely classified loans and leases, trends in volume and terms of loans and leases, levels and trends in credit concentrations, effects of changes in underwriting standards, policies, procedures and practices, national and local economic trends and conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements.

We cannot provide you with any assurance that further economic difficulties or other circumstances which would adversely affect our borrowers and their ability to repay outstanding loans and leases will not occur. These difficulties or other circumstances could result in increased losses in our loan and lease portfolio, which could result in actual losses that exceed reserves previously established.

Allowance for Losses Related to Undisbursed Loan and Lease Commitments

We maintain a separate reserve for undisbursed loan and lease commitments. Management estimates the amount of probable losses by applying the loss factors used in our allowance for loan and lease loss methodology to our estimate of the expected usage of undisbursed commitments for each loan or lease type. Because the amount of the reserves were insignificant, we included them in the allowance for loan and lease losses.

Available-for-Sale Securities

Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities, requires that available-for-sale securities be carried at fair value. We believe this is a “critical accounting estimate” in that the fair value of a security is based on quoted market prices or if quoted market prices are not available, fair values are extrapolated from the quoted prices of similar instruments. Unrealized holding gains or losses, net of the related tax effect, on available-for-sale securities are excluded from income and are reported as a separate component of shareholders’ equity as other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. A decline in the fair value of any available-for-sale security below cost that is deemed to be other than temporary results in a reduction in carrying amount to fair value. The impairment is charged to income and a new cost basis for the security is established.

In March 2004, the Emerging Issue Task Force reached a consensus opinion on Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments, regarding the determination of whether an investment is considered impaired, whether the identified impairment is considered other-than-temporary, how to measure other-than-temporary impairment and how to disclose unrealized losses on investments that are not other-than-temporarily impaired. Adoption of the new measurement requirements has been delayed by the FASB pending reconsideration of implementation guidance relating to debt securities that are impaired solely due to market interest rate fluctuations.

Deferred Income Taxes

Deferred income taxes reflect the estimated future tax effects of temporary differences between the reported amount of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws and regulations. We use an estimate of future earnings to support our position that the benefit of our deferred tax assets will be realized. If future income should prove non-existent or less than the amount of the deferred tax assets within the tax years to which they may be applied, the asset may not be realized and our net income will be reduced.

Results of Operations

The following tables summarize key financial results for the periods indicated:

	Year Ended December 31,		
	2004	2003	2002
	(Dollars in thousands, except per share data)		
Net income	$11,152	$9,033	$4,403
Net income per share, basic	$ 2.02	$ 1.66	$ 0.82
Net income per share, diluted	$ 1.92	$ 1.58	$ 0.77
Return on average assets	1.33%	1.20%	0.65%
Return on average shareholders’ equity	15.51%	14.18%	7.30%

Year Ended December 31, 2004 Compared to Year Ended December 31, 2003

	Year Ended December 31,		
	2004	2003	Increase (Decrease)
	(In thousands, except per share data)		
Statement of Income Data:			
Interest income	$38,643	$34,376	$ 4,267
Interest expense	7,447	8,696	(1,249)
Net interest income	31,196	25,680	5,516
Provision for loan and lease losses	1,550	2,100	(550)
Net interest income after provision for loan and lease losses	29,646	23,580	6,066
Noninterest income	4,199	4,923	(724)
Noninterest expense	15,339	13,774	1,565
Income before provision for income taxes	18,506	14,729	3,777
Provision for income taxes	7,354	5,696	1,658
Net income	$11,152	$ 9,033	$ 2,119
Net income per share, basic	$ 2.02	$ 1.66	$ 0.36
Net income per share, diluted	$ 1.92	$ 1.58	$ 0.34

Net income increased 23.5% to $11.2 million, or $2.02 per share, for the year ended December 31, 2004, from $9.0 million, or $1.66 per share, for the year ended December 31, 2003. Our return on average assets was 1.33% and return on average shareholders' equity was 15.51% for the year ended December 31, 2004, compared to 1.20% and 14.18%, respectively, for the year ended December 31, 2003.

Net income improved significantly in 2004 from 2003, principally as a result of an increase in net interest income of $5.5 million, partially offset by an increase in noninterest expense of $1.6 million and a decrease in noninterest income of $724,000.

The $5.5 million, or 21.5%, increase in net interest income primarily resulted from increased loan volume, in particular commercial real estate loans, and a 31 basis point improvement in net interest margin. The improvement in net interest margin is the result of lower funding costs particularly with higher cost time deposits maturing and being replaced at lower prevailing rates. We also benefited from a change in the mix of our deposits toward lower cost noninterest-bearing demand deposits, interest-bearing demand deposits and money market accounts, and to a lesser extent an increase in the relative amount of higher-yielding investment securities and a reduction in the amount of federal funds sold and lower yielding securities we implemented in response to general interest rates.

As of December 31, 2004, 88% of our loan portfolio was tied to the Prime Rate, which reprices daily, and 10% was tied to the London Interbank Offer Rate, or LIBOR, or other indices, which reprice periodically. Approximately 52% of our loan portfolio had a floor interest rate at various levels, which can provide us with protection in a falling interest rate environment should the Prime Rate decline to a level below the floor interest rate. Approximately 7% of our loan portfolio had interest rate ceilings at various rates limiting the amount of interest rate increases that can be passed on to the borrower. Our weighted average maturity of certificates of deposit at December 31, 2004 was 3.45 months. As a result, our interest-bearing liabilities generally reprice much slower than our loan portfolio and our net income should be positively impacted by a rising interest rate environment.

Net Interest Income and Net Interest Margin

Our net interest income before the provision for loan and lease losses for the year ended December 31, 2004 increased $5.5 million, or 21.5%, as compared to the year ended December 31, 2003. This increase was due to a decrease of $1.2 million in interest expense, and an increase in interest income of $4.3 million. Total interest expense decreased primarily as a result of declines in interest rates with higher cost time certificates of deposit maturing and being replaced at lower prevailing rates. The $4.3 million increase in total interest income primarily was due to the increase in the volume of loans. The redeployment of lower yielding overnight investments into higher yielding investment securities also contributed to the increase in total interest income. This is reflected by the increase in our investment securities by $34.3 million and the corresponding decrease of $27.9 million in federal funds sold and securities purchased under resale agreements during 2004.

The cost of average interest-bearing liabilities declined to 1.25% for the year ended December 31, 2004 from 1.59% for the year ended December 31, 2003. The decline was primarily driven by favorable changes in interest rates with higher cost time deposits maturing and being replaced at lower prevailing rates. To a lesser degree, the increase in the ratio of average noninterest-bearing deposits to average total deposits from 21.43% to 19.37%, the decrease in the ratio of time certificates of deposit to average interest-bearing deposits from 55.69% to 59.33%, and the decrease in the cost of FHLB long-term borrowings all contributed to the decrease in the cost of average interest-bearing liabilities.

The average yield on our interest-earning assets increased slightly to 4.88% in year ended December 31, 2004 from 4.86% in the year ended December 31, 2003. The decline was mainly due to the declining interest rate environment with higher rate loans maturing and being replaced by loans at lower prevailing rates, as well as investment securities maturing or being called and reinvested at lower prevailing rates.

Our interest income, interest expense, net interest income, and net interest margin are influenced by the distribution of our assets and liabilities and the income earned and costs incurred on such assets and liabilities. The following table presents, for the periods indicated, the information regarding the distribution of average assets, liabilities and shareholders' equity, as well as the net interest income from average interest-earning assets and the resulting yields expressed in percentages. Non-accrual loans are included in the calculation of average loans and leases while non-accrued interest thereon is excluded from the computation of yields earned.

	Year Ended December 31, 2004			Year Ended December 31, 2003		
	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost
	(Dollars in thousands)					
ASSETS:						
Interest-earning assets:						
Loans and leases[1][2][3]	$541,402	$32,046	5.92%	$466,793	$28,301	6.06%
Investments securities[1]	159,229	5,272	3.31	124,964	4,656	3.73
Federal funds sold and securities purchased under resale agreements	81,948	1,105	1.35	109,839	1,273	1.16
Interest-bearing deposits with other banks						
Certificate of deposits with other banks	6,390	133	2.08	4,622	88	1.90
Other earning assets[4]	2,258	85	3.76	1,370	58	4.23
Total interest-earning assets	791,227	38,643	4.88	707,588	34,376	4.86
Noninterest earning assets:						
Cash and due from banks	29,590			26,756		
Other assets	19,448			17,753		
Total assets	$840,265			$752,097		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing liabilities:						
Deposits:						
Interest-bearing demand	$ 26,064	$ 82	0.31	$ 23,853	$ 44	0.18
Money market	118,039	735	0.62	93,067	506	0.54
Savings	24,311	76	0.31	22,008	85	0.39
Time certificates of deposit	409,894	6,196	1.51	386,948	7,452	1.93
Total interest-bearing deposits	578,308	7,089	1.23	525,876	8,087	1.54
Short-term borrowings	41	1	2.44	37	1	1.54
Long-term debt	17,582	357	2.03	21,219	608	2.87
Total interest-bearing liabilities	595,931	7,447	1.25	547,132	8,696	1.59
Non-interest-bearing liabilities:						
Demand deposits	157,688			126,361		
Other liabilities	14,750			14,900		
Total liabilities	768,369			688,393		
Shareholders' equity	71,896			63,704		
Total liabilities and shareholders' equity	$840,265			$752,097		
Net interest income		$31,196			$25,680	
Net interest spread			3.63			3.27
Net interest margin			3.94%			3.63%

(1) Yields on loans and leases and securities have not been adjusted to a tax-equivalent basis because the impact is not material.

(2) Includes average non-accrual loans and leases of $463,000 and $3.7 million for the year ended December 31, 2004 and 2003, respectively, primarily reflecting the balance of the UAL Leveraged Lease.

(3) Net loan and lease fees of $1.5 million and $1.2 million for the year ended December 31, 2004 and 2003, respectively, are included in the yield computations.

(4) Includes Federal Home Loan Bank stock.

As a result of the combination of: (1) interest income increasing, despite decreases in interest rates, primarily due to our decision to increase loan volume and to redeploy our investment portfolio to a larger amount of higher yielding investment securities and (2) interest expense decreasing because of lower market rates, our net interest margin increased to 3.94% in 2004 from 3.63% in 2003.

In addition to the distribution, yields and costs of our assets and liabilities, our net income is also affected by changes in the volume of and rates on our assets and liabilities. The following table shows the change in interest income and interest expense and the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates.

	Year Ended December 31, 2004 Compared to Year Ended December 31, 2003			
	Net Change	**Rate**	**Volume**	**Mix**
		(In thousands)		
Interest income:				
Loans and leases	$ 3,747	$ (685)	$4,442	$(10)
Investment securities	616	(561)	1,179	(2)
Federal funds sold and securities purchased under resale agreements	(168)	188	(356)	0
Interest-bearing deposits with other banks	45	9	36	0
Other earning assets	27	(7)	34	0
Total interest income	4,267	(1,056)	5,335	(12)
Interest expense:				
Interest-bearing demand	38	34	4	0
Money market	229	81	149	(1)
Savings	(9)	(17)	8	0
Time certificates of deposit	(1,256)	(1,682)	423	3
Short-term borrowings	0	0	0	0
Long-term debt	(251)	(158)	(93)	0
Total interest expense	(1,249)	(1,742)	491	2
Net interest income	$ 5,516	$ 686	$4,844	$(14)

As reflected above, due to our decision to increase our loan originations and to change the mix of our investment portfolio by increasing the amount of higher yielding investment securities, most of the increase in our net interest income during 2004 was attributable to a combination of increases in the volume of our interest earning assets and decreases in the cost of time certificates of deposit.

Provision for Loan and Lease Losses

The provision for loan and lease losses in each period is a charge against earnings in that period. The provision is that amount required to maintain the allowance for loan and lease losses at a level that, in management's judgment, is adequate to absorb loan and lease losses inherent in the loan and lease portfolio.

The provision for loan and lease losses for 2004 was $1.6 million as compared to $2.1 million for 2003. In 2004, we experienced net loan and lease charge-offs of $1.0 million as compared to net loan and lease charge-offs of $5.2 million for 2003. The decrease in our provision and in net loan and lease charge-offs during 2004 compared to 2003 was primarily the result of the $700,000 specific provision made and the $5.2 million charge-off of the remaining balance of the UAL Leveraged Lease taken during 2003 discussed below.

The UAL Leveraged Lease

In November 1997, we purchased for $6.6 million a leveraged aircraft lease, with United Airlines as lessee, subject to non-recourse debt outstanding at the time of $17.8 million. During 2002, United Airlines declared bankruptcy. Despite various restructuring proposals made during the subsequent 18 months, the subject aircraft was ultimately acquired by the non-recourse lender for the fair market value of the aircraft, an amount below the $15.0 million remaining loan balance, resulting in our investment being eliminated. As a result of these events, in 2002 we made a $8.6 million provision to our allowance for loan and lease losses, and charged-off $3.1 million of this investment. In 2003, we made an additional provision of $700,000 and charged-off $5.2 million. During 2004, we charged-off the remaining $1.0 million on this leveraged lease and made no additional provision. Our entire investment in the UAL Leveraged Lease has been charged-off as of May 31, 2004.

The following table summarizes the UAL Leveraged Lease, and the provision for losses, the specific allowances and the charge-offs pertaining to the lease losses for the periods indicated:

	UAL Leveraged Lease	Provision	Specific Allowances
		(In thousands)	
Total Lease Balance	$ 9,316[(1)]		
Provision in 2002		$8,616	$ 8,616
Charged-off in 2002	(3,084)		(3,084)
Lease Balance at December 31, 2002	6,232		5,53
Provision in 2003		700	700
Charged-off in 2003	(5,232)		(5,232)
Lease Balance at December 31, 2003	1,000		1,000
Charged-off in May 2004	(1,000)		(1,000)
Lease Balance at December 31, 2004	$ —	$9,316	$ —

(1) The $9.3 million balance as of December 31, 2002 reflects the original lease investment of $6.4 million plus recognized lease income from 1997 to 2002 of $2.9 million.

Noninterest Income

We earn noninterest income primarily through fees related to:

- services provided to deposit customers;
- services provided in connection with trade finance; and
- services provided to current and potential loan customers as well as loan pre-payment penalties.

In addition, we earn rental income from other real estate owned, such as 60 Federal, and income from increases in the surrender value of bank owned life insurance policies, or BOLI.

The following table presents, for the periods indicated, the major categories of noninterest income:

	Year Ended December 31, 2004	Year Ended December 31, 2003	Increase (Decrease)
	(In thousands)		
Service charges and fees on deposit accounts	$2,393	$2,419	$ (26)
Trade finance income	729	677	52
Increase in cash surrender value of life insurance	316	347	(31)
Net other real estate owned income	526	227	299
Gain on sale of investment securities, net	35	1,111	(1,076)
Other income	200	142	58
Total noninterest income	$4,199	$4,923	$ (724)

Total noninterest income decreased by $724,000 or 14.7%, to $4.2 million during 2004 from $4.9 million during 2003. The decrease principally relates to gain on sales of securities of $1.1 million during 2003 that were not repeated during 2004. This decrease in noninterest income during 2004, was partially offset by $299,000 of net other real estate owned income that was attributable to 60 Federal.

Our results can be influenced by the unpredictable nature of gains and losses in connection with the sale of investment securities and other real estate owned. We do not engage in active securities trading; however, from time to time we sell securities in our portfolio to realize gains or reduce losses, and to rebalance our portfolio. It is likely we will continue this practice in the future. From time to time, we acquire real estate in connection with non-performing loan transactions, and sell such real estate to recoup a portion of the principal amount of the defaulted loans. These sales can result in gains or losses from time to time that are not expected to occur in predictable patterns during future periods.

Service charges on deposit accounts increased primarily due to increase in non-sufficient funds charges and account analysis fees associated with demand deposit activities.

Noninterest Expense

Noninterest expense is the cost, other than interest expense and the provision for loan and lease losses, associated with providing banking and financial services to customers and conducting our business.

The following table presents, for the periods indicated, the major categories of noninterest expense:

	Year Ended December 31, 2004	Year Ended December 31, 2003	Increase (Decrease)
	(In thousands)		
Salaries and employee benefits	$ 9,741	$ 8,733	$1,008
Net occupancy expense	1,826	1,745	81
Business development and promotion expense	250	270	(20)
Professional fees	855	799	56
Office supplies and equipment expense	754	721	33
Other expense	1,913	1,506	407
Total noninterest expense	$15,339	$13,774	$1,565

Total noninterest expense increased $1.6 million, or 11.4%, to $15.3 million during 2004 from $13.8 million during 2003. Salaries and employee benefits increased $1.0 million, or 11.5%, principally as a result of an

increase in bonus accrual of $888,000 and normal salary and staff increases of $120,000. We had 113 and 104 full-time equivalent employees at December, 2004 and 2003, respectively. If we are successful in opening the two new branch offices in 2005 and in implementing other aspects of our strategic plan, it is likely that our salaries and employee benefits and net occupancy expense will increase. It is also expected that as a public company our professional expenses will increase significantly in connection with additional reporting and compliance requirements.

Provision for Income Taxes

We recorded a tax provision of $7.4 million for 2004 and $5.7 million for 2003. Our effective tax rates were 39.7% and 38.7% for 2004 and 2003, respectively, as compared to the expected effective tax rate of 42.1%. The difference from the expected rates in both periods is due to the nontaxable nature of income from municipal securities and BOLI.

Year Ended December 31, 2003 Compared to Year Ended December 31, 2002

	Year Ended December 31,		Increase
	2003	2002	(Decrease)
	(In thousands, except per share data)		
Statement of Income Data:			
Interest income	$34,376	$33,902	$ 474
Interest expense	8,696	10,718	(2,022)
Net interest income	25,680	23,184	2,496
Provision for loan and lease losses	2,100	10,146[(1)]	(8,046)
Net interest income after provision for loan and lease losses	23,580	13,038	10,542
Noninterest income	4,923	4,514	409
Noninterest expense	13,774	10,261	3,513
Income before provision for income taxes	14,729	7,291	7,438
Provision for income taxes	5,696	2,888	2,808
Net income	$ 9,033	$ 4,403	$ 4,630
Net income per share, basic	$ 1.66	$ 0.82	$ 0.84
Net income per share, diluted	$ 1.58	$ 0.77	$ 0.81

(1) Includes $8.6 million attributed to UAL Leveraged Lease.

Net income increased 105.2% to $9.0 million, or $1.66 per share and $1.58 per share for basic and diluted earnings per share, respectively, for the year ended December 31, 2003, from $4.4 million, or $0.82 per share and $0.77 per share for basic and diluted earnings per share, respectively, for the year ended December 31, 2002. Our return on average assets was 1.20% and return on average shareholders' equity was 14.18% for the year ended December 31, 2003, compared to 0.65% and 7.30%, respectively, for the year ended December 31, 2002.

Net Interest Income and Net Interest Margin

Our net interest income before the provision for loan and lease losses for the year ended December 31, 2003 increased $2.5 million, or 10.8%, as compared to the year ended December 31, 2002. This increase was due to a decrease of $2.0 million in interest expense, and an increase in interest income of $474,000. Total interest expense decreased primarily due to declining interest rates throughout the financial marketplace, which resulted in higher cost time certificates of deposit maturing and being replaced at lower prevailing rates. To a lesser degree, interest expense attributable to core deposits, which includes interest-bearing demand, money market and savings accounts, also decreased. The slight increase in interest income is due to the higher volume of loans, primarily commercial

real estate loans and commercial loans, which was largely offset by the decrease in the yield on such loans resulting from declines in market interest rates. Further, although the average balance in investment securities increased by $14.5 million during this period, the yield on the investment securities continued to decline as investment securities that matured or were called were reinvested at lower prevailing rates.

The cost of average interest-bearing liabilities declined to 1.59% in the year ended December 31, 2003 from 2.16% in the year ended December 31, 2002. The decline was temporarily driven by favorable changes in interest rates with higher cost time deposits maturing and being replaced at lower prevailing rates and the decrease in the interest expense on core deposits as a result of the lower interest rate environment.

The average yield on interest-earning assets declined 47 basis points to 4.86% in the year ended December 31, 2003 from 5.33% in the year ended December 31, 2002. The decline was attributed to the repricing of the interest rates on our adjustable rate loans as a result of declines in the Prime Rate, and to our investment securities that matured or were called and reinvested at lower prevailing rates.

The following table presents, for the years indicated, the information regarding the distribution of average assets, liabilities and shareholders' equity, as well as the net interest income from average interest-earning assets and the resultant yields expressed in percentages. Non-accrual loans are included in the calculation of average loans and leases while non-accrued interest thereon, is excluded from the computation of yields earned.

	Year Ended December 31, 2003			Year Ended December 31, 2002		
	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost
	(Dollars in thousands)					
ASSETS						
Interest-earning assets:						
Loans and leases[1][2][3]	$466,793	$28,301	6.06%	$418,845	$26,910	6.42%
Investment securities[1]	124,964	4,656	3.72	110,498	5,128	4.64
Federal funds sold and securities purchased under resale agreements	109,839	1,273	1.16	105,487	1,812	1.72
Interest-bearing deposits with other banks	4,622	88	1.91	317	9	2.84
Other earning assets[4]	1,370	58	4.21	906	43	4.75
Total interest-earning assets	707,588	34,376	4.86	636,053	33,902	5.33
Noninterest earning assets:						
Cash and due from banks	26,756			24,898		
Other assets	17,753			18,234		
Total assets	$752,097			$679,185		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing liabilities:						
Deposits:						
Interest-bearing demand	$ 23,853	$ 44	0.18	$ 19,693	$ 52	0.26
Money market	93,067	506	0.54	64,601	476	0.74
Savings	22,008	85	0.39	22,154	148	0.67
Time certificates of deposit	386,948	7,452	1.93	363,195	9,424	2.59
Total interest-bearing deposits	525,876	8,087	1.54	469,643	10,100	2.15
Short-term borrowings	37	1	1.54	14,026	220	1.57
Long-term debt	21,219	608	2.87	12,027	398	3.31
Total interest-bearing liabilities	547,132	8,696	1.59	495,696	10,718	2.16
Noninterest-bearing liabilities:						
Demand deposits	126,361			111,491		
Other liabilities	14,900			11,713		
Total liabilities	688,393			618,900		
Shareholders' equity	63,704			60,285		
Total liabilities and shareholders' equity	$752,097			$679,185		
Net interest income		$25,680			$23,184	
Net interest spread			3.27			3.17
Net interest margin			3.63%			3.65%

(1) Yields on loans and leases and securities have not been adjusted to a tax-equivalent basis because the impact is not material.
(2) Includes average non-accrual loans and leases of $3.7 million in 2003 and $1.8 million in 2002.
(3) Net loan and lease fees of $1.2 million for 2003 and $884,000 for 2002 are included in the yield computations.
(4) Includes Federal Home Loan Bank stock.

As a result of the significant decline in the yields on our interest earning assets, at a rate faster than the decline in the cost of our interest bearing liabilities during 2003 compared to 2002, our net interest margin decreased to 3.63% in 2003 from 3.65% in 2002.

The following table shows the change in interest income and interest expense and the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates.

	Year Ended December 31, 2003 Compared to Year Ended December 31, 2002			
	Net Change	Rate	Volume	Mix
	(In thousands)			
Interest income:				
Loans and leases	$ 1,391	$(1,572)	$2,963	$0
Investment securities	(472)	(1,090)	618	0
Federal funds sold and securities purchased under resale agreements	(539)	(611)	72	0
Interest-bearing deposits with other banks	79	(4)	83	0
Other earning assets	15	(5)	20	0
Total interest income	474	(3,282)	3,756	0
Interest expense:				
Interest-bearing demand	(8)	(18)	10	0
Money market	30	(145)	175	0
Savings	(63)	(62)	(1)	0
Time certificates of deposit	(1,972)	(2,556)	584	0
Short-term borrowings	(219)	(4)	(215)	0
Long-term debt	210	(59)	269	0
Total interest expense	(2,022)	(2,844)	822	0
Net interest income	$ 2,496	$ (438)	$2,934	$0

Noninterest Income

The following table presents, for the years indicated, the major categories of noninterest income:

	Year Ended December 31,		Increase (Decrease)
	2003	2002	
	(In thousands)		
Service charges and fees on deposit accounts	$2,419	$2,252	$167
Trade finance income	677	581	96
BOLI income	347	366	(19)
Net other real estate owned income	227	240	(13)
Gain on sale of investment securities, net	1,111	931	180
Other income	142	144	(2)
Total noninterest income	$4,923	$4,514	$409

Total noninterest income increased by $409,000, or 9.1%, to $4.9 million in 2003 from $4.5 million in 2002. The largest component of noninterest income, income from service charges and fees on deposit accounts,

increased 7.4% to $2.4 million in 2003 from $2.3 million in 2002. Average balances in transaction accounts (demand deposits, money market and interest-bearing demand accounts) increased 24.3% in 2003 as compared to 2002. The smaller increase in revenues from transaction accounts as compared to average outstanding transaction account balances reflects the impact of the growth in our business deposit accounts. Service charges on these accounts typically are more a function of account activity than of average balance. Gain on sale of investment securities reflects gains realized during 2003 as we took advantage of market conditions and we began to implement a re-balancing of our investment portfolio, which required the sale of certain of our securities.

Noninterest Expense

The following table presents, for the years indicated, the major categories of noninterest expense:

	Year Ended December 31,		Increase (Decrease)
	2003	2002	
	(In thousands)		
Salaries and employee benefits	$ 8,733	$ 5,532	$3,201
Net occupancy expense	1,745	1,626	119
Business development and promotion expense	270	229	41
Professional fees	799	875	(76)
Office supplies and equipment expense	721	753	(32)
Other	1,506	1,246	260
Total noninterest expense	$13,774	$10,261	$3,513

Total noninterest expense increased $3.5 million, or 34.2%, to $13.8 million in 2003 from $10.3 million in 2002. The increase was principally the result of an increase in salaries and employee benefits of $3.2 million from $5.5 million in 2002 to $8.7 million in 2003. The increase in salaries and employee benefits of $3.2 million consists of a $2.5 million increase in bonus accrual and $681,000 increase from normal salary and staff increases. The lower bonus accrual in 2002 was attributable to lower earnings for the year.

Provision for Income Taxes

We recorded tax provisions of $5.7 million in 2003 and $2.9 million in 2002. Our effective tax rates were 38.7% for 2003 and 39.6% for 2002, as compared to the expected effective tax rate of 42.1%. The difference from the expected rate in both years is largely due to the nontaxable nature of income from municipal securities and BOLI.

Financial Condition

For the period between December 31, 2003 and December 31, 2004, our assets, loans and deposits grew at the rate of 19.1%, 22.2% and 20.9%, respectively. During the three-year period ended December 31, 2004, our assets, loans and deposits grew by 37.8%, 64.6% and 39.1%, respectively. Our total assets at December 31, 2004 were $907.3 million compared to $761.8 million at December 31, 2003. Our earning assets at December 31, 2004 totaled $847.1 million compared to $712.6 million at December 31, 2003. Total deposits at December 31, 2004 and December 31, 2003 were $801.5 million and $662.8 million, respectively.

Loans and Leases

The largest component of our assets and source of interest income is our loan portfolio. The following table sets forth the amount of our loans and leases outstanding at the end of each of the periods indicated. We had no foreign loans or energy-related loans as of the dates indicated.

	Year Ended December 31,				
	2004	2003	2002	2001	2000
Loans and leases:					
Real estate—mini-perm	$358,221	$250,993	$214,661	$138,829	$123,482
Real estate—construction	112,002	94,816	85,584	78,031	45,207
Commercial	98,547	117,607	108,767	122,808	121,528
Trade finance	45,951	37,829	31,439	31,687	30,759
Consumer	222	348	446	409	645
Leases receivable and other	1,018	2,460	7,615	2,396	2,990
Total gross loans and leases	615,961	504,053	448,512	374,160	324,611
Less: allowance for loan and lease losses	(6,724)	(6,168)	(9,257)	(4,906)	(4,391)
Deferred loan and lease fees, net	(2,382)	(1,395)	(1,212)	(865)	(777)
Total net loans and leases	$606,855	$496,490	$438,043	$368,389	$319,443

Our total loans and leases increased by $111.9 million, or 22.2% between December 31, 2004 and December 31, 2003. This follows increases of $55.5 million, or 12.4% between December 31, 2003 and 2002, $74.35 million, or 19.9% between December 31, 2002 and 2001, and $49.55 million, or 15.3% between December 31, 2001 and 2000. Most of this loan growth has been in real estate mini perm loans (typically loans secured by a first trust deed on income producing real estate amortizing over 25 years and due in 5 years) and construction loans. This growth reflects the strong real estate economy in the Southern California market during this period.

Our real estate mini-perm loan portfolio grew during 2004 by $107.2 million, or 42.7%, to $358.2 million at December 31, 2004 from $251.0 million at December 31, 2003, and grew in 2003 by $36.3 million, or 16.9%, from $214.7 million at December 31, 2002. This follows a $75.83 million, or 54.6% increase at December 31, 2002 compared to December 31, 2001. We believe this growth reflects a combination of our marketing efforts as well as a reduction of competition for permanent financing for smaller retail and office properties from other sources, such as insurance companies, during portions of this period. We are unable to predict whether these other sources will provide permanent financing on these properties at higher levels. If they or other sources offer permanent financing on these properties, we may not be able to continue to grow our portfolio at rates experienced in 2003 and 2004.

The following table provides information about our real estate mini-perm portfolio by property type:

	Year Ended December 31, 2004	
Property Type	Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial/Office	$ 76,820	12.47%
Industrial	53,882	8.75
Retail	106,716	17.33
Apartment 4+	38,967	6.33
Residential 1-4	34,654	5.63
Other	47,182	7.65
Total	$358,221	58.16%

Real estate construction loans grew during 2004 by $17.2 million to $112.0 million at December 31, 2004 from $94.8 million at December 31, 2003, and grew in 2003 by $9.2 million, or 10.8%, from $85.6 million at December 31, 2002. This follows a modest increase of $7.55 million, or 9.68%, at December 31, 2002 compared to December 31, 2001. We have grown our construction loan portfolio modestly during this period, which reflects adherence to our underwriting criteria and our additional caution during 2002, 2003 and 2004 as we addressed the UAL Leveraged Lease. We expect the construction portfolio will continue to grow modestly in the future subject to market conditions and interest rates.

Commercial loans outstanding at December 31, 2004 declined by $19.1 million, or 16.2%, to $98.5 million at December 31, 2004 from $117.6 million at December 31, 2003, and increased modestly in 2003 by $8.8 million, or 8.1%, from $108.8 million at December 31, 2002. Total commercial loan commitments (including undisbursed amounts) at December 31, 2004 increased $18.9 million or 10.2% to $203.7 million compared to $184.8 million at December 31, 2003. During this period, the rate of credit utilization declined from 63.7% at December 31, 2003 to 48.4% at December 31, 2004 causing the lower balance of outstanding commercial loans. We believe the lower utilization rate reflects the addition of new customer relationships who have not yet used the lines of credit established for them as well as caution by our existing customers in using credit lines in reaction to uncertain economic conditions. Subject to market conditions and interest rates, we intend to expand our commercial loans in the future through enhanced marketing efforts and expansion of our branch network.

Trade finance loans grew during 2004 by $8.1 million, or 21.5%, to $46.0 million at December 31, 2004, and grew in 2003 by $6.4 million, or 20.3%, from $31.4 million at December 31, 2002. We believe this modest increase in trade finance reflects both caution by our trade finance customers comparable to that of our commercial loan customers as well as continued caution by us in the application of our underwriting standards. It is possible that if the U.S. dollar continues to weaken against other foreign currencies, as it has during 2004, the cost of imported goods will increase, which could have an adverse impact on some of our customers who import goods for resale in the United States.

Leases receivable and other loans declined during 2004 by $1.4 million, or 58.6%, to $1.0 million at December 31, 2004 from $2.5 million at December 31, 2003, and declined by $5.2 million, or 67.7%, from $7.6 million at December 31, 2002. The decline in both periods was principally due to the $1.0 million and $5.2 million charge-offs in 2004 and 2003, respectively, with respect to the UAL Leveraged Lease.

Non-Performing Assets

Generally, loans and leases are placed on non-accrual status when they become 90 days or more past due or at such earlier time as management determines timely recognition of interest to be in doubt. Accrual of interest is discontinued on a loan or lease when management believes, after considering economic and business conditions and collection efforts, that the borrower’s financial condition is such that collection of interest is doubtful.

At December 31, 2004 and 2003, we had one OREO property, 60 Federal, with an aggregate carrying value of $8.3 million. At December 31, 2002, we had $8.2 million in OREO properties compared to $795,000 at December 31, 2001. For the year ended December 31, 2004, our net year to date OREO income was $526,000.

We record all OREO properties at the lower of the carrying value of the loan or fair market value of the property based on current appraisals, less estimated selling costs.

The following table summarizes the loans and leases for which the accrual of interest has been discontinued and loans and leases more than 90 days past due and still accruing interest, including those loans and leases that have been restructured, and OREO:

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(Dollars in thousands)				
Non-accrual loans and leases, not restructured	$ 382	$1,000	$ 6,235	$2,077	$4,388
Accruing loans and leases past due 90 days or more	—	—	—	3,956	40
Restructured loans and leases	—	—	—	—	—
Total non-performing loans (NPLs)	382	1,000[(1)]	6,235[(1)]	6,033	4,428
OREO	8,258[(2)]	8,258[(2)]	8,188[(2)]	795	—
Total non-performing assets (NPAs)	$8,641	$9,258	$14,423	$6,828	$4,428
Selected ratios:					
NPLs to total loans and leases held for investment	0.06%	0.20%	1.39%	1.61%	1.37%
NPAs to total assets	0.95%	1.22%	2.04%	1.04%	0.75%

(1) Represents the UAL Leveraged Lease.

(2) Represents 60 Federal.

The amount of interest income that we would have recorded on non-accrual and impaired loans and leases had the loans and leases been current totaled $11,000 during 2004, $132,000 for 2003, $26,000 for 2002 and $633,000 for 2001. All payments received on loans classified as non-accrual are applied first to principal. Accordingly, interest income on such loans and leases was not significant during 2004 or during 2003, 2002 and 2001.

Impaired Loans and Leases

Impaired loans and leases are commercial, commercial real-estate, other real-estate related and individually significant mortgage and consumer loans and leases for which it is probable that we will not be able to collect all amounts due according to the contractual terms of the loan or lease agreement. The category of impaired loans and leases is not coextensive with the category of non-accrual loans and leases, although the two categories overlap. Non-accrual loans and leases include impaired loans and leases that are not reviewed on an individual basis for impairment. Management may choose to place a loan or lease on non-accrual status due to payment delinquency or uncertain collectibility, while not classifying the loan or lease as impaired if it is probable that we will collect all amounts due in accordance with the original contractual terms of the loan or lease or the loan or lease is not a commercial, commercial real estate, other real estate related or an individually significant mortgage or consumer loan or lease.

In determining whether or not a loan or lease is impaired, we apply our normal loan and lease review procedures on a case-by-case basis taking into consideration the circumstances surrounding the loan or lease and borrower, including the collateral value, the reasons for the delay, the borrower's prior payment record, the amount of the shortfall in relation to the principal and interest owed and the length of the delay. We measure impairment on a loan-by-loan basis using either the present value of expected future cash flows discounted at the loan's or lease's effective interest rate or at the fair value of the collateral if the loan or lease is collateral dependent, less estimated selling costs. Loans or leases for which an insignificant shortfall in amount of payments is anticipated, but where we expect to collect all amounts due, are not considered impaired.

We had no impaired loans or leases at December 31, 2004, $1.0 million at December 31, 2003 and $6.2 million at December 31, 2002. The total allowance for loan and lease losses related to these loans and leases was $0 at December 31, 2004, $850,000 at December 31, 2003 and $4.4 million at December 31, 2002. The large allowance during 2002 reflected the UAL Leveraged Lease.

At December 31, 2004, we had no loans not disclosed above as non-accrual loans, as to which management has serious doubts as to the ability of the borrower to comply with the present loan repayment terms.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses is maintained at a level which, in management's judgment, is adequate to absorb loan and lease losses inherent in the loan and lease portfolio. The amount of the allowance is based on management's evaluation of the collectibility of the loan and lease portfolio and that evaluation is based on historical loss experience and other significant factors. These other significant factors include the level and trends in delinquent, non-accrual and adversely classified loans and leases, trends in volume and terms of loans and leases, levels and trends in credit concentrations, effects of changes in underwriting standards, policies, procedures and practices, national and local economic trends and conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements.

We must maintain an adequate allowance for loan and lease losses, or ALLL, based on a comprehensive methodology that assesses the probable losses inherent in the loan portfolio. The appropriateness of both the methodology and the adequacy of the ALLL are the responsibility of the Chief Credit Officer under the supervision of our board of directors. Each quarter end, our Chief Credit Officer must assess the methodology and adequacy of the ALLL, representing that they comply with applicable banking regulations and generally accepted accounting principles.

Like all financial institutions, we maintain an ALLL based on a number of quantitative and qualitative factors, including those discussed above. Provisions for loan and lease losses are provided on both a specific and general basis. Specific allowances are provided for specific credits for which the expected/anticipated loss is measurable. General valuation allowances are based on the historical loss experience in those categories covering the most recent eight quarters, as well as factors noted above.

The table below summarizes loans and leases, average loans and leases, non-performing loans and leases and changes in the allowance for loan and lease losses arising from loan and lease losses and additions to the allowance from provisions charged to operating expense:

Allowance For Loan Losses & Loss Histories

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(Dollars in thousands)				
Allowance for loan losses:					
Balance at beginning of period	$ 6,168	$ 9,257	$ 4,906	$ 4,391	$ 3,284
Actual charge-offs:					
Commercial	103	39	1,947	222	79
Trade finance	0	74	653	8	0
Construction	0	0	0	0	0
Real estate (mini-perm)	0	0	549	0	0
Leveraged lease	1,000	5,232	3,084	219	150
Other (credit card)	0	0	1	0	0
Total charge-offs	1,103	5,345	6,234	449	229
Less recoveries:					
Commercial	106	45	16	64	6
Trade finance	0	111	60	0	0
Construction	0	0	0	0	0
Real estate (mini-perm)	0	0	363	0	0
Leveraged leases	0	0	0	0	0
Other	3	0	0	0	0
Total recoveries	109	156	439	64	6
Net loans charged-off	994	5,189	5,795	385	223
Provision for loan losses	1,550	2,100	10,146	900	1,330
Balance at end of period	$ 6,724	$ 6,168	$ 9,257	$ 4,906	$ 4,391
Total loans at end of period	$615,961	$504,063	$448,512	$374,160	$324,611
Average total loans	541,402	466,793	418,845	338,097	297,792
Non-performing loans and leases	382	1,000	6,418	6,033	4,428
Selected ratios:					
Net charge-offs to average loans and leases[(1)]	0.18%	1.11%	1.38%	0.11%	0.07%
Provision for allowance for loan and lease losses to average loans and leases[(1)]	0.29%	0.45%	2.42%	0.27%	0.45%
Allowance for loan and lease losses to loans and leases at end of period	1.09%	1.22%	2.06%	1.31%	1.35%
Allowance for loan and lease losses to non-performing loans and leases	1758.64%	616.80%	144.23%	81.32%	99.16%

(1) Net charge-offs to average loans and leases and provisions for allowance for loan and lease losses to average loans and leases for the nine months ended September 30, 2004 are calculated on an annualized basis.

The allowance for loan and lease losses of $6.7 million at December 31, 2004 represented 1.09% of total loans and leases, net of deferred fees and costs. At December 31, 2003, the allowance for loan and lease losses totaled $6.2 million, or 1.22% of total loans and leases, net of deferred fees and costs, and 616.8% of non-performing loans and leases as of that date. At December 31, 2002, the allowance for loan and lease losses

totaled $9.3 million, or 2.06% of total loans and leases, net of deferred fees and costs, and 144.2% of non-performing loans and leases. Net charge-offs to average loans and leases were 0.18% for 2004 compared to 1.11% for the year ended December 31, 2003. This decrease is primarily related to the UAL Leveraged Lease write-off of $5.2 million in 2003. See "—Critical Accounting Policies," and Note 5 of the "Notes to Financial Statements." Of the total net loan and lease charge-offs during 2004 and for each of 2003 and 2002, charge-offs of the UAL Leveraged Lease represented 100.60%, 100.83%, and 53.22%.

In allocating our allowance for loan and lease losses, management has considered the credit risk in the various loan and lease categories in our portfolio. As such, the allocations of the allowance for loan and lease losses are based upon average historical net loan and lease loss experience and the other factors discussed above. While every effort has been made to allocate the allowance to specific categories of loans, management believes that any allocation of the allowance for loan and lease losses into loan categories lends an appearance of precision that does not exist.

The following table indicates management's allocation of the allowance and the percent of loans in each category to total loans and leases as of each of the following dates:

	At December 31,									
	2004		2003		2002		2001		2000	
	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans
	(Dollars in thousands)									
Commercial*	$1,511	16.0%	$1,390	23.3%	$1,392	24.2%	$1,487	31.8%	$ 397	36.7%
Trade finance*	645	7.5	438	7.5	556	7.0	481	8.3	357	9.3
Real estate construction*	1,064	18.2	508	18.8	623	19.1	408	20.9	113	13.7
Real estate (mini-perm)*	3,456	58.1	2,132	49.8	1,662	47.9	1,024	36.4	657	37.3
Lease	7	0.1	861	0.4	4,380	1.6	433	2.4	247	2.7
Other	4	0.1	12	0.2	12	0.2	5	0.2	4	0.3
Unallocated	37	0.0	827	0.0	632	0.0	1,068	0.0	2,617	0.0
Total	$6,724	100.0%	$6,168	100.0%	$9,257	100.0%	$4,906	100.0%	$4,392	100.0%

* These categories include watch list credits.

As noted above, we reserved for the UAL Leveraged Lease in 2002 and wrote the remaining balance off in 2003 and 2004. Since this was the only asset of its type, we have not established a "lease portfolio" category for lease loss analysis nor allocation within the overall ALLL. After 2000, we revised our methodology to allocate the allowance more specifically among the various portfolios utilizing qualitative factors including concentrations and trends within the portfolio.

Allowance for Losses Related to Undisbursed Loan and Lease Commitments

We maintain a reserve for undisbursed loan and lease commitments. Management estimates the amount of probable losses by applying the loss factors used in our allowance for loan and lease loss methodology to our estimate of the expected usage of undisbursed commitments for each loan and lease type. The allowance for undisbursed loan and lease commitments totaled $149,000, $102,000 and $85,000 and represented 0.05%, 0.05% and 0.04% of unfunded loan and lease commitments at September 30, 2004 and December 31, 2003 and 2002, respectively. Because the amount of the reserves were insignificant, we included them in the allowance for loan and lease losses.

Investment Securities Available for Sale

Our portfolio of investment securities consists primarily of U.S. Treasury securities, government agencies, investment grade corporate notes, mortgage-backed securities, municipal bonds and FHLMC preferred stock, which is included in other securities. We carry our entire securities portfolio as available-for-sale securities. We invest in securities to generate interest income and to maintain a liquid source of funding for our lending and other operations, including withdrawals of deposits. While we do not engage in active trading in our investment securities portfolio, we have realized and intend to realize gains from sales of selected securities primarily in response to changes in interest rates.

The carrying value of our investment securities at December 31, 2004 totaled $164.6 million compared to $155.9 million at December 31, 2003. During 2004, we significantly increased our investment portfolio as a relative component of our total assets at December 31, 2004 which was 18.15% compared to 20.46% at December 31, 2003. This reflects continuing growth in our deposits and a strategic decision to increase liquidity. During 2004, the increase in our investment securities portfolio reflects a continuation of deposit growth as well as a strategic decision to reduce the amount of lower yielding federal funds sold and securities purchased under resale agreements and to increase our investment in higher yielding securities.

The carrying value of our portfolio of investment securities at December 31, 2004, 2003 and 2002 was as follows:

	Estimated Market Value At December 31,		
	2004	2003	2002
	(In thousands)		
U.S. Treasury securities	$ —	$ 1,016	$ 1,053
U.S. Government agencies	71,027	36,321	44,287
Corporate notes	53,913	72,217	42,625
Mortgage-backed securities	12,713	17,579	5,946
Municipal securities	19,111	26,127	—
Other securities	7,871	2,609	4,050
Total available-for-sale	$164,635	$155,869	$97,961

The following table shows the maturities of investment securities at December 31, 2004, and the weighted average yields of such securities (municipal securities are not on a tax-equivalent basis):

	December 31, 2004									
	Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)									
U.S. Treasury Securities	$ —	0.00%	$ —	0.00%	$ —	0.00%	$ —	0.00%	$ —	%
U.S. Government Agencies	23,972	2.23	47,056	2.89	—	0.00	—	0.00	71,027	2.66
Corporate notes	27,269	2.52	19,794	5.59	5,347	6.69	1,502	8.22	53,913	4.18
Mortgage-backed securities	3,946	2.59	6,616	3.23	1,386	3.29	765	4.21	12,713	3.10
Municipal securities	—	0.00	1,936	3.65	5,506	3.79	11,669	4.07	19,111	3.94
Other securities	5,352	2.49		0.00	—	0.00	2,519	2.38	7,871	2.45
Total available-for-sale	$60,539	2.40%	$75,402	3.62%	$12,239	4.95%	$16,455	4.17%	$164,635	3.33%

The following table shows the maturities of investment securities at December 31, 2003, and the weighted average yields of such securities (municipal securities are not on a tax-equivalent basis):

	At December 31, 2003									
	Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)									
U.S. Treasury Securities	$ 1,016	4.22%	$ —	0.00%	$ —	0.00%	$ —	0.00%	$ 1,016	4.22%
U.S. Government Agencies	4,007	2.23	32,314	2.45	—	—	—	—	36,321	2.42
Corporate notes	29,761	2.16	34,522	4.25	6,457	6.60	1,478	8.22	72,218	3.68
Mortgage-backed securities	7,583	2.37	7,777	2.22	2,023	4.48	195	2.50	17,578	2.55
Municipal securities	7,454	1.74	1,915	3.65	5,418	3.79	11,340	4.07	26,127	3.94
Other securities	—	0.00	—	0.00	—	0.00	2,609	1.78	2,609	1.75
Total available-for-sale	$49,821	2.18%	$76,528	3.27%	$13,898	5.19%	$15,622	3.76%	$155,869	3.14%

Additional information concerning investment securities is provided in Note 4 of the “Notes to Financial Statements” contained elsewhere in this offering circular.

Deposits

We have experienced continuous growth in deposits since inception. Total deposits were $801.5 million at December 31, 2004 compared to $662.8 million at December 31, 2003. Noninterest-bearing demand deposits increased to $180.8 million at December 31, 2004 compared to $135.3 million at December 31, 2003. The ratio of noninterest-bearing deposits to total deposits was 22.6% at December 31, 2004 and 20.4% at December 31, 2003. Interest-bearing deposits are comprised of money market accounts, regular savings accounts, time deposits of under $100,000 and time deposits of $100,000 or more.

The following table shows the average amount and average rate paid on the categories of deposits for each of the periods indicated:

	Year Ended December 31,					
	2004		2003		2002	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
	(Dollars in thousands)					
Noninterest-bearing deposits	$157,688	0.00%	$126,361	0.00%	$111,491	0.00%
Interest-bearing demand deposits	26,064	0.31	23,853	0.18	19,693	0.27
Money market	118,039	0.62	93,067	0.54	64,601	0.74
Savings	24,311	0.31	22,008	0.39	22,154	0.67
Time certificates of deposit	409,894	1.51	386,948	1.93	363,195	2.59
Total	$735,996	0.96%	$652,237	1.23%	$581,134	1.74%

Average total deposits increased steadily through 2004. The increase in average total deposits for 2004 was primarily driven by increases of $25.0 million, $31.3 million, and $22.9 million, respectively in money market accounts, noninterest bearing demand deposits, and time certificates of deposit of $100,000 or more. We intend to increase the relative percentage of noninterest bearing demand deposits through the growth in our commercial lending activities and planned branch expansion. However, to the extent interest rates increase, customers will be more likely to re-allocate their cash from noninterest bearing demand deposits to interest bearing demand, money market and savings accounts. Additional information concerning deposits is provided in Note 7 of the “Notes to Financial Statements” contained elsewhere in the offering circular.

The largest component of our deposits has been, and in the near term is likely to be, time certificates of deposit of $100,000 or more. We market and receive time certificates of deposit from our existing and new high net worth customers, especially from the Chinese communities within our branch network. While we do not attempt to be a market leader in offered interest rates, we attempt to offer competitive rates on these time certificates of deposit within a range offered by other banks with which we compete.

The following table shows the maturities of time certificates of deposit and other time deposits of $100,000 or more at December 31, 2004:

	At December 31, 2004
	(In thousands)
Due in three months or less	$236,360
Due in over three months through six months	64,340
Due in over six months through twelve months	67,661
Due in over twelve months	300
Total	$368,661

Capital Resources

Current risk-based regulatory capital standards generally require banks to maintain a ratio of "core" or "Tier 1" capital (consisting principally of common equity) to risk-weighted assets of at least 4%, a ratio of Tier 1 capital to adjusted total assets (leverage ratio) of at least 4% and a ratio of total capital (which includes Tier 1 capital plus certain forms of subordinated debt, a portion of the allowance for loan and lease losses and preferred stock) to risk-weighted assets of at least 8%. Risk-weighted assets are calculated by multiplying the balance in each category of assets by a risk factor, which ranges from zero for cash assets and certain government obligations to 100% for some types of loans, and adding the products together.

Our goal is to exceed the minimum regulatory capital requirements for well-capitalized institutions. At December 31, 2004, our capital ratios were above the minimum requirements for well-capitalized institutions. In the future, we intend to make minor adjustments and increase our investment securities portfolio, such as reducing our investments in corporate notes, which are 100% risk weighted assets, and increasing our investments in mortgage-backed securities or U.S. agency notes, which are generally 20% risk weighted assets. In addition, in the future, we intend to originate credit lines when possible for 365 days or less, which are 0% risk weighted assets, instead of 366 days or more, which are 50% risk weighted assets. We believe that our existing capital, along with the net proceeds to us from this offering, will be sufficient for the foreseeable future to satisfy minimum regulatory capital requirements, including as those increase due to our presently anticipated growth in our loan portfolio.

	At December 31, 2004	At December 31, 2003
Leverage Ratio		
Preferred Bank	9.30%	8.74%
Minimum requirement for "Well-Capitalized" institution	5.00%	5.00%
Minimum regulatory requirement	4.00%	4.00%
Tier 1 Risk-Based Capital Ratio		
Preferred Bank	9.33%	9.52%
Minimum requirement for "Well-Capitalized" institution	6.00%	6.00%
Minimum regulatory requirement	4.00%	4.00%
Total Risk-Based Capital Ratio		
Preferred Bank	10.15%	10.38%
Minimum requirement for "Well-Capitalized" institution	10.00%	10.00%
Minimum regulatory requirement	8.00%	8.00%

Contractual Obligations and Off-Balance Sheet Arrangements

The following table presents our contractual cash obligations, excluding deposits, as of December 31, 2004:

Contractual Obligations[1]	Amount of Commitment Expiring Per Period				
	Total Amounts Committed	Less Than 1 Year	1-3 Years	3-5 Years	After 5 Years
	(In thousands)				
FHLB Advances	$15,000	$10,000	$ —	$5,000	$ —
Operating Lease Obligations	6,346	1,569	2,346	1,187	1,243
Total	$21,346	$11,569	$2,346	$6,187	$1,243

(1) Contractual obligations do not include interest.

In the normal course of business, we enter into off-balance sheet arrangements consisting of commitments to fund commercial letters of credit and standby letters of credit. The following table presents these off-balance sheet arrangements at December 31, 2004:

Other Commitments	Amount of Commitment Expiring Per Period				
	Total Amounts Committed	Less Than 1 Year	1-3 Years	3-5 Years	After 5 Years
	(In thousands)				
Commercial letters of credit	$15,133	$15,133	$—	$—	$—
Standby letters of credit	5,031	4,951	80	—	—
Total	$20,164	$20,084	$ 80	$—	$—

Liquidity

Based on our existing business plan, we believe that our level of liquid assets is sufficient to meet our current and presently anticipated funding needs. During the balance of 2004, and for the near term, we intend to continue the reduction of our lower yielding liquid assets, such as federal funds sold, and increasing our loan portfolio and higher yielding investment securities.

We rely on deposits as the principal source of funds and, therefore, must be in a position to service depositors' needs as they arise. We attempt to maintain a loan-to-deposit ratio below approximately 90%. Our loan-to-deposit ratio was 75.7% at December 31, 2004 and 74.9% at December 31, 2003.

Borrowings from the Federal Home Loan Bank of San Francisco, or FHLBSF, is another source of funding for our loan and investment activities. We may lend up to 90% of our borrowings from the FHLBSF that are securitized by certain loans. At December 31, 2004, we could borrow up to $39.1 million with collateral of specifically identified loans and securities. We intend to explore the feasibility of utilizing the FHLBSF as a source of funding to a greater extent than we have in the past. In view of planned balance sheet growth and liquidity needs, we presently have further increased our borrowing line with the FHLBSF to $66.3 million. We also attempt to maintain a liquidity ratio (liquid assets, including cash and due from banks, federal funds sold and investment securities not pledged as collateral expressed as a percentage of total deposits) above approximately 18%. Our liquidity ratio was 28.6% at December 31, 2004 and 30.5% at December 31, 2003. Subject to prevailing market and other conditions, we will seek to reduce our liquidity ratio, which had increased during 2003, in response to the UAL Leveraged Lease and growth of our deposits, by increasing our loan portfolio consistent with our underwriting standards, and possibly funding a greater portion of our loans and certain investment securities with borrowings from the FHLBSF.

We believe that if the level of liquid assets (our primary liquidity) does not meet our liquidity needs, other available sources of liquid assets (our secondary liquidity), including the purchase of federal funds, sales of

securities under agreements to repurchase, sales of loans, discount window borrowings from the Federal Reserve Bank (where we maintain a borrowing line of $9.5 million) and the FHLBSF, could be employed to meet those current and presently anticipated funding needs.

In assessing our liquidity, we also take into account commitments to extend credit. The following table sets forth our other significant commitments at December 31, 2004:

	Amount of Commitment Expiring Per Period				
Other Commitments	Total Amounts Committed	Less Than 1 Year	1-3 Years	3-5 Years	After 5 Years
			(In thousands)		
Commitments to extend credit	$312,185	$233,652	$71,487	$2,555	$4,131
Standby letters of credit	5,031	4,951	80	—	—
Total	$317,216	$238,603	$71,927	$2,555	$4,131

Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss in a financial instrument arising from adverse changes in market prices and rates, foreign currency exchange rates, commodity prices and equity prices. Our market risk arises primarily from interest rate risk inherent in our lending and deposit taking activities. To that end, management actively monitors and manages our interest rate risk exposure. We do not have any market risk sensitive instruments entered into for trading purposes. We manage our interest rate sensitivity by matching the re-pricing opportunities on our earning assets to those on our funding liabilities. Management uses various asset/liability strategies to manage the re-pricing characteristics of our assets and liabilities designed to ensure that exposure to interest rate fluctuations is limited and within our guidelines of acceptable levels of risk-taking. Hedging strategies, including the terms and pricing of loans and deposits and managing the deployment of our securities, are used to reduce mismatches in interest rate re-pricing opportunities of portfolio assets and their funding sources.

Interest rate risk is addressed by our Asset Liability Management Committee, or the ALCO, which is comprised of the Chief Executive Officer, Chief Financial Officer and members of the board of directors. The ALCO monitors interest rate risk by analyzing the potential impact on the net portfolio of equity value and net interest income from potential changes in interest rates, and considers the impact of alternative strategies or changes in balance sheet structure. The ALCO manages our balance sheet in part to maintain the potential impact on net portfolio value and net interest income within acceptable ranges despite rate changes in interest rates.

Our exposure to interest rate risk is monitored continuously by senior management and is reviewed by the ALCO at least eight times a year, and at least quarterly by our board of directors. Interest rate risk exposure is measured using interest rate sensitivity analysis to determine our change in net portfolio value and net interest income in the event of hypothetical changes in interest rates. If potential changes to net portfolio value and net interest income resulting from our analysis of hypothetical interest rate changes are not within board-approved limits, the board may direct management to adjust the asset and liability mix to bring interest rate risk within board-approved limits. This analysis of hypothetical interest rate changes is performed on a monthly basis by a third party vender utilizing detailed data that we provide to them.

Market Value of Portfolio Equity

We measure the impact of market interest rate changes on the net present value of estimated cash flows from our assets, liabilities and off-balance sheet items, defined as market value of portfolio equity, using a simulation model. This simulation model assesses the changes in the market value of interest rate sensitive financial instruments that would occur in response to an instantaneous and sustained increase or decrease in market interest rates.

The following table presents forecasted changes in net portfolio value using a base market rate and the estimated change to the base scenario given an immediate and sustained upward and downward movement in interest rates of 100 and 200 basis points at December 31, 2004.

Market Value of Portfolio Equity

Interest Rate Scenario	Market Value	Percentage Change from Base	Percentage of Total Assets	Percentage of Portfolio Equity Book Value
	(Dollars in thousands)			
Up 200 basis points	$95,313	6.34%	10.51%	124.09%
Up 100 basis points	92,307	2.98	10.17	120.18
BASE	89,634	—	9.88	116.70
Down 100 basis points	84,896	(5.29)	9.36	110.53
Down 200 basis points	77,295	(13.77)	8.52	100.63

The computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, asset prepayments and deposit decay, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions we may undertake in response to changes in interest rates. Actual amounts may differ from the projections set forth above should market conditions vary from the underlying assumptions.

Net Interest Income

In order to measure interest rate risk at December 31, 2004, we used a simulation model to project changes in net interest income that result from forecasted changes in interest rates. This analysis calculates the difference between net interest income forecasted using a rising and a falling interest rate scenario and a net interest income forecast using a base market interest rate derived from the current treasury yield curve. The income simulation model includes various assumptions regarding the re-pricing relationships for each of our products. Many of our assets are floating rate loans, which are assumed to re-price immediately, and to the same extent as the change in market rates according to their contracted index. Some loans and investment vehicles include the opportunity of prepayment (embedded options), and accordingly the simulation model uses national indexes to estimate these prepayments and reinvest their proceeds at current yields. Our non-term deposit products re-price more slowly, usually changing less than the change in market rates and at our discretion.

This analysis indicates the impact of changes in net interest income for the given set of rate changes and assumptions. It assumes no growth in the balance sheet and that its structure will remain similar to the structure at year end. It does not account for all factors that impact this analysis, including changes by management to mitigate the impact of interest rate changes or secondary impacts such as changes to our credit risk profile as interest rates change. Furthermore, loan prepayment rate estimates and spread relationships change regularly. Interest rate changes create changes in actual loan prepayment rates that will differ from the market estimates incorporated in this analysis. Changes that vary significantly from the assumptions may have significant effects on our net interest income.

For the rising and falling interest rate scenarios, the base market interest rate forecast was increased or decreased on an instantaneous and sustained basis.

Sensitivity of Net Interest Income December 31, 2004

Interest Rate Scenario	Adjusted Net Interest Income	Percentage Change from Base	Net Interest Margin Percent	Net Interest Margin Change (in basis points)
	(Dollars in thousands)			
Up 200 basis points	$42,036	21.45%	4.94%	88
Up 100 basis points	38,223	10.44	4.49	43
BASE	34,611	—	4.06	—
Down 100 basis points	34,007	(1.75)	3.99	(7)
Down 200 basis points	32,727	(5.44)	3.84	(22)

At December 31, 2004, we had $723.3 million in assets and $630.1 million in liabilities re-pricing within one year. This means that $93.2 million more of our interest rate sensitive assets than our interest rate sensitive liabilities will change to the then current rate (changes occur due to the instruments being at a variable rate or because the maturity of the instrument requires its replacement at the then current rate). The ratio of interest-earning assets to interest-bearing liabilities maturing or re-pricing within one year at December 31, 2004 is 114.8%. In theory, this analysis indicates that at December 31, 2004, if interest rates were to increase, the gap would tend to result in a higher net interest margin. However, changes in the mix of earning assets or supporting liabilities can either increase or decrease the net interest margin without affecting interest rate sensitivity. In addition, the interest rate spread between an asset and its supporting liability can vary significantly while the timing of re-pricing of both the asset and its supporting liability can remain the same, thus impacting net interest income. This characteristic is referred to as basis risk, and generally relates to the re-pricing characteristics of short-term funding sources such as certificates of deposit.

Gap Analysis

Another way to measure the impact that future changes in interest rates will have on net interest income is through a cumulative gap measure. The gap represents the net position of assets and liabilities subject to re-pricing in specified time periods.

The following table sets forth the distribution of re-pricing opportunities of our interest-earning assets and interest-bearing liabilities, the interest rate sensitivity gap (that is, interest rate sensitive assets less interest rate sensitive liabilities), cumulative interest-earning assets and interest-bearing liabilities, the cumulative interest rate sensitivity gap, the ratio of cumulative interest-earning assets to cumulative interest-bearing liabilities and the cumulative gap as a percentage of total assets and total interest-earning assets as of December 31, 2004 and 2003. The table also sets forth the time periods during which interest-earning assets and interest-bearing liabilities will mature or may re-price in accordance with their contractual terms. The interest rate relationships between the re-priceable assets and re-priceable liabilities are not necessarily constant and may be affected by many factors, including the behavior of customers in response to changes in interest rates. This table should, therefore, be used only as a guide as to the possible effect of changes in interest rates might have on our net interest margins.

	at December 31, 2004 Amounts Maturing or Re-pricing in					
	3 Months or Less	3 to 12 Months	1 to 5 Years	Noninterest Sensitive	Noninterest Sensitive[1]	Total
	(Dollars in thousands)					
ASSETS						
Cash and due from banks	$ —	$ —	$ —	$ —	$ 35,212	$ 35,212
Federal funds sold and securities purchased under resale agreements	73,000	—	—	—	—	73,000
Investment securities available-for-sale	11,181	42,579	62,142	43,381	—	159,283
Loans and leases—floating rate	557,270	32,291	—	—	—	589,561
Loans and leases—fixed rate	1,812	807	831	13,844	—	17,294
Certificates of deposit with other financial institutions and other earning assets	—	4,402	950	—	2,609	7,961
Other assets[2]	—	—	—	—	24,959	24,959
Total assets	$643,263	$ 80,079	$ 63,923	$ 57,225	$ 62,780	$907,270
LIABILITIES AND SHAREHOLDERS' EQUITY						
Noninterest-bearing demand deposits	$ —	$ —	$ —	$ —	$ 180,849	$180,849
Interest-bearing demand deposits, money market and savings	171,974	—	—	—	—	171,974
Time certificates of deposit	279,662	168,463	587	—	—	448,712
Long-term debt	5,000	5,000	5,000	—	—	15,000
Other liabilities	—	—	—	—	13,927	13,927
Shareholders' equity	—	—	—	—	76,808	76,808
Total liabilities and shareholders' equity	$456,636	$173,463	$ 5,587	$ —	$ 271,584	$907,270
GAP	$186,627	$ (93,384)	$ 58,336	$ 57,225	$(208,804)	
Cumulative interest-earning assets	643,263	723,342	787,265	844,490		
Cumulative interest-bearing liabilities	456,636	630,999	695,686	635,686		
Cumulative gap	186,627	93,243	151,579	208,804		
Cumulative interest-earning assets to cumulative interest-bearing liabilities	140.87%	114.80%	123.84%	132.85%		
Cumulative GAP as % of:						
Total assets	20.57%	10.28%	16.71%	23.01%		
Interest-earning assets	22.03%	11.01%	17.89%	24.65%		

(1) Assets or liabilities and equity which are not interest rate-sensitive.

(2) Allowance for loan and lease losses of $6.7 million as of December 31, 2004 is included in other assets.

	At December 31, 2003 Amounts Maturing or Re-pricing in					
	3 Months or Less	3 to 12 Months	1 to 5 Years	More than 5 Years	Noninterest Sensitive[(1)]	Total
	(Dollars in thousands)					
ASSETS						
Cash and due from banks	$ —	$ —	$ —	$ —	$ 22,909	$ 22,909
Federal funds sold and securities purchased under resale agreements	59,000	—	—	—	—	59,000
Investment securities available-for-sale	15,168	19,314	72,672	41,262	—	148,416
Loans and leases—floating rate	446,241	22,083	—	—	—	468,324
Loans and leases—fixed rate	2,158	7,389	4,513	14,106	—	28,166
Certificates of deposit with other financial institutions and other earning assets	—	7,454	—	—	1,243	8,697
Other assets[(2)]					26,313	26,313
Total assets	$522,567	$ 56,240	$ 77,185	$ 55,368	$ 50,465	$761,825
LIABILITIES AND SHAREHOLDERS' EQUITY						
Noninterest-bearing demand deposits	$ —	$ —	$ —	$ —	$ 135,261	$135,261
Interest-bearing demand deposits, money market and savings	156,332	—	—	—	—	156,332
Time certificates of deposit	202,408	167,955	856	—	—	371,219
Long-term debt	—	5,000	10,000	—	—	15,000
Other liabilities	—	—	—	—	16,277	16,277
Shareholders' equity	—	—	—	—	67,736	67,736
Total liabilities and shareholders' equity	$358,740	$ 172,955	$ 10,856	$ —	$ 219,274	$761,825
GAP	$163,827	$(116,715)	$ 66,329	$ 55,368	$(168,809)	
Cumulative interest-earning assets	522,567	578,807	655,992	711,360		
Cumulative interest-bearing liabilities	358,740	531,695	542,551	542,551		
Cumulative gap	163,827	47,112	113,441	168,809		
Cumulative interest-earning assets to cumulative interest-bearing liabilities	145.67%	108.86%	120.91%	131.11%		
Cumulative GAP as a percent of:						
Total assets	21.50%	6.18%	14.89%	22.16%		
Interest-earning assets	31.35%	9.02%	21.71%	32.30%		

(1) Assets or liabilities and equity which are not interest-rate sensitive.

(2) Allowance for loan and lease losses of $6.2 million as of December 31, 2003 is included in other assets.

Gap analysis has certain limitations. Measuring the volume of re-pricing or maturing assets and liabilities does not always measure the full impact on the portfolio value of equity or net interest income. Gap analysis does not account for rate caps on products, dynamic changes such as increasing prepayment speeds as interest rates decrease, basis risk, embedded options or the benefit of no-rate funding sources. The relation between product rate re-pricing and market rate changes (basis risk) is not the same for all products. The majority of interest-earning assets generally re-price along with a movement in market rates, while non-term deposit rates in general move more slowly and usually incorporate only a fraction of the change in market rates. Products categorized as non-rate sensitive, such as our noninterest-bearing demand deposits, in the gap analysis behave like long term

fixed rate funding sources. These factors tend to make our actual behavior more asset sensitive than is indicated in the gap analysis. We have experienced higher net interest income when rates rise, and lower net interest income when rates fall. Therefore, we use income simulation, net interest income rate shocks and market value of portfolio equity as our primary interest rate risk management tools.

The market value of portfolio equity and net interest income analyses under various interest rate shock scenarios described above indicate that we were asset sensitive at December 31, 2004. As a result, we believe that our balance sheet should generally be positively impacted by a rising interest rate environment.

Recent Accounting Pronouncements

In May 2003, the Financial Accounting Standards Board, or FASB, issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*. This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). This statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003, except for mandatorily redeemable financial instruments of nonpublic entities. For mandatorily redeemable financial instruments of a nonpublic entity, this statement shall be effective for existing or new contracts for fiscal periods beginning after December 15, 2004. In management's opinion, adoption of this statement did not have a material effect on our financial position, results of operations or cash flows. We currently do not have any financial instruments that are within the scope of SFAS No. 150.

In December 2003, the FASB revised FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46). This interpretation of Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, addresses consolidation by business enterprises of variable interest entities that possess certain characteristics. FIN 46 requires that if a business enterprise has a controlling financial interest in a variable interest entity, the assets, liabilities and results of the activities of the variable interest entity must be included in the consolidated financial statements with those of the business enterprise. In management's opinion, the application of this statement is not expected to have a material effect on our financial condition, results of operations or cash flows.

In December 2003, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued Statement of Position 03-03, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*, or SOP 03-03. This SOP addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities (loans) acquired in a transfer if those differences are attributable, at least in part, to credit quality. It includes such loans acquired in purchase business combinations and applies to all nongovernmental entities, including not-for-profit organizations. This SOP does not apply to loans originated by the entity. This SOP limits the yield that may be accreted (accretable yield) to the excess of the investor's estimate of undiscounted expected principal, interest, and other cash flows (cash flows expected at acquisition to be collected) over the investor's initial investment in the loan. This SOP requires that the excess of contractual cash flows over cash flows expected to be collected (nonaccretable difference) not be recognized as an adjustment of yield, loss accrual or valuation allowance. This SOP prohibits investors from displaying accretable yield and nonaccretable difference in the balance sheet. 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 impairment. This SOP prohibits "carrying over" or creation of valuation allowances in the initial accounting of all loans acquired in a transfer that are within the scope of this SOP. The prohibition of the valuation allowance carryover applies to the purchase of an individual loan, a pool of loans, a group of loans and loans acquired in a purchase business combination. This SOP is effective for loans acquired in fiscal years beginning after December 15, 2004. In management's opinion, the application of this statement is not expected to have a material effect on our financial condition, results of operations and cash flows.

On March 9, 2004, the SEC issued Staff Accounting Bulletin No. 105, *Application of Accounting Principles to Loan Commitments*, which provides guidance regarding loan commitments on loans to be classified as held-for-sale that are accounted for as derivative instruments. In this Bulletin, the SEC determined that an interest rate lock commitment should generally be valued at zero at inception. The rate locks will continue to be adjusted for changes in value resulting from changes in market interest rates. We adopted this new standard prospectively as of April 1, 2004 and it did not have a material impact on our financial statements.

In March 2004, the Emerging Issue Task Force reached a consensus opinion on Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments*, regarding the determination of whether an investment is considered impaired, whether the identified impairment is considered other-than-temporary, how to measure other-than-temporary impairment and how to disclose unrealized losses on investments that are not other-than-temporarily impaired. Adoption of the new measurement requirements has been delayed by the FASB pending reconsideration of implementation guidance relating to debt securities that are impaired solely due to market interest rate fluctuations. Our contractual cashflows of our mortgage-backed securities are guaranteed by Fannie Mae, Freddie Mac or Ginnie Mae. Because a decline in fair value is attributable to changes in interest rates and not credit quality, and because we have the ability and intent to hold these investments until a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

In December 2004, the FASB issued SFAS No. 123 (Revised 2004) (SFAS 123 (R)), *Share-Based Payment.* SFAS 123 (R) addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise or (b) liabilities that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. SFAS 123 (R) requires an entity to recognize the grant-date fair-value of stock options and other equity-based compensation issued to employees in the income statement. SFAS 123 (R) generally requires that an entity account for those transactions using the fair-value-based method and eliminates an entity's ability to account for share-based compensation transactions using the intrinsic value method of accounting in APB Opinion No. 25, *Accounting for Stock Issued to Employees*, which was permitted under Statement 123, as originally issued. Statement 123 (R) is effective for public companies that do not file as small business issuers as of the beginning of the first interim or annual reporting period that begins after June 15, 2005 (i.e. third-quarter 2005 for calendar year-end companies). Nonpublic companies are required to adopt the new statement for annual periods beginning after December 15, 2005. All public companies, including small business issuers, and those nonpublic entities that adopted the fair-value-based method of accounting, rather than the minimum-value method, must use either the modified prospective or the modified retrospective transition method. The impact on adoption of this statement in 2005 has not been determined.

Inflation

The majority of our assets and liabilities are monetary items held by us, the dollar value of which is not affected by inflation. Only a small portion of total assets is in premises and equipment. The lower inflation rate of recent years has not had the positive impact on us that was felt in many other industries. Our small fixed asset investment minimizes any material misstatement of asset values and depreciation expenses that may result from fluctuating market values due to inflation. Higher inflation rates may increase operating expenses or have other adverse effects on borrowers of the banks, making collection on extensions of credit more difficult for us. Rates of interest paid or charged generally rise if the marketplace believes inflation rates will increase.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES OF MARKET RISKS

For quantitative and qualitative disclosures regarding market risks in our portfolio, see, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Quantitative and Qualitative Disclosure About Market Risk."

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements of the Bank, including the "Report of Independent Registered Public Accounting Firm," are included in this report immediately following Part IV.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer along with our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15(e). Based upon that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective. There have been no significant changes in our internal controls during the period covered by this report that has materially affected or is reasonably likely to materially affect our internal controls over financial reporting.

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

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information concerning directors and executive officers of the Bank, to the extent not included under "Item 1 under the heading "*Executive Officers of the Bank*" appearing at the end of Part I of this report, will appear in the Bank's definitive proxy statement for the 2005 Annual Meeting of Shareholders (the "2005 Proxy Statement"), and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "ELECTION OF DIRECTORS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 11. EXECUTIVE COMPENSATION

Information concerning executive compensation will appear in the 2005 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "ELECTION OF DIRECTORS" and "EXECUTIVE OFFICER COMPENSATION," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information concerning security ownership of certain beneficial owners and management and information related to the Bank's equity compensation plans will appear in the 2005 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "BENEFICIAL SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT" and "SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information concerning certain relationships and related transactions will appear in the 2005 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year, or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information concerning principal accountant fees and services will appear in the 2005 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "RATIFY SELECTION OF INDEPENDENT PUBLIC ACCOUNTANTS FOR 2005," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

	Page
Preferred Bank:	
Report of Independent Registered Public Accounting Firm	71
Statements of Financial Condition at December 31, 2004 and 2003	72
Statements of Income and Comprehensive Income for the Years Ended December 31, 2004, 2003 and 2002	73
Statements of Changes in Stockholders' Equity for the Years Ended December 31, 2004, 2003 and 2002	74
Statements of Cash Flows for the Years Ended December 31, 2004, 2003 and 2002	75
Notes to Financial Statements for the Years Ended December 31, 2004, 2003 and 2002	76

(a)(2) Financial statement schedules

Schedules have been omitted because they are not applicable, not material or because the information is included in the consolidated financial statements or the notes thereto.

(a)(3) Exhibits

Exhibit No.	Exhibit Description
3.1	Amended and Restated Articles of Incorporation(1)
3.2	Amended and Restated Bylaws(1)
4.1	Common Stock Certificate(2)
10.1	Lease relating to the Bank's principal executive office at 601 S. Figueroa Street, 20th Floor, Los Angeles, California with Mitsui Fudoson (U.S.A.), Inc.(1)
10.2	Agreement for Item-Processing Services with Fiserv Solutions, Inc., dated as of July 31, 2002(1)
10.3	Agreement for Data-Processing with Fiserv Solutions, Inc., dated as of May 1, 2003(1)
10.4	Maintenance and Service Agreement, dated August 1, 2003 with Exilcom, Inc. d/b/a Northstar Technologies(1)
10.5*	1992 Stock Option Plan(1)
10.6*	Management Incentive Bonus Plan(1)
10.7*	Deferred Compensation Plan(1)
10.8*	Stock Option Gain Deferred Compensation Plan(1)
10.9*	2004 Equity Incentive Plan(1)
10.10*	Form of Indemnification Agreement for directors and executive officers(1)
21.1	Subsidiaries of the Registrant
24.1	Power of Attorney
31.1	Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002

(1) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on January 18, 2005.

(2) Incorporated by reference from Registrant's Registration Statement on Form 10 Amendment No. 1 filed with the Federal Deposit Insurance Corporation on February 2, 2005.

* Denotes management contract or compensatory plan or arrangement.

Report of Independent Registered Public Accounting Firm

The Board of Directors of Preferred Bank:

We have audited the accompanying statements of financial condition of Preferred Bank (the Bank) as of December 31, 2004 and 2003 the related statements of income and comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2004. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Preferred Bank as of December 31, 2004 and 2003 the results of its operations and its cash flows for each of the year in the three-years period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

Los Angeles, California
March 30, 2005

PREFERRED BANK

Statements of Financial Condition
December 31, 2004 and 2003
(In thousands, except for shares)

	2004	2003
Assets		
Cash and due from banks	$ 35,212	22,960
Federal funds sold and securities purchased under resale agreements	73,000	59,000
Cash and cash equivalents	108,212	81,960
Securities available-for-sale, at fair value	164,635	155,869
Loans and leases	615,961	504,053
Less allowance for loan losses	(6,724)	(6,168)
Less unearned income	(2,382)	(1,395)
Net loans and leases	606,855	496,490
Other real estate owned	8,258	8,258
Bank premises and equipment, net	1,365	1,101
Customers' liability on acceptances	2,502	5,554
Bank-owned life insurance (BOLI)	7,388	7,131
Accrued interest receivable and other assets	8,055	5,462
Total assets	$907,270	761,825
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Demand	$180,849	135,261
Interest-bearing demand	138,972	135,760
Savings	33,771	21,439
Time certificates of $100,000 or more	368,661	284,967
Other time certificates	79,282	85,385
Total deposits	801,535	662,812
Acceptances outstanding	2,502	5,554
Federal Home Loan Bank (FHLB) borrowings	15,000	15,000
Accrued expenses and other liabilities	11,425	10,723
Total liabilities	830,462	694,089
Commitments and contingencies		
Stockholders' equity:		
Preferred stock. Authorized 5,000,000 shares; issued and outstanding 0 shares at December 31, 2004 and 2003	—	—
Common stock, no par value. Authorized 100,000,000 shares; issued and outstanding 5,554,182 and 5,454,982 shares at December 31, 2004 and 2003, respectively	32,138	31,009
Retained earnings	44,591	36,756
Accumulated other comprehensive income (loss):		
Unrealized gain (loss) on securities available-for-sale, net of tax	79	(29)
Total stockholders' equity	76,808	67,736
Total liabilities and stockholders' equity	$907,270	761,825

See accompanying notes to financial statements.

PREFERRED BANK

Statements of Income and Comprehensive Income
Years ended December 31, 2004, 2003 and 2002
(In thousands, except for shares and net income per share)

	2004	2003	2002
Interest income:			
Loans and leases, including fees	$ 32,048	28,301	26,910
Investment securities	5,490	4,802	5,180
Federal funds sold and securities purchased under resale agreements	1,105	1,273	1,812
Total interest income	38,643	34,376	33,902
Interest expense:			
Interest-bearing demand	817	550	528
Savings	76	85	148
Time certificates of $100,000 or more	4,985	5,701	7,107
Other time certificates	1,211	1,752	2,317
FHLB borrowings	357	607	409
Federal funds purchased and securities sold under repurchase agreements	1	1	209
Total interest expense	7,447	8,696	10,718
Net interest income	31,196	25,680	23,184
Provision for credit losses	1,550	2,100	10,146
Net interest income after provision for loan losses	29,646	23,580	13,038
Noninterest income:			
Fees and service charges on deposit accounts	2,393	2,419	2,252
International operating income	729	677	581
BOLI income	316	347	366
Net other real estate owned income	526	227	240
Gain on sale of securities available-for-sale	35	1,111	931
Other income	200	142	144
Total noninterest income	4,199	4,923	4,514
Noninterest expense:			
Salary and employee benefits	9,741	8,733	5,532
Net occupancy expense	1,826	1,745	1,626
Business development and promotion expense	250	270	229
Professional services	855	799	875
Office supplies and equipment expense	754	721	753
Other	1,913	1,506	1,246
Total noninterest expense	15,339	13,774	10,261
Income before provision for income taxes	18,506	14,729	7,291
Provision for income taxes	7,354	5,696	2,888
Net income	11,152	9,033	4,403
Other comprehensive income, before tax:			
Unrealized net gains on securities available-for-sale	186	257	456
Less reclassification adjustments for gains included in net income	(6)	(732)	(123)
Other comprehensive income (loss), before tax	180	(475)	333
Income taxes related to items of other comprehensive income (loss)	72	200	(141)
Other comprehensive income (loss), net of tax	108	(275)	192
Comprehensive income	$ 11,260	8,758	4,595
Net income per share:			
Basic	$ 2.02	1.66	0.82
Diluted	1.92	1.58	0.77
Weighted-average common shares outstanding:			
Basic	5,518,398	5,440,319	5,398,114
Diluted	5,809,234	5,730,379	5,724,186
Dividends per share	0.60	0.24	0.38

See accompanying notes to financial statements.

PREFERRED BANK

Statements of Changes in Stockholders' Equity
Years ended December 31, 2004, 2003 and 2002
(In thousands, except for shares and dividends declared per share)

	Common shares outstanding	Common stock	Retained earnings	Accumulated other comprehensive income (loss)	Total stockholders' equity
Balance at December 31, 2001	5,358,782	$30,387	26,681	54	57,122
Change in unrealized gain on securities available-for-sale, net of income taxes	—	—	—	192	192
Dividends declared $0.38 per share	—	—	(2,058)	—	(2,058)
Tax Benefit—Exercise of Stock Options					
Stock options exercised	56,500	259	—	—	259
Net income	—	—	4,403	—	4,403
Balance at December 31, 2002	5,415,282	30,646	29,026	246	59,918
Change in unrealized gain on securities available-for-sale, net of income taxes	—	—	—	(275)	(275)
Dividends declared $0.24 per share	—	—	(1,303)	—	(1,303)
Tax Benefit—Exercise of Stock Options		60			60
Stock options exercised	39,700	303	—	—	303
Net income	—	—	9,033	—	9,033
Balance at December 31, 2003	5,454,982	31,009	36,756	(29)	67,736
Change in unrealized gain on securities available-for-sale, net of income taxes	—	—	—	108	108
Dividends declared $0.60 per share	—	—	(3,317)	—	(3,317)
Tax Benefit—Exercise of Stock Options		206			206
Stock options exercised	99,200	923	—	—	923
Net income	—	—	11,152	—	11,152
Balance at December 31, 2004	5,554,182	$32,138	44,591	79	76,808

PREFERRED BANK

Statements of Cash Flows
Years ended December 31, 2004, 2003 and 2002
(In thousands)

	2004	2003	2002
Cash flows from operating activities:			
Net income	$ 11,152	9,033	4,403
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	1,550	2,100	10,146
Amortization of net deferred loan fees and loan purchase discount	(987)	(183)	(347)
Amortization of investment securities discounts and premiums, net	2,002	1,397	347
Gain on sale of securities available-for-sale	(36)	(1,111)	(931)
Depreciation and amortization	492	502	513
Gain on sale of other real estate owned	—	(299)	(376)
(Gain) loss on sale of fixed assets	—	—	(4)
Other than temporary impairment write down on investment	296	—	—
Provision for deferred taxes	(6,568)	(575)	(3,318)
Decrease in BOLI, accrued interest receivable and other assets	3,718	(1,332)	3,668
Increase in accrued expenses and other liabilities	632	2,977	3,482
Net cash provided by operating activities	12,251	12,509	17,583
Cash flows from investing activities:			
Purchase of securities available-for-sale	(96,189)	(176,808)	(137,138)
Proceeds from securities available-for-sale transactions:			
Matured and called	73,468	84,606	121,000
Sales	5,094	27,535	31,905
Principal collected and stock dividends, net	6,779	5,996	1,425
Proceeds from sale of other real estate owned	—	701	3,086
Net increase in loans	(110,928)	(60,836)	(89,555)
Purchase of bank premises and equipment	(756)	(98)	(267)
Net cash used in investing activities	(122,532)	(118,904)	(69,544)
Cash flows from financing activities:			
Net increase in deposits	138,722	47,944	38,543
Proceeds from FHLB borrowings	5,000	10,000	15,000
Repayments of FHLB borrowings	(5,000)	(15,000)	—
Net decrease in Federal funds purchased and securities sold under repurchase agreements	—	—	(11,000)
Issuance of common stock, net	1,129	363	259
Cash dividends	(3,318)	(1,303)	(2,058)
Net cash provided by financing activities	136,533	42,004	40,744
Net increase (decrease) in cash and cash equivalents	26,252	(64,391)	(11,217)
Cash and cash equivalents at beginning of year	81,960	146,351	157,568
Cash and cash equivalents at end of year	$ 108,212	81,960	146,351
Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Interest	$ 7,011	9,297	10,882
Income taxes	6,990	4,832	5,290
Supplemental disclosure of noncash transactions:			
Loans transferred to other real estate owned through foreclosure	—	472	10,103

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Preferred Bank (the Bank) is a full service commercial bank and is engaged primarily in commercial, real estate, and international lending to customers with businesses domiciled in the state of California. The accounting and reporting policies of the Bank are in accordance with accounting principles generally accepted in the United States of America and conform to general practices in the banking industry. The following is a summary of the Bank's significant accounting policies.

(a) Cash and Cash Equivalents

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

(b) Investment Securities

The Bank classifies its debt and equity securities in two categories: held-to-maturity or available-for-sale. Securities that could be sold in response to changes in interest rates, increased loan demand, liquidity needs, capital requirements, or other similar factors are classified as securities available-for-sale. These securities are carried at fair value. Unrealized holding gains or losses, net of the related tax effect, on available-for-sale securities are excluded from income and are reported as a separate component of stockholders' equity as other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. Securities classified as held-to-maturity are those that the Bank has the positive intent and ability to hold until maturity. These securities are carried at amortized cost, adjusted for the amortization or accretion of premiums or discounts. At December 31, 2004 and 2003, no security was held for trading or held-to-maturity purposes.

A decline in the fair value of any available-for-sale or held-to-maturity security below cost that is deemed to be other than temporary results in a reduction in carrying amount to fair value. The impairment is charged to income and a new cost basis for the security is established.

Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective-interest method. Dividend and interest income are recognized when earned.

(c) Loans and Credit Fees

Loans are carried at face value, less payments received, the allowance for loan and lease losses, and deferred loan fees. Loans receivable are stated at the principal amount outstanding. Interest income is recorded on an accrual basis in accordance with the terms of the loans.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days or more unless the loan is both well secured and in the process of collection. When loans are placed on nonaccrual status, all interest previously accrued, but not collected, is reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible.

Loan origination fees, offset by certain direct loan origination costs and commitment fees, are deferred and recognized in income as a yield adjustment using the straight-line method over the contractual life of the loan, which approximates the interest method. If a commitment expires unexercised, the commitment fee is recognized as income.

The Bank considers a loan to be impaired when it is "probable" that it will be unable to collect all amounts due (i.e., both principal and interest) according to the contractual terms of the loan agreement. The measurement of impairment may be based on (1) the present value of the expected future cash flows of the impaired loan discounted at the loan's original effective interest rate, (2) the observable market price of the impaired loan, or (3) the fair value of the collateral of a collateral-dependent loan. The amount by which the recorded investment of the loan exceeds the measure of the impaired loan is recognized by recording a valuation allowance with a corresponding charge to the provision for loan losses. The Bank stratifies its loan portfolio by size and treats smaller performing loans with an outstanding balance less than $750,000 as a homogenous portfolio. For loans in excess of $750,000, the Bank conducts a periodic review of each loan in order to measure impairment, if any. The Bank recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans.

(d) Allowance for Loan and Lease Losses

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

Management believes that the allowance for loan and lease losses is adequate. While management uses available information to recognize losses on loans and leases, future adjustments to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan and lease losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

(e) Other Real Estate Owned

Other real estate owned, consisting of real estate acquired through foreclosure or other proceedings, is initially stated at the lower of the carrying value of the loan or fair value of the property based on appraisal, less estimated selling cost. Any cost in excess of the fair value at the time of acquisition is accounted for as a loan charge-off and deducted from the allowance for loan and lease losses. A valuation allowance is established for any subsequent declines in value. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating income or expense, as appropriate.

(f) Bank Premises and Equipment

Bank premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation on furniture and equipment is computed on a straight-line method over the estimated useful lives of the assets, generally three to five years. Leasehold improvements are capitalized and amortized on the straight-line method over the estimated useful life of the improvement or the term of lease, whichever is shorter.

(g) Comprehensive Income

Comprehensive income consists of net income and net unrealized gains (losses) on securities available-for-sale and is presented in the statements of income and comprehensive income.

(h) Income Taxes

The Bank accounts for income taxes using the asset and liability method. The objective of the asset and liability method is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the tax basis of the Bank's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. A valuation allowance is established for deferred tax assets if based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The valuation allowance is sufficient to reduce the deferred tax assets to the amount that is more likely than not to be realized.

(i) Earnings per Share

Earnings per share (EPS) are computed on a basic and diluted basis. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shares in the earnings of the Bank.

(j) Stock Option Plan

The Bank applies the intrinsic-value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations including FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25*, issued in March 2000, to account for its fixed-plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123) and SFAS No. 148, *Accounting for Stock-based Compensation—Transition and Disclosure*, *an amendment of FASB Statement No. 123*, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Bank has elected to continue to apply the intrinsic-value-based method of accounting described above and has adopted only the disclosure requirements of SFAS No. 123, as amended. The following table illustrates the effect on net income if the fair-value-based method had been applied to all outstanding and unvested awards in each period:

	2004	2003	2002
	(In thousands)		
Net income, as reported	$11,152	9,033	4,403
Deduct total stock-based employee compensation expense determined under fair-value-based method for all rewards, net of tax	(72)	(139)	(178)
Pro forma net income	$11,080	8,894	4,225

	2004	2003	2002
Earnings per share:			
Basic—as reported	$ 2.02	1.66	0.82
Basic—pro forma	2.01	1.63	0.78
Diluted—as reported	1.92	1.58	0.77
Diluted—pro forma	1.91	1.55	0.74

During 2004, the Bank granted 132,000 options. The per share weighted average fair value of options granted during 2004 was $2.18 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, dividend rate of 2.00%, risk-free interest rate of 3.80%, and expected life of five years. During 2003, the Bank granted 104,000 options. The per share weighted average fair value of options granted during 2003 was $1.98 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, no expected dividends, risk-free interest rate of 2.65%, and expected life of five years. During 2002, the bank granted 35,000 options. The per share weighted average fair value of options granted during 2002 was $4.87 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, no expected dividends, risk-free interest rate of 4.30%, and expected life of five years.

(k) Statement of Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold, and securities purchased under resale agreements.

(l) Bank-Owned Life Insurance

Bank-owned life insurance policies (BOLI) are carried at their cash surrender value. Income from BOLI is recognized when earned.

(m) Use of Estimates

Management of the Bank has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from these estimates. The most significant estimate subject to change relates to the allowance for loan and lease losses.

(n) Reclassifications

Certain reclassifications have been made to the 2003 and 2002 amounts to conform to the 2004 presentation.

(o) Risk and Uncertainties

The Bank's operations are located and concentrated primarily in Southern California and are likely to remain so for the foreseeable future. At December 31, 2004, approximately 97% of the total dollar amount of the Bank's loans and commitments was related to collateral or borrowers located within California. The performance of these loans may be affected by changes in California's economic and business conditions. Deterioration in economic conditions could have a material adverse effect on the quality of the Bank's loan portfolio and the demand for its products and services. In addition, during periods of economic slowdown or a recession, the Bank may experience a decline in collateral values and an increase in delinquencies and defaults. A decline in collateral values and an increase in delinquencies and defaults increase the possibilities and severity of losses. California real estate is also subject to certain natural disasters, such as earthquakes, fires, floods and mud slides, as well as civil unrest, which are typically not covered by the standard hazard insurance policies maintained by the borrowers. Uninsured disasters may render borrowers

unable to repay loans made by the Bank and lower collateral values. The occurrence of adverse economic conditions or natural disasters in California could have a material adverse effect on the Bank's financial condition, results of operations, and business prospects.

(p) Segment Reporting

Through our branch network, we provide a broad range of financial services to individuals and companies located primarily in Southern California. There services include demand, time and savings deposits and real estate, business and consumer lending. While our chief decision makers monitor the revenue streams of our various products and services, operations are managed and financial performance in evaluated on a company-wide basis. Accordingly, we consider all of our operations are aggregated in one reportable operating segment.

(q) Recent Issued Accounting Standards

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123R (revised 2004), "Share-Based Payment". SFAS No. 123R addresses the accounting for share-based payment transactions in which of the company's equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using the intrinsic method that is currently used and requires that such transactions be accounted for using a fair value-based method and recognized as expense in the Consolidated Statement of Income. The effective date of SFAS No. 123R is for interim and annual periods beginning after June 15, 2005. The Bank has been providing pro forma disclosures under SFAS No. 123, which are included in "Note 1—Stock Option Plan."

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

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

In December 2004, the FASB issued SFAS No. 153, "Exchange of Non-Monetary Assets, an Amendment of APB Option No. 29, "Accounting for Non-Monetary Transactions". SFAS No. 153 is based on the principle that exchange of non-monetary assets should be measured based on the fair market value of the assets exchanged. SFAS No. 153 eliminates the exception of non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. SFAS No. 153 is effective for non-monetary asset exchanges in fiscal periods beginning after June 15, 2005 and is required to be adopted beginning on January 1, 2006. Adoption is not expected to have a material impact on our financial position or results of operations.

(2) Cash and Due from Banks

The Bank is required to maintain minimum reserve balances on deposit with the Federal Reserve Bank. Reserve requirements are based on a percentage of deposit liabilities. The average reserve balances required were $10,827,000 and $8,179,000 during 2004 and 2003, respectively.

(3) Securities Purchased under Resale Agreements

The Bank enters into purchases of overnight securities under agreements to resell identical securities. Securities purchased under resale agreements are collateralized by mortgage loans.

The amounts advanced under these agreements represent overnight loans and are reflected as securities purchased under resale agreements in the statements of financial condition. At December 31, 2004 and 2003, securities purchased under resale agreements matured within one business day and the amount outstanding was $0 and $49,000,000, respectively. Securities purchased under resale agreements averaged approximately $44,000,000 and $48,000,000 during 2004 and 2003, respectively. The maximum amount outstanding at any month-end during 2004 and 2003 was $53,000,000 and $49,000,000, respectively. The average rates for the years ended December 31, 2004 and 2003 were 1.45% and 1.25%, respectively. The securities underlying the agreements were maintained under the Bank's control.

(4) Securities Available-for-Sale

The amortized cost and estimated fair value of securities available-for-sale at December 31, 2004 and 2003 are summarized as follows:

	2004			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
U.S. Agency	$ 71,431	24	(428)	71,027
Corporate notes	52,820	1,154	(61)	53,913
Mortgage-backed securities	12,771	113	(171)	12,713
Other securities	27,482	17	(517)	26,982
Total securities available-for-sale	$164,504	1,308	(1,177)	164,635

	2003			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
U.S. Treasury	$ 1,004	12	—	1,016
U.S. Agency	36,230	100	(9)	36,321
Corporate notes	71,102	1,162	(47)	72,217
Mortgage-backed securities	17,680	105	(206)	17,579
Other securities	29,904	7	(1,175)	28,736
Total securities available- for-sale	$155,920	1,386	(1,437)	155,869

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

	Less than 12 months		12 months or greater		Total	
	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses
	(In thousands)					
U.S. Agency	$64,030	393	3,968	35	67,998	428
Corporate notes	22,233	40	3,104	21	25,337	61
Mortgage-backed securities	1,811	10	8,848	161	10,659	171
Other securities	—	—	18,828	517	18,828	517
	$88,074	443	34,748	734	122,822	1,177

The Bank's investment portfolio is primarily comprised of U.S. Agency securities, corporate notes, mortgage-backed securities, municipalities and Federal Home Loan Mortgage Corporation (FHLMC) preferred stock which are included in other securities. Approximately $2,600,000 (or less than 2% of the total investment portfolio) is invested in FHLMC preferred stock at December 31, 2004.

At December 31, 2004, there were 52 and 48 investment securities that were in an unrealized loss position for less than 12 months and for 12 months or greater, respectively. Temporary impairments related to U.S. Agency securities, corporate notes, mortgage-backed securities, and municipalities are primarily attributable to declining market prices caused by interest rate fluctuations. Unrealized losses on the FHLMC preferred stock are due mainly to lower interest rate environments.

Whenever the cost of an investment security exceeds its fair value, management evaluates, among other factors, general market conditions, the duration and extent to which cost is more than fair value, as well as specific adverse conditions affecting the business outlook of the issuer. At December 31, 2004, the Bank's FHLMC preferred stock has been in an unrealized loss position for more than 24 consecutive months and the Bank believes that the market price of the said investment might not improve based on the prevailing interest rate environment. Although the Bank has the ability and intent to hold this investment until a market price recovery, management considers this investment is other-than-temporarily impaired. Accordingly, the cost basis of the FHLMC preferred stock was written down by $296,000 to reflect its fair value as of December 31, 2004. With the exception of the aforementioned discussion, management believes that investment securities in an unrealized loss position were temporary in nature, and therefore, no impairment losses were recognized in the statements of income and comprehensive income.

The amortized cost and estimated fair value of securities at December 31, 2004 and 2003, by contractual maturity, are shown below. Mortgage-backed securities are classified in accordance with their estimated average life. The average yield on mortgage-backed securities was 2.89%, 3.34% and 6.05% in 2004, 2003 and 2002, respectively. Expected maturities differ from contractual maturities mainly due to prepayment rates; changes in prepayment rates will affect a security's average life.

	2004	
	Amortized cost	Estimated fair value
	(In thousands)	
Due in one year or less	$ 56,738	56,593
Due after one year through five years	53,366	53,294
Due after five years through ten years	6,471	6,665
Due after ten years	47,929	48,083
Total securities available-for-sale	$164,504	164,635

	2003	
	Amortized cost	Estimated fair value
	(In thousands)	
Due in one year or less	$ 40,886	40,931
Due after one year through five years	72,036	72,190
Due after five years through ten years	5,978	6,340
Due after ten years	37,020	36,408
Total securities available-for-sale	$155,920	155,869

Cash proceeds from sales of securities available-for-sale totaled $5,094,000 and $27,535,000 in 2004 and 2003, respectively. Gross realized gains and losses on sales of securities available-for-sale totaled $38,000 and $2,000, respectively, in 2004, $1,111,000 and $0, respectively, in 2003 and $931,000 and $0, respectively, in 2002, based on the specific-identification method. Investment securities having a fair value of approximately $61,426,000 and $62,270,000 were pledged to secure governmental deposits, treasury tax and loan deposits, borrowing line from the Federal Reserve Bank, and government deposits as of December 31, 2004 and 2003, respectively.

(5) Loans and Leases and Allowance for Loan and Lease Losses

The loan and leases portfolio as of December 31, 2004 and 2003 is summarized as follows:

	2004	2003
	(In thousands)	
Real estate	$358,221	250,993
Commercial	98,547	117,607
Construction	112,002	94,816
Trade Finance	45,951	37,829
Installment/consumer	222	348
Other loans	305	582
Leases:		
Aircraft	—	1,000
Other	713	878
	615,961	504,053
Less:		
Allowance for loan and lease losses	(6,724)	(6,168)
Unearned income	(2,382)	(1,395)
	$606,855	496,490

The majority of the Bank's loans are to customers with businesses domiciled in the state of California and/or secured by properties located in the greater Los Angeles metropolitan area. All loans are made based on the same credit standards regardless of where the customers and/or collateral properties are located.

Nonaccrual loans and leases amounted to approximately $382,000 and $1,000,000 at December 31, 2004 and 2003, respectively. These loans and leases had interest due, but not recognized, of approximately $11,000 and $132,000 in 2004 and 2003, respectively.

The Bank had approximately $382,000 and $1,000,000 of impaired loans and leases as of December 31, 2004 and 2003, respectively. As of December 31, 2004 and 2003, the amount of impaired loans and leases for which there is a specific allowance for loan and lease loss was $0 and $1,000,000, respectively, with the amount of the specific allowance for loan and lease loss of approximately $0, and $850,000, respectively. The average recorded investment in impaired loans and leases for 2004 and 2003 was $333,000 and $2,675,000, respectively. Interest income recognized on such loans and leases during 2004 and 2003 was $15,000 and $0, respectively.

At December 31, 2004, the Bank had no commitments to lend additional funds to debtors whose loans are nonperforming.

Changes in the allowance for loan and lease losses are summarized as follows:

	2004	2003	2002
	(In thousands)		
Balance at beginning of year	$ 6,168	9,257	4,906
Provision for loan and lease losses	1,550	2,100	10,146
Loans and leases charged off	(1,103)	(5,345)	(6,234)
Recoveries	109	156	439
Balance at end of year	$ 6,724	6,168	9,257

In November 1997, the Bank purchased a beneficial interest in a trust which owns a Boeing 737-500 aircraft with a then fair value of $24.4 million and a remaining estimated economic life of 30 years. The trust is the lessor under the lease, which lease term is through 2016. The Bank's equity investment was $6.6 million. The aircraft is subject to $17.8 million of third-party financing in the form of long-term debt that provides for no recourse against the Bank and is secured by a first lien on the aircraft.

For federal income tax purposes, the Bank has the benefit of tax deductions for depreciation on the entire leased asset and for interest paid on the long-term debt. Deferred taxes are provided to reflect the temporary differences between the book tax provisions and the taxes that are payable.

During 2002, the lessee airline, United Airlines, declared bankruptcy, and accordingly, the Bank downgraded the aircraft leveraged lease to doubtful classification. To provide sufficient allowance for loan losses to cover the estimated loss on the lease, cumulatively, the Bank has provided allowances of $9.2 million as of December 31, 2003. Of the said allowance, approximately $1,000,000, $5,232,000 and $3,084,000 was charged off in 2004, 2003 and 2002, respectively. The Aircraft leveraged lease was completely charged off as of December 31, 2004.

The Bank's investment in the aircraft leveraged lease is composed of the following elements at December 31:

	2004	2003
	(In thousands)	
Rental receivable (net of principal and interest on the nonrecouse debit)	$—	—
Direct cost	—	48
Estimated residual value of leased asset	—	6,853
Less unearned and deferred income	—	(5,901)
Investment in aircraft leveraged lease	$—	1,000

(6) Premises and Equipment

As of December 31, 2004 and 2003, premises and equipment consists of the following:

	2004	2003
	(In thousands)	
Leasehold improvements	$ 2,376	2,364
Furniture, fixtures, and equipment	3,144	2,468
	5,520	4,832
Less accumulated depreciation and amortization	(4,155)	(3,731)
	$ 1,365	1,101

Depreciation and amortization expense was $492,000, $502,000 and $513,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

(7) Deposits

Time deposit accounts at December 31, 2004 mature as follows:

	Maturities of time deposits
	(In thousands)
2005	$447,341
2006	402
2007	200
	$447,943

At December 31, 2004 and 2003, approximately $46,051,000 and $46,298,000, respectively, of the Bank's investment securities were pledged as collateral for certain public deposits. The amount of deposits from related parties was $6,207,000 and $7,798,000 at December 31, 2004 and 2003, respectively. The aggregate amount of overdrafts that have been reclassified as loan balances was $249,000 and $529,000 at December 31, 2004 and 2003, respectively.

Interest expense on deposits and borrowings for the years ended December 31, 2004, 2003 and 2002 is as of follow:

	2004	2003	2002
	(In thousands)		
Interest bearing demand	$ 817	550	528
Savings	76	85	148
Time certificates of $100,000 or more	4,985	5,701	7,107
Other time certificates	1,211	1,752	2,317
FHLB borrowings	357	607	409
Federal funds purchased and securities sold under repurchase agreements	1	1	209
	$7,447	8,696	10,718

(8) Income Taxes

The provision for income taxes for the years ended December 31, 2004, 2003 and 2002 was as follows:

	2004	2003	2002
	(In thousands)		
Current:			
Federal	$10,856	4,628	4,708
State	3,066	1,643	1,498
	13,922	6,271	6,206
Deferred:			
Federal	(5,426)	(413)	(2,480)
State	(1,142)	(162)	(838)
	(6,568)	(575)	(3,318)
	$ 7,354	5,696	2,888

At December 31, 2004 and 2003, other liabilities include current income taxes payable of approximately $6,513,000 and $1,866,000, respectively.

The components of the net deferred tax liabilities as of December 31, 2004 and 2003 are as follows:

	2004	2003
	(In thousands)	
Deferred tax assets:		
Loan losses	$2,827	2,609
State franchise tax	1,051	615
Accrued expenses, mainly due to accrued bonuses	1,184	574
Deferred compensation	1,397	1,163
Gain on sale of other real estate owned	—	189
Unrealized losses on securities available-for-sale	—	22
Other, net	242	26
Total deferred tax assets	6,701	5,198
Deferred tax liabilities:		
Discount accretion	(77)	(50)
Leveraged leases	(112)	(5,099)
FHLB stock dividends	—	(83)
Unrealized gains on securities available-for-sale	(52)	—
Total deferred tax liabilities	(241)	(5,232)
Net deferred tax assets(liabilities)	$6,460	(34)

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not the Bank will realize all benefits related to these deductible differences.

A reconciliation of the income tax provision and the amount computed by applying the statutory federal income tax rate to income before income taxes is as follows for the years ended December 31, 2004, 2003 and 2002 (in thousands):

	2004		2003		2002	
	Amount	Percentage	Amount	Percentage	Amount	Percentage
Statutory U.S. federal income tax	$6,477	35.0%	$5,155	35.0%	2,552	35.0%
State taxes, net of federal benefit	1,271	6.8	914	6.2	428	5.9
Life insurance policies	(90)	(0.5)	(101)	(0.7)	(128)	(1.8)
Other	(304)	(1.6)	(272)	(1.8)	36	0.5
	$7,354	505.0%	$5,696	38.7%	2,888	39.6%

(9) Federal Funds Purchased and Securities Sold under Repurchase Agreements

Federal funds purchased and securities sold under repurchase agreements are overnight transactions, which mature within one business day from the trade date.

U.S. Treasury securities and U.S. Agency securities sold under repurchase agreements were delivered to the broker-dealers who arranged the transactions. The broker-dealers may have sold, loaned, or otherwise disposed of such securities to other parties in the normal course of their operation and have agreed to resell to the Bank identical securities at the maturities of the agreements. There were no outstanding amounts of these overnight agreements as of December 31, 2004 and 2003. There were no securities underlying these agreements at December 31, 2004 and 2003. These overnight agreements averaged approximately $41,000 and $37,000 during 2004 and 2003, respectively. The maximum amount outstanding at any month-end during 2004 and 2003 was $0 and $0, respectively. The average rate for the years ended December 31, 2004, 2003 and 2002 was 2.11%, 1.54% and 1.55%, respectively.

At December 31, 2004, the Bank had federal fund lines of $25,000,000 at Wells Fargo Bank and $20,000,000 at Bank of America. The Bank had $0 outstanding at December 31, 2004 and 2003. At December 31, 2004 and 2003, the Bank also had additional short-term financing of $9,486,000 and $11,848,000, respectively, available through the discount window at the Federal Reserve Bank of San Francisco. The Bank had $0 outstanding at December 31, 2004 and 2003.

(10) FHLB Borrowings

FHLB borrowings at December 31, 2004 mature as follows:

	2004
	(In thousands)
2005	$10,000
2006	5,000
	$15,000

All borrowings are collateralized by investment securities or residential real estate loans. At December 31, 2004, approximately $118,908,000 of the Bank's real estate loans were pledged as collateral. The average rate on the fixed rate debt was 1.89% and 2.39% at December 31, 2004 and 2003, respectively.

(11) Commitments and Contingencies

The Bank is obligated under certain operating leases for the premises of its head office and regional offices. As of December 31, 2004, the future total minimum lease payments for the Bank's premises are as follows:

	Total lease payment
	(In thousands)
2005	$ 964
2006	769
2007	597
2008	490
2009	109
Thereafter	—
	$2,929

Rental expense was $1,036,000, $976,000 and $756,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

(12) Off-Balance-Sheet Risks

As a financial institution, the Bank enters into a variety of financial transactions with its customers in the normal course of business. Many of these products do not necessarily entail present or future funded asset or liability positions but are instead in the nature of executory contracts.

Financial instrument transactions are subject to the Bank's normal credit standards, financial controls and risk-limiting, and monitoring procedures. Collateral requirements are made on a case-by-case evaluation of each customer and product.

The Bank's exposure to credit risk under commitments to extend credit, standby letters of credit, and financial guarantees written is limited to the contractual amount of those instruments.

At December 31, 2004 and 2003, the Bank had commitments to fund loans of $286,599,000 and $173,397,000, respectively. Other financial instruments with off-balance-sheet risk at December 31, 2004 and 2003 are as follows:

	2004	2003
	(In thousands)	
Commercial letters of credit	$15,133	3,489
Standby letters of credit	5,031	5,572

The majority of loan commitments have terms up to one year and have variable rates of interest. Standby letters of credit have terms up to one year. Most standby letters of credit expire unused. The allowance for off-balance-sheet reserve was $200 and $102,000 at December 31, 2004 and 2003, respectively.

(13) Loans to Related Parties

The Bank has extended credit to certain directors and officers and companies in which they have an interest and certain stockholders which beneficially own more than 5% of the Bank's capital stock. In management's opinion, the loans to these related parties are made on substantially the same terms, including interest rates and collateral, as those made to nonrelated persons.

At December 31, 2004 and 2003, the aggregate loans (including commitments) to related parties were approximately $12,858,000 (of which $3,060,000 was outstanding) and $14,238,000 (of which $8,502,000 was outstanding), respectively. All loans were current at December 31, 2004 and 2003.

Changes in the outstanding loans are summarized as follows:

	2004	2003	2002
	(In thousands)		
Balance at beginning of year	$ 8,502	3,755	5,764
New loans	—	81	1,028
Net drawdowns (repayments)	(5,442)	4,666	(3,037)
Balance at end of year	$ 3,060	8,502	3,755

(14) Restrictions on Cash Dividends, Regulatory Capital Requirements

The Bank has authorized 5,000,000 shares of preferred stock. The Board has the authority to issue the preferred stock in one or more series, and to fix the designations, rights, preferences, privileges, qualifications, and restrictions, including dividend rights, conversion rights, voting rights and terms of redemptions, liquidation preferences, and sinking fund terms, any or all of which may be greater than the rights of the common stock.

Under Section 642 of the California Financial Code, funds available for cash dividend payments by a bank are restricted to the lesser of: (i) retained earnings or (ii) the bank's net income for its last three fiscal years (less any distributions to stockholders made during such period). Cash dividends may also be paid out of the greatest of: (i) retained earnings, (ii) net income for a bank's last preceding fiscal year, or (iii) net income of the Bank for its current fiscal year upon the prior approval of the Commissioner of Financial Institutions, State of California, without regard to retained earnings or net income for its prior three fiscal years.

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

The quantitative measures established by the regulation to ensure capital adequacy require the Bank to maintain amounts and ratios (set forth in the table below) of total and Tier 1 risk-based capital (as defined in the regulation) to risk-weighted assets (as defined) and of Tier 1 risk-based capital (as defined) to average assets (as defined). Management believes, as of December 31, 2004, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2004, the most recent notification from the FDIC categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes changed the institution's category.

The Bank's actual and required capital amounts and ratios are presented in the following table:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provision	
	Amount	Percent	Amount	Percent	Amount	Percent
			(In thousands)			
As of December 31, 2004:						
Total risk-based capital	$83,398	10.15%	$65,733	≥ 8.00%	$82,166	≥ 10.00%
Tier I risk-based capital	76,674	9.33	32,872	4.00	49,308	6.00
Leverage ratio	76,674	9.30	32,978	4.00	41,223	5.00
As of December 31, 2003:						
Total risk-based capital	$73,909	10.38%	$56,963	≥ 8.00%	$71,203	≥ 10.00%
Tier I risk-based capital	67,741	9.52	28,463	4.00	42,694	6.00
Leverage ratio	67,741	8.74	31,003	4.00	38,783	5.00

(15) Stock Option Plans

The 1992 Stock Option Plan provides granting of nonstatutory stock options and incentive stock options to key full-time employees, officers, and the directors of the Bank. The total shares authorized in this plan are 1,447,920 shares. The 1992 Stock Option Plan expired by its terms in April 2003, and no shares are available for future grants. The options vest 20% each year and become fully vested after five years. Options expire ten years after the grant date. The exercise price cannot be less than 100% of the fair value of the shares on the date of grant. As of December 31, 2004 and 2003, the exercise prices ranged from $4.55 to $25.40.

The Interim Stock Option Plan provides granting of nonstatutory stock options and incentive stock options to key full-time employees, officers, and the directors of the Bank. Even though the terms of these stock options are consistent with the terms of the stock options granted under the 1992 plan, these stock options are outside of the 1992 plan because they were granted after the 1992 plan's expiration. No shares are available for future grants. As of December 31, 2004 and 2003, the exercise prices ranged from $16.04 and $28.51.

The 2004 Equity Incentive Plan provides granting of nonqualified stock options, incentive stock options, stock appreciation rights (SRAs), performance shares, performance units, deferred stock units and restricted stock to key full-time employees, officers, and the directors of the Bank. The total shares authorized in this plan are 1,200,000 shares. Options vest 20% each year and become fully vested after five years. Options expire 10 years after the grant date. In the event of a change in control, all awards granted under the 2004 plan will vest and become exercisable immediately, unless the awards are assumed or substituted by the successor corporation. As of December 31, 2004, there were no outstanding options under the 2004 plan.

During 2004, the Bank granted 132,000 options. The per share weighted average fair value of options granted during 2004 was $2.18 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, dividend rate of 2.00%, risk-free interest rate of 3.80%, and expected life of five years. During 2003, the Bank granted 104,000 options. The per share weighted average fair value of options granted during 2003 was $1.98 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, no expected dividends, risk-free interest rate of 2.65%, and expected life of five years. During 2002, the bank granted 35,000 options. The per share weighted average fair value of options granted during 2002 was $4.87 on the date of the grant using the Black-Scholes option-pricing model with the following assumptions: volatility of 0%, no expected dividends, risk-free interest rate of 4.30%, and expected life of five years.

The weighted average exercise price for the outstanding options was $16.12 and $12.18 per share, respectively, and the weighted average remaining contractual life for the options outstanding was approximately 5.42 years and 4.98, respectively, at December 31, 2004 and 2003. A summary of option activity follows:

	Number of options	Weighted average option price
Outstanding at December 31, 2002	531,600	$11.17
Options granted	104,000	16.04
Options exercised	(39,700)	7.62
Options canceled	(14,600)	15.32
Outstanding at December 31, 2003	581,300	12.18
Options granted	132,000	28.51
Options exercised	(99,200)	9.30
Options canceled	(11,500)	17.91
Outstanding at December 31, 2004	602,600	16.12

As of December 31, 2004 and 2003, 375,700 and 436,800 options were exercisable, respectively. The weighted average exercise prices of exercisable options were $11.46 and $10.56 and December 31, 2004 and 2003, respectively.

(16) Employee Benefit Plan

Effective January 1, 1994, the Bank began a 401(k) profit sharing plan for its eligible employees. Under the plan, the Bank matches 50% of a participant's contributions up to 6% of his/her salary. Contributions made by the Bank for the years ended December 31, 2004, and 2003 totaled $106,000 and $97,000, respectively.

(17) Bonus Plan

In April 1994, the Management Incentive Bonus Plan was approved. The plan is administered by the Compensation Committee of the board of directors (the Committee). The Committee determines which employees may participate in the plan. All awards are contingent upon the Bank attaining certain financial objectives. Total expense of the plan recorded by the Bank was approximately $4,626,000, $3,475,000 and $1,218,000 for 2004, 2003 and 2002, respectively. As of December 31, 2004, the total bonus accrual included in the other liabilities amounted to $5,996,000. The amounts accrued are generally paid out over a three-year period subsequent to the year the bonus was granted. There is no vesting requirement to receive the bonus; however, employees must be employed with the Bank at the time the bonus is distributed.

(18) Deferred Compensation Arrangements

In 1996, the Bank implemented deferred compensation arrangements for the Bank's executive officers and directors. Pursuant to the Plan, each participant receives benefits for his/her deferred compensation upon his/her retirement or termination of service with the Bank prior to retirement. At December 31, 2004 and 2003, liabilities recorded for the estimated present value of deferred compensation totaled approximately $3,324,000 and $2,765,000, respectively.

In order to fund its obligation under the deferred compensation arrangements, the Bank purchased a single-premium life insurance policy under which the executive officers and directors are the insureds, while the Bank is the owner and beneficiary thereof. At December 31, 2004 and 2003, the cash surrender value of the policy totaled $7,388,000 and $7,131,000, respectively. During 2004, 2003 and 2002, the income on the insurance policy was $316,000, $347,000 and $366,000, respectively.

(19) Litigation

From time to time, the Bank is a party to claims and legal proceedings arising in the ordinary course of business. There are no pending legal proceedings or, to the best of management's knowledge, threatened legal proceedings, to which the Bank is a party which may have a material adverse effect upon the Bank's financial condition, results of operations, or business prospects.

(20) Fair Value of Financial Instruments

SFAS No. 107, *Disclosures about Fair Value of Financial Instruments* (SFAS No. 107), requires that an entity disclose the fair value of all financial instruments, as defined, regardless of whether recognized in the financial statements of the reporting entity. For purposes of determining fair value, SFAS No. 107 provides that the fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

(a) Cash Due from Banks, Federal Funds Sold and Securities Purchased under Resale Agreements

For cash and short-term instruments whose maturity is less than 90 days, the carrying amount was assumed to be a reasonable estimate of fair value.

(b) Securities available-for-sale

For securities available-for-sale, fair values were based on quoted market prices obtained from dealer quotes. If a quoted market price was not available, fair value was estimated using quoted market prices for similar securities.

(c) Loans

Fair values were estimated for portfolios of loans with similar financial characteristics. Each loan category was further segmented into fixed and adjustable rate interest terms and by performing and nonperforming categories.

The fair value of performing loans was calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan.

Fair value for nonperforming real estate loans was based on recent external appraisals of the underlying collateral of the loan. If appraisals were not available, estimated cash flows were discounted using a rate commensurate with the risk associated with the estimated cash flows. Assumptions regarding credit risk,

cash flows, and discount rates were judgmentally determined using available market information and specific borrower information.

(d) Accrued Interest Receivable and Accrued Interest Payable

The carrying amount of accrued interest receivable and accrued interest payable approximate its fair value due to their short-term nature.

(e) Deposits

The fair value of demand deposits, saving accounts, and certain money market deposits was assumed to be the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit was estimated using the rates currently offered for deposits with similar remaining maturities.

(f) FHLB Borrowings

The fair value of FHLB borrowings was based on rates currently offered for borrowings with similar remaining maturities.

(g) Commitment to Extend Credit and Letters of Credit

The fair value of commitments was estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. The fair value of letters of credit was based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

	December 31, 2004		December 31, 2003	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
	(In thousands)			
Assets:				
Cash and cash equivalents	$108,212	108,212	81,960	81,960
Securities available-for-sale	164,635	164,635	155,869	155,869
Loans, net of allowance and unearned income	606,855	606,582	496,490	496,455
Accrued interest receivable	2,481	2,481	1,950	1,950
Liabilities:				
Demand deposits and savings:				
Non-interest bearing	$180,849	180,849	135,261	135,261
Interest-bearing	173,743	172,743	157,199	157,199
Time deposits	447,943	448,412	370,352	370,826
FHLB borrowings	15,000	14,804	15,000	14,839
Accrued interest payable	1,292	1,292	855	855
Commitments to extend credit and letters of credit	—	2,206	—	1,529

The fair value estimates do not reflect any premium or discount that could result from offering the instruments for sale. Potential taxes and other expenses that would be incurred in an actual sale or settlement are

not reflected in amounts disclosed. The fair value estimates are dependent upon subjective estimates of market conditions and perceived risks of financial instruments at a point in time and involve significant uncertainties resulting in variability in estimates with changes in assumptions.

(21) Subsequent Events

On February 17, 2005, we completed our initial public offering ("IPO") of 985,622 shares of our common stock at $38.00 per share, excluding 1,452,378 shares sold by certain selling shareholders. The net proceeds to the bank from our IPO of common stock was $34.6 million, after deducting underwriting discounts and offering expenses.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 30, 2005

PREFERRED BANK
(Registrant)

By /s/ LI YU

Li Yu
Chairman of the Board, President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

Signature	Title	Date
/s/ LI YU **Li Yu**	Chairman of the Board, President, Chairman and Chief Executive Officer (principal executive officer)	March 30, 2005
/s/ CHRIS CHAN **Chris Chan**	Senior Vice President and Chief Financial Officer (principal financial and accounting officer)	March 30, 2005
/s/ CHIH-WEI WU **Chih-Wei Wu**	Director	March 30, 2005
/s/ J. RICHARD BELLISTON **J. Richard Belliston**	Director	March 30, 2005
/s/ GARY S. NUNNELLY **Gary S. Nunnelly**	Director	March 30, 2005
/s/ AMBASSADOR JASON G. YUAN **Ambassador Jason G. Yuan**	Director	March 30, 2005
/s/ WILLIAM C.Y. CHENG **William C.Y. Cheng**	Director	March 30, 2005
/s/ FRANK T. LIN **Frank T. Lin**	Director	March 30, 2005
/s/ ALBERT YU, PH.D. **Albert Yu, Ph.D.**	Director	March 30, 2005

Exhibit 21.1

SUBSIDIARIES OF THE REGISTRANT

None.

Exhibit 24.1

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned, a director or an officer, or both of Preferred Bank, a California state-chartered bank (the "Bank"), does hereby make, constitute and appoint Li Yu, whose address is in care of the Bank, 601 S. Figueroa Street, 20th Floor, Los Angeles, California 90017, the true and lawful attorney for the undersigned, with full power of substitution and revocation to each for the undersigned, and in the name, place and stead of the undersigned, to sign in any and all capacities and to file or cause to be filed, an annual report on Form 10-K with the Federal Deposit Insurance Corporation, pursuant to the Securities Exchange Act of 1934, as amended, and any and all amendments to such Form 10-K, hereby giving to such attorney full power to do everything whatsoever required or necessary to be accomplished in and about the premises as fully as the undersigned could do if personally present, hereby ratifying and confirming all that such attorney or substitutes shall lawfully do or cause to be done by virtue thereof.

IN WITNESS WHEREOF, the undersigned has set his hand this 30th day of March, 2005.

/s/ LI YU **Li Yu**	/s/ CHIH-WEI WU **Chih-Wei Wu**
/s/ CHRIS CHAN **Chris Chan**	/s/ FRANK T. LIN **Frank T. Lin**
/s/ J. RICHARD BELLISTON **J. Richard Belliston**	/s/ ALBERT YU, PH.D. **Albert Yu, Ph.D.**
/s/ GARY S. NUNNELLY **Gary S. Nunnelly**	
/s/ WILLIAM C. Y. CHENG **William C. Y. Cheng**	
/s/ AMBASSADOR JASON G. YUAN **Ambassador Jason G. Yuan**	

Exhibit 31.1

CERTIFICATION PURSUANT TO RULE
13a-14(a) AND 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Li Yu, certify that:

1. I have reviewed this Annual Report on Form 10-K of Preferred Bank;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2005

/s/ LI YU

Li Yu
Chairman, President and Chief Executive Officer

Exhibit 31.2

CERTIFICATION PURSUANT TO RULE
13a-14(a) AND 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Chris Chan, certify that:

1. I have reviewed this Annual Report on Form 10-K of Preferred Bank;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2005

/s/ CHRIS CHAN

Chris Chan
Senior Vice President and Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Preferred Bank (the "Bank") on Form 10-K for the period ending December 31, 2004 as filed with the Federal Deposit Insurance Corporation on the date hereof (the "Report"), I, Li Yu, Chairman, President and Chief Executive Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: March 30, 2005

/s/ LI YU

Li Yu
Chairman, President and Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Preferred Bank (the "Bank") on Form 10-K for the period ending December 31, 2004 as filed with the Federal Deposit Insurance Corporation on the date hereof (the "Report"), I, Chris Chan, Senior Vice President and Chief Financial Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: March 30, 2005

/s/ CHRIS CHAN

Chris Chan
Senior Vice President and
Chief Financial Officer