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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

# FORM 10-KSB/A

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the fiscal year ended December 31, 2007.**

**OR**

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from to**

**File Number** **000-51901**

# SANTA LUCIA BANCORP

(Name of small business issuer in its charter)

| | |
|---|---|
| **State of California**<br>(State or other jurisdiction of incorporation or organization) | **35-2267934**<br>(I.R.S. Employer Identification No.) |
| **7480 El Camino Real, Atascadero,**<br>(Address of principal executive offices) | **California 93422**<br>(Zip Code) |

Issuer's telephone number **(805) 466-7087**

Securities registered under Section 12(b) of the Exchange Act: **None**

Securities registered under Section 12(g) of the Exchange Act:

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock (no par value) | None |

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 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 ☐

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB ☐.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

Registrant's revenues for the year ended December 31, 2007 were $18,789,927.

The aggregate market value of the voting common stock held by non-affiliates of the Registrant at March 1, 2008 was approximately $29,486,326.

As of March 1, 2008, the Registrant had 1,924,863 shares of Common Stock outstanding.

The information required in Part III, Items 9 through 12 and 14 is incorporated herein from the Registrant's definitive proxy statement for the 2008 annual meeting of shareholders previously filed pursuant to Regulation 14A and Part II, Items 6 and 7 of the 2007 Annual Report to Shareholders filed as an exhibit hereto.

Transitional Small Business Disclosure Format (check one) Yes ☐ No ☒

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**EXPLANATORY NOTE**

This Amendment No. 1 on Form 10-KSB/A (this "amendment") amends our Annual Report on form 10-KSB for the fiscal year ended December 31, 2007, originally filed on March 21, 2008 (the "Original Filing"). This amendment does the following: supplements certain information in Management's Discussion and Analysis; adds Exhibit 13.1, which was inadvertently omitted from the Original Filing; and corrects Exhibit 23.1. The Original Filing continues to speak as of the date of the original filing, and we have not updated the disclosures contained therein to reflect any events which occurred at a date subsequent to the filing of the Original Filing.

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**PART II**

**ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS AND RESULTS OF OPERATIONS**

**Liquidity**

The Company closely monitors its liquidity so that the cash requirements for loans and deposit withdrawals are met in an orderly manner. Management monitors liquidity in relation to trends of loans and deposits for short term and long-term requirements. Liquidity sources are cash, deposits with other banks, overnight Federal Fund investments, investment securities and the ability to sell loans. As of December 31, 2007, the Bank's liquidity ratio was 25.0% compared to 24.5% at December 31, 2006 and 27.7% at December 31, 2005. The 25.0% liquidity ratio at December 31, 2007 is well within the Company's policy limit.

The ability to have readily available funds that are sufficient to repay fully maturing liabilities is of primary importance to depositors, creditors and regulators. The Company's liquidity (represented by cash and due from banks, federal funds sold and available-for-sale securities) is a result of its operating, investing and financing activities and related cash flows. In order to ensure funds are available at all times, the Company devotes time and resources to analyzing trends and demands and projecting the amount of funds that will be required and maintains relationships with a diversified customer base so funds are accessible. Liquidity requirements can also be met through short term borrowings or the disposition of short term assets. The Bank has two borrowing arrangements with the Federal Home Loan Bank of San Francisco. The first allows the Bank to borrow up to approximately $41.0 million against which the Bank has pledged approximately $100.0 million in its real estate secured loans. The second arrangement allows the Bank to borrow up to approximately $12.0 million against which the Bank has pledged approximately $12 million of its investment securities. The Bank also has two borrowing lines at correspondent banks totaling $5.9 million.

As a secondary source of liquidity, the Company has reviewed the relative distribution of its asset portfolios (e.g., reducing investment or loan volumes and/or selling or encumbering assets). Further, the Company has the ability to increase liquidity by soliciting higher levels of deposit accounts through promotional activities and borrowing from correspondent banks as well as the FHLB. At the current time, the Company's long term liquidity needs primarily relate to funds required to support loan originations and commitments and deposit withdrawals.

The Company follows a formal liquidity policy, and in the opinion of management, its liquid assets are considered adequate to meet the cash flow needs for loan funding and deposit cash withdrawal for the next 60-90 days. At December 31, 2007, the Company had $63.5 million in liquid assets comprised of $7.4 million in cash and cash equivalents and $56.1 million in available-for-sale securities.

The Company's liquidity is comprised of three primary classifications: cash flows provided by operating activities; cash flows used in investing activities; and cash flows provided by financing activities. Net cash provided by operating activities has consisted primarily of net income adjusted for changes in certain other asset and liability accounts and certain non-cash income and expense items such as investment and other amortizations and depreciation. For the year ended December 31, 2007, net cash provided by operating activities was $4.3 million, compared to net cash provided by operating activities of $2.9 million in 2006.

The Company's primary investing activities was the purchase of $13.3 million in securities. The main contribution of the net cash in investing activities has been influenced by the decrease of loan activity. The net decrease in loans for the year ended December 31, 2007 was $5.3 million compared to the same period in 2006 of which net loans increased $23.9 million.

**Capital**

The Bank is required to maintain a minimum leverage-capital ratio of Tier I (as defined) to total assets based on the Bank's ratings under the regulatory rating system. At the end of 2007, all Bank capital ratios were above all current Federal capital guidelines for a "well capitalized" bank. As of December 31, 2007 the regulatory total capital to risk-weighted assets ratio was 13.8% compared to 13.1% as of December 31, 2006 and 11.3% as of December 31, 2005. The regulatory Tier I capital to risk-weighted assets ratio was 12.3% on December 31, 2007 compared to 11.4% on December 31, 2006 and 9.3% as of December 31, 2005. The regulatory Tier I capital to average assets ratio was 9.9% as of December 31, 2007 compared to 9.1% as of December 31, 2006 and 7.2% as of December 31, 2005.

The Bank's Tier I Capital ratio increased 74 basis points and the Bank's Total Capital to Risk Weighted Assets ratio increased 67 basis points, due to the strong earnings of $3.2 million for 2007.

In order to manage the Company's capital position more efficiently, in 2006 the Company issued $5,155,000 in junior subordinated debt securities (the "debt securities") to the Santa Lucia Bancorp (CA) Capital Trust, a statutory trust created under the laws of the State of Delaware. These debt securities are subordinated to effectively all borrowings of the Company and are due and payable on July 7, 2036. These debt securities may be redeemed for 105% of the principal balance through July 7, 2011, subject to any required regulatory approvals, and then at par thereafter. Interest is payable quarterly beginning July 7, 2006 at 1.48% over the quarterly adjustable 3-month LIBOR. Of this $5.2 million, the Company contributed $3 million to the Bank and retained $2.2 million at the Company level in which $1.0 million was used to repurchase the Company's stock. The securities do not entitle the holders to voting rights in the Company but contain certain restrictive covenants, including restrictions on the payment of dividends to the holders of the Company's common stock in the event that interest payments on the trust preferred securities are postponed. The capital received from the trust preferred issuance is designated as Tier 1 capital for regulatory purposes.

During the third quarter of 2003, the Bank undertook and completed a private placement of subordinated debentures ("notes") to augment its Tier 2 capital. The total principal amount of the notes issued was $2,000,000. The notes were sold pursuant to an applicable exemption from registration under the Securities Act of 1933 to certain accredited investors, including some of the Company's directors and executive officers. The notes include quarterly payment of interest at prime plus 1.5% and quarterly principal installments of approximately $166,666 commencing on September 30, 2008 until paid in full on June 30, 2011.

**Off-Balance Sheet Arrangements**

The Company, in the ordinary course of business, routinely enters into contracts for services. These contracts may require payment for services to be provided in the future and may also contain penalty clauses for the early termination of the contracts. The Company is also party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Additionally, in connection with the issuance of trust preferred securities, the Company has committed to irrevocably and unconditionally guarantee the following payments or distributions with respect to the preferred securities to the holders thereof to the extent that the trust has not made such payments or distributions and has the funds, therefore: (i) accrued and unpaid distributions; (ii) the redemption price; and (iii) upon a dissolution or termination of the trust, the lesser of the liquidation amount and all accrued and unpaid distributions and the amount of assets of the trust remaining available for distribution. Management does not believe that these off-balance sheet arrangements have a material effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources, but there can be no assurance that such arrangements will not have a future effect. See Consolidated Financial Statements in Note M for more information regarding the Company's commitments.

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**PART 111**

**ITEM 13. EXHIBITS**

(a) The following exhibits are filed as part of the form 10-KSB, and this list includes the Exhibit Index:

**EXHIBIT INDEX**

| Exhibit Sequentially Number Pages | Exhibit | Numbered |
|---|---|---|
| 3.1 | Articles of Incorporation of the Bancorp, as amended | (13) |
| 3.2 | Bylaws of the Bancorp, as amended | (13) |
| 3.3 | Certificate of Amendment to Bylaws of Santa Lucia Bank, dated January 16, 2002 | (7) |
| 10.4 | Santa Lucia Bank's Employee Stock Ownership Plan | (1) |
| 10.5 | Plan Administrator's Guide for the Bank's Employee Stock Ownership Plan | (1) |
| 10.6 | Santa Lucia Bank's Profit Sharing Plan | (1) |
| 10.9 | Salary Continuation agreement by and between Santa Lucia Bank and Stanley R. Cherry, dated February 1, 1997 | (2) |
| 10.10 | Salary Continuation agreement by and between Santa Lucia Bank and Larry H. Putnam, dated February 1, 1997 | (2) |
| 10.11 | Deferred Fee Agreement by and Between Santa Lucia Bank and Khatchik Achadjian, dated February 1, 1997 | (2) |
| 10.12 | Deferred Fee Agreement by and Between Santa Lucia Bank and Dino Boneso, dated February 1, 1997 | (2) |
| 10.13 | Deferred Fee Agreement by and Between Santa Lucia Bank and Jerry W. DeCou, III, dated February 1, 1997 | (2) |
| 10.14 | Deferred Fee Agreement by and Between Santa Lucia Bank and Douglas C. Filipponi, dated February 1, 1997 | (2) |
| 10.15 | Deferred Fee Agreement by and Between Santa Lucia Bank and Jean Hawkins, dated February 1, 1997 | (2) |
| 10.16 | Deferred Fee Agreement by and Between Santa Lucia Bank and Paul G. Moerman, dated February 1, 1997 | (2) |
| 10.17 | Deferred Fee Agreement by and Between Santa Lucia Bank and Norman J. Norton, Jr., dated February 1, 1997 | (2) |

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| 10.18 | Deferred Fee Agreement by and Between Santa Lucia Bank and William S. Osibin, dated February 1, 1997 | (2) |
| 10.19 | Deferred Fee Agreement by and Between Santa Lucia Bank and D. Jack Stinchfield, dated February 1, 1997 | (2) |
| 10.20 | Director Retirement Agreement by and between Santa Lucia Bank and Khatchik Achadjian, dated February 1, 1997 | (2) |
| 10.21 | Director Retirement Agreement by and between Santa Lucia Bank and Dino A. Boneso, dated February 1, 1997 | (2) |
| 10.22 | Director Retirement Agreement by and between Santa Lucia Bank and Jerry W. DeCou, III, dated February 1, 1997 | (2) |
| 10.23 | Director Retirement Agreement by and between Santa Lucia Bank and Douglas C. Filipponi, dated February 1, 1997 | (2) |
| 10.24 | Director Retirement Agreement by and between Santa Lucia Bank and Jean Hawkins, dated February 1, 1997 | (2) |
| 10.25 | Director Retirement Agreement by and between Santa Lucia Bank and Paul G. Moerman, dated February 1, 1997 | (2) |
| 10.26 | Director Retirement Agreement by and between Santa Lucia Bank and Willard S. Osibin, dated February 1, 1997 | (2) |
| 10.27 | Director Retirement Agreement by and between Santa Lucia Bank and D. Jack Stinchfield, dated February 1, 1997 | (2) |
| 10.28 | Agreement for Data Processing Services between Santa Lucia Bank and Fiserv Savings and Community Bank Group, dated February 21, 1997 | (3) |
| 10.29 | Equipment Sales Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.30 | Equipment Sales Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.31 | Equipment Sales Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.32 | Software License Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.33 | Product License Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.34 | Product License Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.35 | Product License Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |

10.36 Services Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 (3)

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| 10.37 | Remote Access Support Agreement between Santa Lucia Bank and Information Technology, Inc., dated February 14, 1997 | (3) |
| 10.38 | Salary Continuation Agreement by and between Santa Lucia Bank and John C. Hansen, dated August 1, 1998 | (4) |
| 10.39 | Employment Agreement by and between Santa Lucia Bank and Stanley R. Cherry, dated August 1, 1998 | (4) |
| 10.40 | Employment Agreement by and between Santa Lucia Bank and Larry H. Putnam, dated August 1, 1998 | (4) |
| 10.41 | Employment Agreement by and between Santa Lucia Bank and John C. Hansen dated August 1, 1998 | (4) |
| 10.42 | Santa Lucia Bank 2000 Stock Option Plan and form of stock option agreement | (5) |
| 10.44 | Amendment to Salary Continuation Agreement of Stanley R. Cherry, Dated April 15, 1998 | (6) |
| 10.45 | Amendment to Salary Continuation Agreement of Larry H. Putnam, dated April 15, 1998 | (6) |
| 10.46 | Amendment to Salary Continuation Agreement of Stanley R. Cherry, dated May 10, 2000 | (6) |
| 10.47 | Amendment to Santa Lucia Bank Director Retirement Agreement with Khatchik H. Achadjian | (6) |
| 10.48 | Amendment to Santa Lucia Bank Director Retirement Agreement with Dino Boneso, dated January 10, 2001 | (6) |
| 10.49 | Amendment to Santa Lucia Bank Director Retirement Agreement with Jerry W. DeCou, III, dated January 10, 2001 | (6) |
| 10.50 | Amendment to Santa Lucia Bank Director Retirement Agreement with Douglas C. Filipponi, dated January 10, 2001 | (6) |
| 10.51 | Amendment to Santa Lucia Bank Director Retirement Agreement with Jean Hawkins, dated January 10, 2001 | (6) |
| 10.52 | Amendment to Santa Lucia Bank Director Retirement Agreement with Paul G. Moerman, dated January 10, 2001 | (6) |
| 10.53 | Amendment to Santa Lucia Bank Director Retirement Agreement with D. Jack Stinchfield, dated January 10, 2001 | (6) |
| 10.54 | Amendment to Salary Continuation agreement with Stanley R. Cherry, dated January 10, 2001 | (6) |
| 10.55 | Amendment to Salary Continuation agreement with Larry H. Putnam, dated January 10, 2001 | (6) |
| 10.56 | Amendment to Salary Continuation agreement with John C. Hansen, dated January 10, 2001 | (6) |

| | | |
|---|---|---|
| 10.57 | 401(K) Profit Sharing Plan adopted effective July 1, 2001 | (7) |
| 10.59 | Form of Note Purchase Agreement | (9) |
| 10.60 | Subordinated Note | (9) |
| 10.62 | Amendment to Employment Agreement by and between Santa Lucia Bank and John Hansen dated November 11, 2004 | (11) |
| 10.63 | Employment Agreement by and between Santa Lucia Bank and Jim Cowan dated November 11, 2004 | (11) |
| 10.65 | Santa Lucia Bancorp 2006 Equity Based Compensation Plan | (12) |
| 10.66 | Amended and Restated Employment Agreement by and between Santa Lucia Bank and Larry H. Putnam dated December 15, 2006 | (13) |
| 10.67 | Amended and Restated Employment Agreement by and between Santa Lucia Bank and John C. Hansen dated December 15, 2006 | (13) |
| 10.68 | Amended and Restated Employment Agreement by and between Santa Lucia Bank and James M. Cowan dated December 15, 2006 | (13) |
| 10.70 | Amendment to the Salary Continuation Agreement by and between Santa Lucia Bank and Larry H. Putnam dated April 12, 2007. | (14) |
| 10.71 | Amendment to the Salary Continuation Agreement by and between Santa Lucia Bank and John C. Hansen dated April 12, 2007. | (14) |
| 13.1 | The Company's 2007 Annual Report to Shareholders (parts not incorporated by reference are furnished for informational purposes only and are not filed herewith) previously filed on February 15, 2008 * | |
| 23.1 | Revised consent of independent accountants from Vavrinek, Trine, Day & Co., LLP * | |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 15d-14 * | |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 15d-14 * | |
| 32.1 | Certification pursuant to Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code * | |

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* Filed Herewith

(1) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 1995

(2) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 1996

(3) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 1997

(4) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 1998

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(5) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 1999

(6) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 2000

(7) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 2001

(8) Incorporated by reference from the Bank's Form 10-KSB for the year ended December 31, 2002

(9) Incorporated by reference from the Bank's Form 10-QSB for the period ended September 30, 2003

(10) Incorporated by reference from the Bank's Form 10-KSB for the period ended December 31, 2003

(11) Incorporated by reference from the Bank's Form 10-KSB for the period ended December 31, 2004

(12) Filed as part of Registrants Registration Statement on Form S-8 (File #333-137997) (Filed on 10/13/06)

(13) Incorporated by reference from the Bank's Form 10-KSB for the period ended December 31, 2006

(14) Incorporated by reference from the Bank's Form 10-QSB for the period ended March 31, 2007

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**SIGNATURES**

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**SANTA LUCIA BANCORP**

By: /s/ Larry H. Putnam
LARRY H. PUTNAM
President and Chief Executive Officer
(Principal Executive Officer)
Dated: July 22, 2008

By: /s/ John C. Hansen
JOHN C. HANSEN
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)
Dated: July 22, 2008

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

| | | **Dated:** |
|---|---|---|
| /s/ Larry H. Putnam<br>LARRY H. PUTNAM | President and Chief Executive Officer, and Director | July 22, 2008 |
| /s/ Jerry W. DeCou III<br>JERRY W. DECOU III | Chairman of the Board of Directors | July 22, 2008 |
| /s/ Douglas C. Filipponi<br>DOUGLAS C. FILIPPONI | Vice Chairman of the Board of Directors | July 22, 2008 |
| /s/ John C. Hansen<br>JOHN C. HANSEN | Executive Vice President and Chief Financial Officer and Director | July 22, 2008 |
| /s/ Jean Hawkins<br>JEAN HAWKINS | Director | July 22, 2008 |
| /s/ Paul G. Moerman<br>PAUL G. MOERMAN | Director | July 22, 2008 |

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## EXHIBIT INDEX

**Index to Exhibits**

| | |
|---|---|
| **13.1** | Annual Report to Shareholders filed on February 15, 2008 |
| **23.1** | Revised consent of independent accountants from Vavrinek, Trine, Day & Co., LLP |
| **31.1** | Certification of Chief Executive Officer pursuant to Rule 15d-14 |
| **31.2** | Certification of Chief Financial Officer pursuant to Rule 15d-14 |
| **32.1** | Certification pursuant to Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code |

**Exhibit 13.1**

# Santa Lucia Bancorp 2007 Annual Report



**2007**

**Santa Lucia Bancorp**
7480 El Camino Real
Atascadero, California 93422

*Stock Symbol* – SLBA.OB

**Santa Lucia Bank**
7480 El Camino Real
Atascadero, California 93422

**www.santaluciabank.com**

**Atascadero**
7480 El Camino Real
(805) 466-7087

**Paso Robles**
1240 Spring St.
(805) 239-1140

**Arroyo Grande**
1530 E. Grand Ave.
(805) 473-1988

**Santa Maria**
1825 S. Broadway
(805) 614-9100

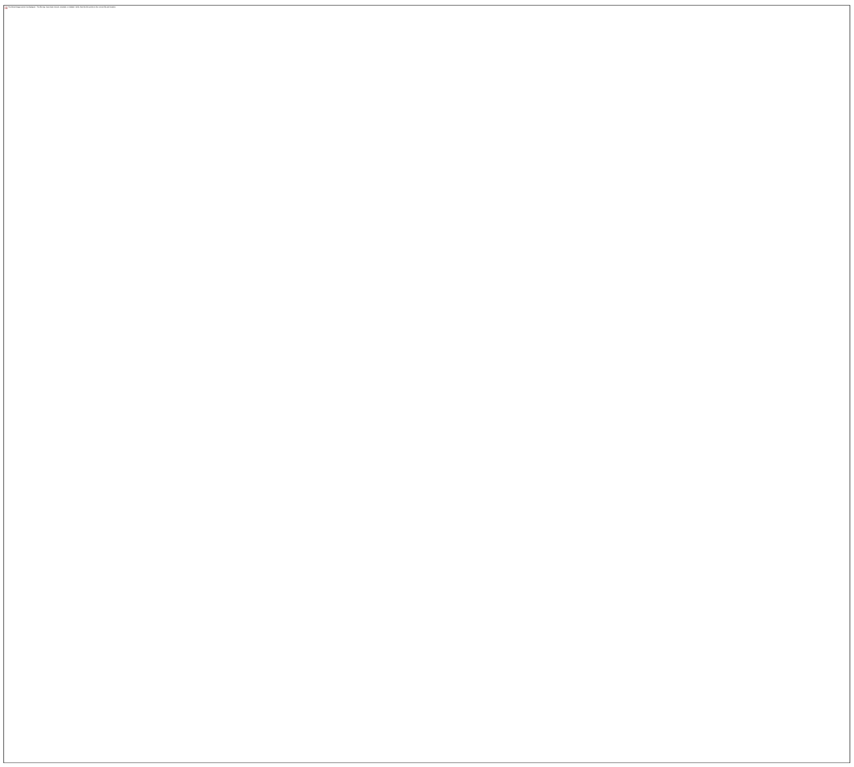
**Santa Lucia Bancorp**

***Message from the President***

Dear Shareholders, Customers and Friends,

Santa Lucia Bancorp (“The Company”) is pleased to report the results from operations for 2007. The economy and more specifically, “The Real Estate Market”, went through some difficult times in 2007, and are still in the process of recovering. We are pleased to report that these events, neither directly, nor indirectly have had a significant affect on The Company or Santa Lucia Bank (“The Bank”), its wholly owned subsidiary.

Net profits for The Company were $3,002,819 for the year 2007. This compares to 2006’s net income of $3,388,271, which was an all time high for The Company. The net income for 2007 is down 11.38% from 2006.



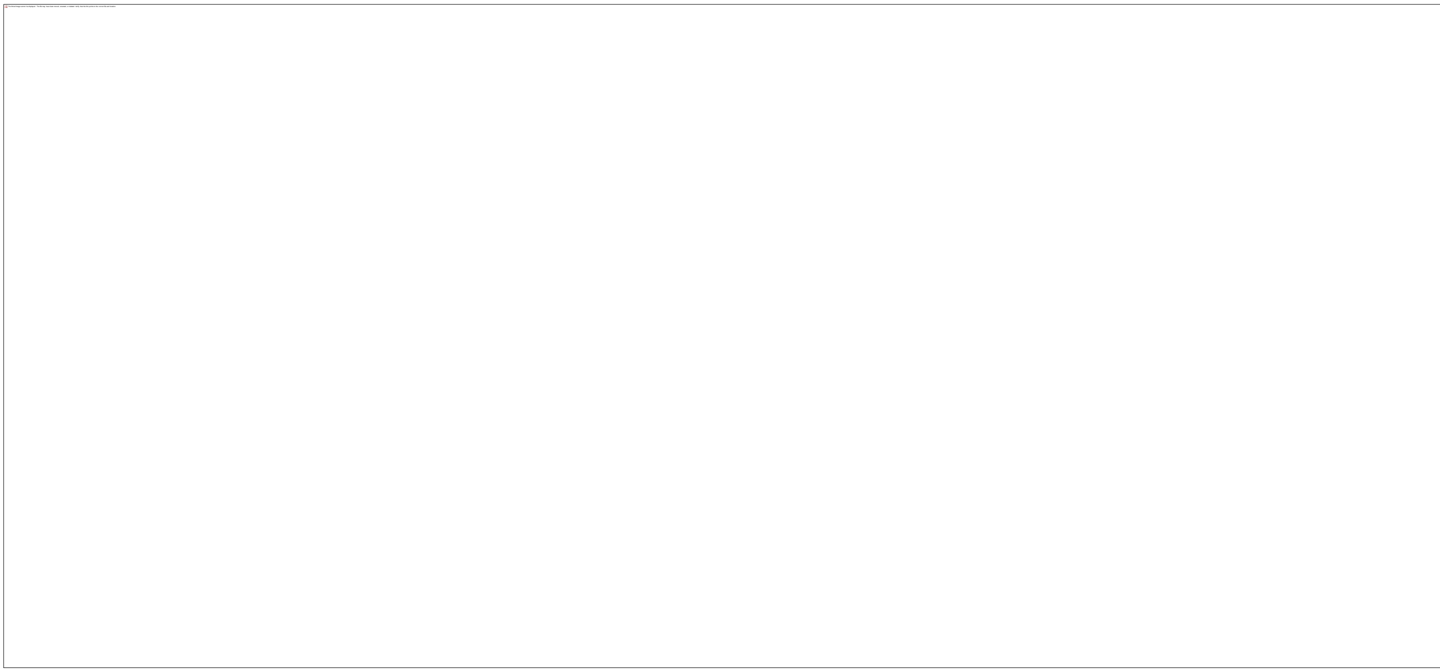
Larry H. Putnam, President and Chief Executive Officer

Due to the change in the economic conditions we operate in, our customers have reinvested funds in their businesses and have less excess funds, which have had a negative effect on the Company’s deposits. The trend of depositing excess funds into Time Certificates of Deposit or other interest bearing accounts that started in 2006 has continued into 2007. Despite this trend, the Bank has 36.25% of total deposits in non-interest bearing deposits. This compares to 40.50% in non-interest bearing deposits as of December 31, 2006. Non-interest bearing deposits at these levels continue to be well above industry averages.

The Company was able to effectively reallocate funds from real estate lending, specifically construction lending into loans for general commercial credit purposes. The Bank was pleased to see the significant growth in loans for general commercial credit purposes, which increased 11.73% between December 31, 2006 and 2007. This is an area we have been concentrating on for the last several years, as a significant change was anticipated in the real estate construction industry. We would expect this trend to continue.

Despite the fact that we have seen some changes in our business, we have a strong core deposit and loan base. We remain committed to providing quality customer service on a consistent basis in the markets we serve. Building solid relationships with our customers allows us to continue to build on our core business.

Santa Lucia Bancorp continues the practice of paying cash dividends to our shareholders. Two cash dividends were paid in 2007 for a total of $0.45 per share. The dividend payable to



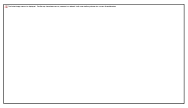
Santa Lucia Bancorp’s Board of Directors. Standing left to right—John C. Hansen, Executive Vice President - Chief Financial Officer, Jerry W. DeCou III, Chairman of the Board, Larry H. Putnam, President and Chief Executive Officer, Douglas C. Filipponi, Vice Chairman. Seated left to right—Paul G. Moerman, D. Jack Stinchfield, Jean Hawkins, Stanley R. Cherry and Khatchik H. Achadjian.

shareholders as of September 30, 2007 was increased by 25% to $0.25 per share compared to the dividend of $0.20 per share paid to shareholders of record as of March 31, 2007. This is the eighteenth consecutive year that cash dividends have been paid to our shareholders.

On June 30, 2005, the Company split its stock on a 4 to 1 basis. Since the stock split, the marketability and activity has increased in the companies stock, which was anticipated. Prior to the split, the companies stock was selling for $81.00 per share, resulting in a post split price of $20.25 per share compared to the current price of $25.00. Despite the recent decline in price, the stock has increased in value $4.75 per share or 23.46% in the past 2-1/2 years.

We look forward to the challenges of 2008 and are very optimistic about the future. We have effectively weathered the economic challenges of 2007. Our Board of Directors, Officers and Staff remain committed to building a solid banking franchise.

I would like to thank our shareholders for your support and trust over the years. This coupled with our loyal customer base, strategic locations on the Central Coast of California and dedicated staff will ensure that we continue to enhance the Company’s performance and value in years to come.



**Larry H. Putnam**
President and Chief Executive Officer

**SANTA LUCIA BANK**
*(a wholly owned subsidiary of Santa Lucia Bancorp)*

**Senior Management Team**

John C. Hansen, Larry H. Putnam, James M. Cowan

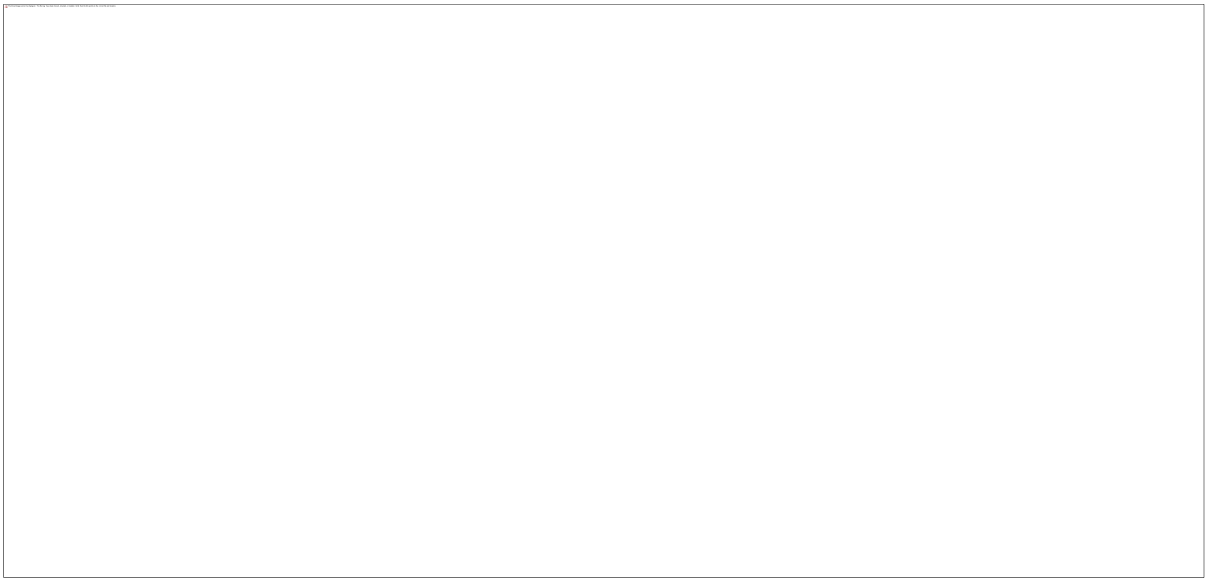
LARRY H. PUTNAM
Chief Executive Officer

JOHN C. HANSEN
President and
Chief Operating Officer

JAMES M. COWAN
Executive Vice President
Chief Credit Officer

***Eager to service your banking needs***

**Administrative Team**




Melodee Fontana, John C. Hansen, Larry H. Putnam, Julie A. Joslin, Kristie Keller, James M. Cowan, Larry Womack, Sharon Satterthwaite

LARRY H. PUTNAM
Chief Executive Officer

JOHN C. HANSEN
President and Chief Operating Officer

JAMES M. COWAN
Executive Vice President
Chief Credit Officer

MELODEE FONTANA
Senior Vice President
Operations Administrator

SHARON SATTERTHWAITE
Vice President
Controller

LARRY WOMACK
Vice President
Assistant Credit Administrator

JULIE A. JOSLIN
Vice President
Cashier

KRISTIE KELLER
Assistant Vice President
Central Operations

**Atascadero Office**

7480 El Camino Real, Atascadero, California

**Atascadero Officer Team**

Jim Kelley, Karen Sampson, Kim Donaldson, J. Darren Barnes, Teri Davis

TERI DAVIS
Vice President
Loan Officer

JIM KELLEY

Vice President
Loan Officer

KIM DONALDSON
Assistant Vice President
Operations Officer

J. DARREN BARNES
Assistant Vice President
Loan Officer

KAREN SAMPSON
Assistant Operations Officer

**Paso Robles Office**
1240 Spring Street, Paso Robles, California

**Paso Robles Officer Team**

Robert Covarrubias, Cheryl Mumford, Ryun McCrory

ROBERT COVARRUBIAS
Senior Vice President
Manager

CHERYL MUMFORD
Assistant Vice President

Operations Officer

RYUN McCRORY
Assistant Vice President
Loan Officer

**Arroyo Grande Office**
1530 East Grand Avenue, Arroyo Grande, California

**Arroyo Grande Officer Team**

Richard Allen, Michael W. McKenzie, Regina M. Sheldon, Jennifer Bassi Ginder

**MICHAEL W. McKENZIE**
Vice President
Manager

**RICHARD ALLEN**
Vice President
Loan Officer

**JENNIFER BASSI GINDER**
Assistant Vice President
Operations Officer

**REGINA M. SHELDON**
Assistant Vice President
Loan Officer

**Santa Maria Office**
1825 South Broadway, Santa Maria, California

**Santa Maria Officer Team**

Leah T. West, James P. Burubeltz, Stella Martinez, Robert J. McConaghy

**LEAH T. WEST**
Vice President
Manager

**JAMES P. BURUBELTZ**
Vice President

Loan Officer

**STELLA MARTINEZ**
Operations Officer

**ROBERT J. McCONAGHY**
Loan Officer

**SANTA LUCIA BANCORP**
**FINANCIAL HIGHLIGHTS**
*As of Years Ended December 31,*

The Company has only one class of securities, common stock, which is traded on the over-the-counter market. Our stock is quoted on the OTC Bulletin Board under the symbol SLBA.OB. The information in the following table indicates the high and low bid prices of the Company's common stock for each quarterly period during the last two years based upon information provided by the Company market makers. These prices do not include retail mark ups, mark downs or commissions, but have been adjusted to reflect the Bank's 4-for-1 stock split that was effective June 2006.

| Quarter Ended 2007 | Low | High |
| --- | --- | --- |

| | Low | High |
|---|---|---|
| December 31 | $ 23.25 | $ 26.25 |
| September 30 | 25.00 | 29.00 |
| June 30 | 26.00 | 28.99 |
| March 31 | 26.00 | 29.00 |

| **Quarter Ended 2006** | **Low** | **High** |
|---|---|---|
| December 31 | $ 24.00 | $ 29.00 |
| September 30 | 24.05 | 27.00 |
| June 30 | 26.55 | 34.50 |
| March 31 | 25.05 | 30.25 |

**Santa Lucia Bancorp and Subsidiary**

**Consolidated Selected Financial Information**

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | **2007** | **2006** | **2005** | **2004** | **2003** |
| | (dollars in thousands, except per share data) | | | | |
| **Summary of Operations:** | | | | | |
| Interest Income | $ 17,719 | $ 17,027 | $ 13,546 | $ 10,220 | $ 9,157 |
| Interest Expense | 4,824 | 3,577 | 1,984 | 1,343 | 1,324 |
| Net Interest Income | 12,895 | 13,450 | 11,562 | 8,877 | 7,833 |
| Provision for Loan Loss | — | 240 | 300 | 110 | 115 |
| Net Interest Income After Provision for Loan Losses | 12,895 | 13,210 | 11,262 | 8,767 | 7,718 |
| Noninterest Income | 1,071 | 1,010 | 1,052 | 1,191 | 1,376 |
| Noninterest Expense | 9,029 | 8,590 | 7,808 | 7,060 | 6,609 |
| Income Before Income Taxes | 4,937 | 5,630 | 4,506 | 2,898 | 2,485 |
| Income Taxes | 1,934 | 2,242 | 1,759 | 1,076 | 873 |
| Net Income | $ 3,003 | $ 3,388 | $ 2,747 | $ 1,822 | $ 1,612 |
| Cash Dividends Paid | $ 871 | $ 768 | $ 730 | $ 697 | $ 685 |
| **Per Share Data:** | | | | | |
| Net Income – Basic | $ 1.55 | $ 1.77 | $ 1.46 | $ 0.98 | $ 0.89 |
| Net Income – Diluted | $ 1.51 | $ 1.68 | $ 1.38 | $ 0.94 | $ 0.86 |
| Dividends | $ 0.450 | $ 0.400 | $ 0.388 | $ 0.375 | $ 0.375 |
| Book Value | $ 11.01 | $ 9.93 | $ 8.35 | $ 7.42 | $ 6.96 |
| **Common Outstanding Shares:** | 1,924,873 | 1,928,097 | 1,899,543 | 1,861,764 | 1,844,708 |
| **Statement of Financial Condition Summary:** | | | | | |
| Total Assets | $ 248,640 | $ 240,738 | $ 231,532 | $ 211,684 | $ 183,827 |
| Total Deposits | 212,718 | 212,988 | 206,879 | 194,868 | 168,033 |
| Total Net Loans | 166,619 | 169,680 | 152,563 | 125,586 | 109,949 |
| Allowance for Loan Losses | 1,673 | 1,654 | 1,470 | 1,200 | 1,112 |
| Total Shareholders' Equity | 21,189 | 19,137 | 15,866 | 13,807 | 12,845 |
| **Selected Ratios:** | | | | | |
| Return on Average Assets | 1.22% | 1.42% | 1.21% | 0.91% | 0.94% |
| Return on Average Equity | 14.87% | 19.45% | 18.67% | 13.71% | 13.00% |
| Average Loans as a Percentage of Average Deposits | 76.11% | 79.74% | 69.90% | 62.77% | 68.93% |
| Allowance for Loan Losses to Total Loans | 0.99% | 0.96% | 0.95% | 0.94% | 1.00% |
| **Company:** | | | | | |
| Tier I Capital to Average Assets | 10.50% | 10.00% | — | — | — |
| Tier I Capital to Risk-Weighted Assets | 13.20% | 12.70% | — | — | — |
| Total Capital to Risk-Weighted Assets | 14.60% | 14.40% | — | — | — |
| **Bank:** | | | | | |
| Tier I Capital to Average Assets | 9.85% | 9.11% | 7.16% | 6.53% | 7.00% |
| Tier I Capital to Risk-Weighted Assets | 12.33% | 11.43% | 9.33% | 8.80% | 9.34% |
| Total Capital to Risk-Weighted Assets | 13.80% | 13.13% | 11.34% | 10.85% | 11.66% |

**Santa Lucia Bancorp and Subsidiary**

## General

Santa Lucia Bancorp (the "Company") (OTC Bulletin Board SLBA.OB) is a California corporation organized April 3, 2006 to act as the holding company for its wholly owned subsidiary Santa Lucia Bank (the "Bank"), collectively referred to herein as the "Company." The Bank was organized as a national banking association on December 19, 1984 and commenced operations on August 5, 1985. The Bank converted from a national to a California state-chartered bank on May 30, 1997.

The Bank is a commercial banking business, operating from offices located at 7480 El Camino Real, Atascadero, California, 1240 Spring Street, Paso Robles, California, 1530 East Grand Avenue, Arroyo Grande, California and 1825 South Broadway, Santa Maria, California.

The Bank's operating policy since its inception has emphasized general commercial banking. Most of the Bank's customers are small to mid-sized businesses and individuals. The business of the Bank emphasizes serving the needs of local businesses, professionals, and wage earners. The Bank provides services designed to meet the needs of the various segments of the markets it serves. These services include a full line of business loans, business leases, personal loans and deposit products.

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

Certain statements contained in this report, including, without limitation, statements containing the words "believes", "anticipates", "intends", "expects", and words of similar import, constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions in those areas in which the Company operates, demographic changes, competition, fluctuations in interest rates, changes in business strategy or developmental plans, changes in governmental regulations, credit quality, the availability of capital to fund the expansion of the Company's business, and other factors referenced in the Company's reports filed pursuant to the Exchange Act. Given these uncertainties, shareholders are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

This discussion should be read in conjunction with the Company's audited financial statements and notes thereto which appear elsewhere in this report.

#### *Overview*

The following sections set forth an analysis of the significant operating changes, business trends, financial condition, earnings, capital position and liquidity that have occurred in the three-year period ended December 31, 2007.

### Consolidated Results of Operations

In 2007 the Company recorded earnings of $3,003,000, which reflects a decrease of $385,000 or 11.4% over the previous year. In 2006, earnings were $3,388,000, an increase of 23.3% from 2005's earnings of $2,747,000, which reflected an increase of 50.8% from earnings posted in 2004. Basic earnings per share in 2007 were $1.55 compared with $1.77 and $1.46 for 2006 and 2005, respectively. This reflects a decrease from 2006 to 2007 of 12.4%. The earnings per share (diluted) for 2007, 2006, and 2005 were $1.51, $1.68, and $1.38, respectively, a 10.1% decrease from 2006 to 2007. The Company paid cash dividends totaling $0.45 per share during 2007 compared to $0.40 paid in 2006 and $0.388 paid in 2005. Return on average shareholder's equity was 14.9% in 2007 compared to 19.5% in

2006 and 18.7% in 2005. Return on average assets was 1.22% in 2007 compared to 1.42% in 2006 and 1.21% in 2005.

The decrease in the Company’s net earnings from 2006 to 2007 was due to four major events: a decrease in average loans of $7,105,000 or 4.2%; a 100 basis point decrease in the prime lending rate; an increase of $10,689,000 in average interest bearing deposits or 8.7%; and a 65 basis point increase in interest bearing deposit rates.

The Company believes that the local economies, in which it operates, Atascadero, Paso Robles, Arroyo Grande, and Santa Maria continue to remain relatively stable. Competition for deposits continues to be very strong both from traditional sources as well as alternative investments such as mutual funds, money market accounts and the stock market. The Bank’s decline in the loan portfolio has been affected by the slow down in the demand for construction lending and real estate related markets.

***Net Interest Income***

Net interest income is the Company's largest source of operating income and is derived from interest and fees received on interest earning assets, less interest expense incurred on interest bearing liabilities. The most significant impact on the Company's net interest income between periods is derived from the interaction of changes in the volume of and rates earned or paid on interest earning assets and interest bearing liabilities. The volume of loans, investment securities and other interest earning assets, compared to the volume of interest bearing deposits and indebtedness, combined with the spread, produces changes in the net interest income between periods.

Interest income increased $692,000 or 4.1% in 2007 from $17,027,000 in 2006 to $17,719,000 in 2007. This is compared to an increase of $3,481,000 or 25.7% from 2005 to 2006 and an increase of $3,326,000 or 32.5% from 2004 to 2005. The slowdown in the increase in interest income is again attributable to the slowdown in real estate lending. The increase in 2007 was primarily due to the increase in average investments of $10,451,000 or 27.1% from 2006 and an increase in the average investment yield from 3.9% in 2006 to 5.0% in 2007.

Total interest and fees produced an 8.1% yield on average earning assets for 2007, 8.1% for 2006 and 6.8% in 2005. The average loan to deposit ratio for 2007 was 76.11%, which represents a decrease of 4.6% over the 79.74% average for 2006.

Total interest expense increased $1,247,000 or 34.9% from $3,577,000 in 2006 to $4,824,000 in 2007 compared to an increase of $1,593,000 or 80.3% from 2005 to 2006. The increase in total interest expense in 2007 was due to a combination of rising rates for all deposit categories coupled with an increase in interest bearing funds. In 2007, total interest bearing liabilities increased $12.1 million or 9.3%. These factors increased our rate paid on interest-bearing liabilities 65 basis points from 2.76% in 2006 to 3.41% in 2007.

Net interest margin decreased 46 basis points from 6.38% in 2006 to 5.92% in 2007. As noted above, this decrease was primarily due to changes in our asset mix and an increase in our cost of funds. In our asset mix, we experienced migration from higher yielding loans to lower yielding investments while in our liability mix, we experienced migration from lower costing NOW, Money Market and Savings accounts to higher costing time certificates of deposits and long-term debt.

We expect this trend of reduction in our net interest margin to continue into 2008 as anticipated prime rate decreases will impact our interest earning assets faster than we can reprice our interest-bearing deposits.

The following table shows the composition of average earning assets and average interest-bearing liabilities, average yields and rates, and the net interest margin for the years ended December 31, 2007, 2006 and 2005. Nonaccrual loans are included in the calculation of the average balances of loans, and nonaccrued interest is excluded.

| | Year Ended December 31 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | | 2005 | | |
| | Average Balance | Interest | Yield/ Rate | Average Balance | Interest | Yield/ Rate | Average Balance | Interest | Yield/ Rate |
| | (dollars in thousands) | | | | | | | | |
| Assets: | | | | | | | | | |
| Loans | $ 163,741 | $ 15,031 | 9.18% | $ 169,139 | $ 15,397 | 9.10% | $ 145,195 | $ 11,747 | 8.09% |
| Investment securities | 49,024 | 2,438 | 4,97% | 38,573 | 1,485 | 3.85% | 48,660 | 1,625 | 3.34% |
| Federal funds sold | 4,954 | 250 | 5.05% | 2,941 | 145 | 4.93% | 5,685 | 174 | 3.06% |
| Total average interest-earning assets | 217,719 | 17,719 | 8.14% | 210,653 | 17,027 | 8.08% | 199,540 | 13,546 | 6.79% |
| Other assets | 29,278 | | | 28,808 | | | 27,913 | | |
| Less allowance for loan losses | (1,707) | | | (1,593) | | | (1,332) | | |
| Total average assets | $ 245,290 | | | $ 237,868 | | | $ 226,121 | | |
| | | | | | | | | | |
| Liabilities and Shareholders' Equity: | | | | | | | | | |
| Interest-bearing demand - NOW | $ 13,391 | $ 55 | 0.41% | $ 14,696 | $ 38 | 0.26% | $ 17,834 | $ 42 | 0.24% |
| Money Market | 24,929 | 722 | 2.90% | 24,103 | 503 | 2.09% | 30,186 | 446 | 1.48% |
| Savings | 27,076 | 289 | 1.07% | 28,074 | 222 | 0.79% | 30,560 | 133 | 0.44% |
| Time certificate of deposits | 68,019 | 3,157 | 4.64% | 55,853 | 2,316 | 4.15% | 40,772 | 1,195 | 2.93% |
| Total average interest- | 133,415 | 4,223 | 3.17% | 122,726 | 3,079 | 2.51% | 119,352 | 1,816 | 1.52% |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| bearing deposits | | | | | | | | | |
| Short-term borrowings | 1,059 | 51 | 4.82% | 1,356 | 65 | 4.79% | 439 | 16 | 3.64% |
| Long-term borrowings | 7,155 | 550 | 7.69% | 5,465 | 433 | 7.92% | 2,000 | 152 | 7.60% |
| Total interest-bearing liabilities | 141,629 | 4,824 | 3.41% | 129,547 | 3,577 | 2.76% | 121,791 | 1,984 | 1.63% |
| Demand deposits | 81,714 | | | 89,383 | | | 88,366 | | |
| Other liabilities | 1,749 | | | 1,515 | | | 1,253 | | |
| Sharholder’s equity | 20,198 | | | 17,423 | | | 14,711 | | |
| Total average liabilities and shareholders’ equity | $ 245,290 | | | $ 237,868 | | | $ 226,121 | | |
| Net interest income | | $ 12,895 | | | $ 13,450 | | | $ 11,562 | |
| Net interest margin | | | 5.92% | | | 6.38% | | | 5.79% |

The Company's net yield on interest-earning assets is affected by changes in the rates earned and paid and the volume of interest-earning assets and interest-bearing liabilities. The impact of changes in volume and rate on net interest income are shown in the following table:

| | Year Ended December 31, 2007 over Year Ended December 31, 2006 Increase (Decrease) Due to Change in (000's) | | | Year Ended December 31, 2006 over Year Ended December 31, 2005 Increase (Decrease) Due to Change in (000's) | | |
|---|---|---|---|---|---|---|
| | Volume | Rate | Change | Volume | Rate | Change |
| Interest-bearing Assets: | | | | | | |
| Net Loans | (495) | 129 | (366) | 2,075 | 1,575 | 3,650 |
| Investment Securities | 459 | 494 | 953 | (366) | 226 | (140) |
| Federal funds sold | 102 | 3 | 105 | (107) | 78 | (29) |
| Interest-earning deposits | — | — | — | — | — | — |
| Total interest income | 66 | 626 | 692 | 1,602 | 1,879 | 3,481 |
| Interest-bearing Liabilities: | | | | | | |
| Interest bearing demand - NOW | (3) | 20 | 17 | (8) | 4 | (4) |
| Money Market | 18 | 201 | 219 | (102) | 159 | 57 |
| Savings | — | 67 | 67 | 1 | 88 | 89 |
| Time Certificates of deposit | 542 | 299 | 841 | 528 | 593 | 1,121 |
| Short-term borrowings | (14) | — | (14) | 43 | 6 | 49 |
| Long-term borrowings | 16 | 101 | 117 | 16 | 265 | 281 |
| Total interest expense | 559 | 688 | 1,247 | 478 | 1,115 | 1,593 |
| Interest differential or net interest income | $ (493) | $ (62) | $ (555) | $ 1,124 | $ 764 | $ 1,888 |

***Noninterest Income***

Noninterest income totaled $1,071,000 compared to $1,010,000 for the same period in 2006. That represents an increase of $61,000 or 6.0%. The increase was primarily due to the recovery of legal fees and costs on a previously charged off loan and an increase in interest income derived from the investment in bank owned life insurance.

Service charges on deposit accounts totaled $583,000, which represents a decrease of $33,000 or 5.4% over the same period in 2006. The decrease in service charges was primarily due to the decrease in non sufficient fund fees collected.

Other noninterest income totaled $488,000 compared to $394,000 for the same period in 2006. That represents an increase of $94,000 or 23.9%. The increase is primarily due to the recovery of legal fees and costs on a previously charged off loan and an increase in interest income derived from the investment in bank owned life insurance.

Refer to the "Statement of Earnings" for a breakdown of noninterest income.

***Noninterest Expense***

Noninterest expense increased $439,000 or 5.1% in 2007 over 2006 to $9,029,000 as compared to an increase of $782,000 or 10.0% in 2006 over 2005. The overall increase can be largely attributed to the continued growth of the Company.

Salaries and related expenses increased $516,000 or 10.9% from 2006 to 2007 compared to an increase of $501,000 or 11.8% between 2005 and 2006. This increase is attributed to normal staff related increases, coupled with a 17.7% increase in group health insurance and a $54,000 shared-based payment, which is part of SFAS 123(R), "Share-Based Payment." SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values.

Occupancy expense for the year ended December 31, 2007 totaled $628,000, which reflects a decrease of $36,000 or 5.4% over the same period in 2006. This was primarily due to a decrease in real estate taxes coupled with fewer maintenance and repair costs.

Equipment expense for the year ended December 31, 2007 totaled $666,000, which reflects a decrease of $25,000 or 3.6% over the same period in 2006. This was primarily due to the eliminations of depreciation expense associated with fully depreciated equipment in the Santa Maria office.

Professional services for the year ended December 31, 2007 totaled $427,000, which reflects a decrease of $111,000 or 20.6% over the same period in 2006. This was primarily due to the decreases in legal and other professional services.

Data processing expense for the year ended December 31, 2007 totaled $489,000, which reflects an increase of $21,000 or 4.5% from the same period in 2006. This was primarily due to a 5.1% increase in contracted fees coupled with the continued growth of the Company.

Office expenses increased $2,000 from $360,000 in 2006 to $362,000 in 2007.

Marketing expense increased $15,000 or 3.7% from $408,000 in 2006 to $423,000 in 2007.

Director fees and expenses for the year ended December 31, 2007 totaled $329,000, which reflects an increase of $66,000 or 25.1% over the like period in 2006. The primary reason for the increase was a $56,000 stock option expense recognized for new option grants made in late 2006.

Messenger and courier expenses increased $9,000 or 6.1% from $148,000 in 2006 to $157,000 in 2007.

Other expense decreased $17,000 or 7.0% from $242,000 in 2006 to $225,000 in 2007. This decrease was due to $9,000 decrease in inspection fees associated with construction loans.

The Company’s efficiency ratio for 2007 was 64.7%. This represents an increase from the 2006 efficiency ratio of 60.4%, which was a decrease from the 2005 ratio of 63.4%. The increase in the efficiency ratio was primarily due to the decrease in the net interest margin, and the increase in non interest expense.

Refer to the “Statement of Earnings” for a breakdown of noninterest expense.

### *Income Taxes*

The provision for income taxes was $1,934,000 in 2007, $2,242,000 in 2006 and $1,759,000 in 2005. The effective tax rate was 39.1% in 2007 as compared to 39.9% in 2006 and 39.0% in 2005. This decrease was partially due to an increasing percentage of tax-free investments.

## Financial Condition

In 2007, the Company’s consolidated total assets increased to $248,640,000 compared to $240,738,000 in 2006 and $231,532,000 in 2005 for increases of 3.3%, 4.0% and 9.4% respectively.

Total deposits decreased $270,000 to $212,718,000 compared to $212,988,000 in 2006 and $206,879,000 in 2005 for a decrease of 0.1% for 2007, and increases of 3.0% and 6.2% for 2006 and 2005 respectively. Deposit competition continues to be very strong in both the traditional bank deposits and alternative investments available in the market place.

Securities available for sale totaled $56,107,000 at December 31, 2007, compared to $42,778,000 at December 31, 2006 and $41,830,000 at December 31, 2005. This represents an increase of 31.2% over December 31, 2006. The increase in securities was primarily due to the decrease in loan demand, which is the result of the softening in the construction and real estate markets.

### *Loan Portfolio*

Total loans outstanding averaged $163,741,000 in 2007 compared to $169,139,000 in 2006. This represents a decrease of $5,398,000 or 3.2% in 2007 compared to an increase of $23,944,000 or 16.5% in 2006. Actual net loans at December 31, 2007 equaled $166,619,000 for a decrease of $3,060,000 or 1.8 % over 2006.

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

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (dollars in thousands) | | | | |
| Commercial | $ 38,017 | $ 36,407 | $ 34,139 | $ 32,797 | $ 30,490 |
| Real Estate – construction | 47,819 | 55,307 | 52,696 | 29,707 | 25,446 |
| Real Estate – other | 81,895 | 78,757 | 66,390 | 63,433 | 53,931 |
| Consumer | 1,237 | 1,604 | 1,533 | 1,570 | 1,645 |
| Total gross loans | 168,968 | 172,075 | 154,758 | 127,507 | 111,512 |
| Less: unearned fees | (676) | (741) | (725) | (721) | (451) |
| Less: allowance for loan losses | (1,673) | (1,654) | (1,470) | (1,200) | (1,112) |
| Total net loans | $ 166,619 | $ 169,680 | $ 152,563 | $ 125,586 | $ 109,949 |

| | | | | | |
|---|---|---|---|---|---|
| Weighted average yield on loans for the year | 9.2% | 9.1% | 8.1% | 7.3% | 7.3% |

The following table sets forth the amount of total loans outstanding at December 31, 2007 by contractual maturity date:

| | One Year or Less | After One Year Through Five Years | After Five Years | Total |
|---|---|---|---|---|
| | | (dollars in thousands) | | |
| Commercial | $ 24,140 | $ 6,865 | $ 7,011 | $ 38,016 |
| Real Estate – construction | 42,862 | 4,505 | 453 | 47,820 |
| Real Estate – other | 5,307 | 7,310 | 69,278 | 81,895 |
| Consumer | 607 | 466 | 164 | 1,237 |
| | $ 72,916 | $ 19,146 | $ 76,906 | $ 168,968 |

A significant portion of the loan portfolio of the Company is dependent on real estate. At December 31, 2007, real estate served as the principal source of collateral with respect to 78.5% of the Company's loan portfolio. A decline in current economic conditions could have an adverse effect on the demand for new loans even if rates continue to decline. It is also understood that the ability of borrowers to repay outstanding loans, the value of real estate and other collateral securing loans and the value of real estate owned by the Company, could affect the Company's financial condition and results of operations in general and the market value of the Company's common stock. Acts of nature, including earthquakes and floods, which may cause uninsured damage and other loss of value to real estate that secures these loans, may also negatively impact the Company's financial condition.

Real estate construction and other real estate loans equaled $129,715,000 or 78.5% of the total loan portfolio and $134,065,000 or 77.9% of the total loan portfolio at December 31, 2007 and 2006, respectively. Other real estate loans are comprised of loans to individuals for their businesses, consumer real estate loans including home equity lines of credit and loans for farmland, including vineyards. The Company has known for some time that it has a concentration in commercial real estate loans. As a means to more closely monitor this concentration, the Company has instituted the use of NAICS codes to monitor industry trends within its commercial real estate portfolio. As of December 31, 2007, the Company had $72,608,000 or 43.0% of its loans in commercial real estate. Of this number, $45,960,000 or 63.3% is commercial real estate for owners use. No industry type exceeds 5.0% of total loans. The remaining $26,648,000 or 36.7% is commercial real estate for non-owners use. Commercial real estate loans for non-owners use as a percentage of total loans equates to 16.0%. We watch the commercial real estate loans for non-owners use along with changes within our owners use very closely and are familiar with the individuals and projects and at this time we do not foresee any problems or undue risk in this segment of our portfolio. Total real estate loans decreased $4,350,000 or 3.2% in 2007 over 2006 compared to an increased of $14,705,000 or 12.3% in 2006 over 2005. The decrease is spread throughout construction of residential units held for resale or for the borrower's personal residence, off-site development, or land held for future development of commercial or residential properties. The Company has seen a significant decrease in the number of residential construction loans, due to the softening in the real estate market. The Company has loans to customers with a long history of successful developments in our market areas, as well as a long-term relationship with Santa Lucia Bank. The Company has experience and knowledge in construction lending and does not feel that there is any undue risk to the Company. These loans are secured by real estate, and in general, do not exceed 75% of the appraised value on commercial residential real estate or 80% on an individual's personal residence.

The Company makes commercial loans to small and mid-size businesses for various reasons, including working capital, inventory and equipment. Commercial loans equaled $38,017,000 or 22.5% of the total loan portfolio and $36,407,000 or 21.2% of the total loan portfolio at December 31, 2007 and 2006, respectively. Commercial loans increased $1,610,000 or 4.4% from 2006 to 2007 compared to an increase of $2,268,000 or 6.6% in 2006 over 2005.

It has always been a part of our business banking practice to loan to small businesses for their facilities as well as their other business needs.

Consumer and other loans equaled $1,237,000 or 0.7% of the total loan portfolio at December 31, 2007 compared to $1,604,000 or 0.9% at December 31, 2006. Consumer loans decreased $367,000 or 22.9% in 2007 over 2006 compared to an increase of $71,000 or 4.6% in 2006 over 2005.

The Company had undisbursed loans totaling $57,326,000, $56,557,000, and $53,280,000 as of December 31, 2007, December 31, 2006 and December 31, 2005, respectively. Standby Letters of Credit accounted for $4,286,000, $2,603,000 and $1,546,000 of the undisbursed loans as of December 31, 2007, December 31, 2006 and December 31, 2005, respectively. The Company uses the same credit policies in making these commitments as is done for all of its lending activities. As such, the credit risk involved in these transactions is the same as that involved in extending loan facilities to customers.

Loans with maturities greater than one year at December 31, 2007 include approximately $40,803,000 of fixed rate loans or 24.2% of the total loan portfolio compared to $11,060,000 or 6.4% of the total loan portfolio as of December 31, 2006 and $7,642,000 or 4.9% of the total loan portfolio as of December 31, 2005. The balance of the loans that have maturities of one year or less, or are variable rate loans at December 31, 2007 totaled $128,165,000 or 31.8% compared to $161,015,000 or 93.6% as of December 31, 2006 and $147,116,000 or 95.1% as of

December 31, 2005. The $69.3 million in other real estate loans with five years or greater maturities are primarily owner occupied commercial properties. The Company has attempted to lengthen the maturities of loans in its portfolio to add additional stability to the loan portfolio.

### *Nonperforming loans*

Interest income is accrued daily as earned on all 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 based on the contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectibility. 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.

The composition of nonperforming loans as of the end of the last five fiscal years is summarized in the following table:

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | **2007** | **2006** | **2005** | **2004** | **2003** |
| | (dollars in thousands) | | | | |
| Nonaccrual loans: | | | | | |
| Commercial | $ 113 | $ — | $ — | $ — | $ 23 |
| Real estate | 2,062 | — | 135 | 758 | 805 |
| Consumer | — | — | — | — | — |
| Total | 2,175 | — | 135 | 758 | 828 |
| Loans 90 days or more past due and still accruing: | | | | | |
| Real estate | — | — | — | — | — |
| Consumer | — | — | — | — | — |
| Commercial | — | 550 | — | — | — |
| Total | — | 550 | — | — | — |
| Total nonperforming loans: | 2,175 | 550 | 135 | 758 | 828 |
| OREO | — | — | — | — | — |
| Total nonperforming assets: | $ 2,175 | $ 550 | $ 135 | $ 758 | $ 828 |
| Nonperforming assets as a percentage of total gross loans | 1.29% | 0.32% | 0.09% | 0.59% | 0.74% |
| Nonperforming assets as a percentageof total assets | 0.87% | 0.23% | 0.06 % | 0.36% | 0.45% |
| Allowance for loan losses to nonperforming loans | 76.92% | 300.73% | 1088.89 % | 158.31% | 134.30% |

The Company had three nonperforming loans totaling $2,175,000 as of December 31, 2007, compared to one nonperforming loan totaling $550,000 at December 31, 2006 and one nonperforming loan totaling $135,000 at December 31, 2005. Of the Company's nonperforming loans, two are well secured by residential real estate with minimal loss exposure. The commercial loan for $113,000 is 50% guaranteed by the U. S. Small Business Administration, and is secured by business assets of the borrower in addition to the personal residence of the guarantor. The Company is in the process of assessing the value of its collateral and any actual loss is unknown at this time. The Company has however, assigned loan loss reserves in an amount it feels is adequate to satisfy any potential loss based on the collateral.

There were no significant loans that were current as of December 31, 2007, where serious doubt existed as to the ability of the borrower to comply with the present loan repayment terms or that represent a "troubled debt restructuring."

The Company had no "Other Real Estate Owned" (OREO) property as of December 31, 2007.

The Company experienced net charge-offs (recoveries) of ($19,000), $56,000 and $30,000 in 2007, 2006 and 2005 respectively.

### *Quality of loans*

Inherent in lending is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan extended and the creditworthiness of the borrower. To reflect the estimated risks of loss associated with its loan portfolio, provisions are made to the Company's allowance for possible loan losses. As an integral part of this process, the allowance for possible loan losses is subject to review and possible adjustment as a result of regulatory examinations conducted by governmental agencies and through management's assessment of risk. The Company's entire allowance is a valuation allocation; that is, it has been created by direct charges against operations through the provision for possible loan losses.

The Company evaluates the allowance for possible loan losses based upon an individual analysis of specific categories of loans, specific categories of classified loans and individual classified assets. The adequacy of the allowance is determinable only on an approximate basis, since estimates as to the magnitude and timing of loan losses are not predictable because of the impact of external events. In addition, the Company contracts with an independent loan review firm to evaluate overall credit quality on an ongoing basis. Management then considers the adequacy of the allowance for possible loan losses in relation to the total loan portfolio.

The provision for possible loan losses charged against operating expense is based upon an analysis of the actual migration of loans to losses plus an amount for other factors that, in management's judgment, deserve recognition in estimating possible loan losses. These factors include numerous items among which are: specific loan conditions as determined by management; the historical relationship between charge-offs and the level of the allowance; the estimated future loss in all significant loans; known deterioration in concentrations of credit; certain classes of loans or pledged collateral; historical loss experience based on volume and type of loan; the results of any independent review or evaluation of the loan portfolio quality conducted by or at the direction of the Company's management or by bank regulatory agencies; trends in portfolio volume, maturity, and composition; off-balance sheet credit risk; volume and trends in delinquencies and nonaccruals; lending policies and procedures including those for charge-off, collection, and recovery; national and local economic conditions and downturns in specific local industries; and the experience, ability, and depth of the lending staff and management. The Company evaluates the adequacy of its allowance for possible loan losses quarterly.

It was management's decision that no additional loan loss provision was needed during 2007 primarily based on the foregoing analysis and due to the decline of $10.3 million in real estate and construction loans during the first nine months ended September 30, 2007. During the last quarter of 2007, real estate and construction loans increased approximately $6.0 million however; year to date gross loans have decreased $3.1 million or 1.8%.

The following table summarizes the allocation of the allowance for loan losses by type for the years indicated and the percent loans in each category to total loans:

| | Year Ended December 31 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | 2006 | | 2005 | | 2004 | | 2003 | |
| | (dollars in thousands) | | | | | | | | | |
| | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent |
| Commerical | $ 525 | 22.50% | $ 495 | 21.16% | $ 536 | 22.06% | $ 502 | 25.72% | $ 460 | 27.34% |
| Real Estate - construction | 229 | 28.30% | 126 | 32.14% | 118 | 34.05% | 71 | 23.30% | 55 | 22.82% |
| Real Estate - other | 572 | 48.47% | 362 | 45.77% | 274 | 42.90% | 281 | 49.75% | 224 | 48.36% |
| Consumer | 32 | 0.73% | 38 | 0.93% | 36 | 0.99% | 39 | 1.23% | 155 | 1.48% |
| Unallocated | 315 | n/a | 633 | n/a | 506 | n/a | 307 | n/a | 218 | n/a |
| Total | $ 1,673 | 100.00% | $ 1,654 | 100.00% | $ 1,470 | 100.00% | $ 1,200 | 100.00% | $ 1,112 | 100.00% |

Management views the allowance for loan losses of $1,673,000 or .99% of total loans as of December 31, 2007 to be adequate after considering the above factors. This allowance is compared to $1,654,000 or .96% in 2006 and $1,470,000 or .95% in 2005. However, there can be no assurance that in any given period the Company will not sustain charge-offs that are substantial in relation to the size of the allowance.

The allocation of the allowance for possible loan losses as of the end of the last five fiscal years is summarized in the following table:

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (dollars in thousands) | | | | |
| **Outstanding loans:** | | | | | |
| Average for the year (net) | $ 163,741 | $ 169,139 | $ 145,195 | $ 115,255 | $ 109,148 |
| End of the year (net) | 166,619 | 169,680 | 152,563 | 125,586 | 109,949 |
| Allowance for loan losses: | | | | | |
| Balance at beginning of year | $ 1,654 | $ 1,470 | $ 1,200 | $ 1,112 | $ 1,026 |
| Actual charge-offs: | | | | | |
| Commercial | 51 | 77 | 43 | 22 | 16 |
| Real estate | — | — | — | — | — |
| Consumer | — | — | — | — | — |
| All other (including overdrafts) | 10 | 6 | 3 | 1 | 17 |
| Total charge-offs | 61 | 83 | 46 | 23 | 33 |
| **Less Recoveries:** | | | | | |
| Commercial | 4 | 26 | 15 | — | 4 |
| Real estate | 76 | — | — | — | — |
| Consumer | — | — | — | — | — |

| | | | | | |
|---|---|---|---|---|---|
| All other (including overdrafts) | — | 1 | 1 | 1 | — |
| Total recoveries | 80 | 27 | 16 | 1 | 4 |
| Net loan charge-offs (recoveries) | (19) | 56 | 30 | 22 | 29 |
| Provision for loan loss | — | 240 | 300 | 110 | 115 |
| Balance at end of period | $ 1,673 | $ 1,654 | $ 1,470 | $ 1,200 | $ 1,112 |
| **Ratios:** | | | | | |
| Net loan charge-offs (recoveries) to average loans | -0.01% | 0.03% | 0.02% | 0.02% | 0.03% |
| Allowance for loan losses to end of year loans | 0.99% | 0.96% | 0.95% | 0.94% | 1.00% |
| Net loan charge-offs (recoveries) to allowance for loan losses | -1.14% | 3.39% | 2.04% | 1.83% | 2.61% |
| Net loan charge-offs (recoveries) to provision charged to operating expense | 0.00% | 23.33% | 10.00% | 20.00% | 25.22% |

***Investment Securities***

The average balance of Federal Funds Sold (overnight investments with other banks) was $4,954,000 in 2007, $2,941,000 in 2006, and $5,685,000 in 2005. These investments are maintained primarily for the short-term liquidity needs of the Company. The major factors influencing the levels of required liquidity are the loan demand of the Company's customers and fluctuations in the Company's deposits. The Company's loan-to-deposit ratio averaged 76.1% in 2007, compared to 79.7% in 2006, and 69.9% in 2005.

Average total investment securities increased by $10,451,000 or 27.1% during 2007, compared to a decrease of $10,087,000 or 20.7% in 2006. The Company focused on maximizing investment opportunities during 2007, due to the softening of the loan demand which decreased by $7,105,000 in average loans or 4.2%. The aggregate market value of the investment portfolio was $334,000 over the amortized cost as of December 31, 2007. As of December 31, 2007, the Company had the ability and intent to hold securities to maturity and saw a significant market value increase of $796,000 over 2006. It is the Company's policy not to engage in securities trading transactions. There are no investments in the portfolio deemed to be permanently impaired. The Company has classified all of its investment securities as available for sale. The exposure to sub prime loans in the Mortgage-Backed securities portfolio is minimal due to the fact these securities are guaranteed by United States Government Agencies and, as such, can be viewed as having credit risk comparable to United States Treasury securities.

| | December 31 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2007 | | | | 2006 | | | |
| | Amortized Cost | Unrealized Gains | Unrealized (Losses) | Estimated Fair Value | Amortized Cost | Unrealized Gains | Unrealized (Losses) | Estimated Fair Value |
| Securities available for sale: | | | | | | | | |
| U.S. Government and Agency securities | $24,097,314 | $243,699 | $ — | $24,341,013 | $19,094,065 | $ 3,029 | $ (76,599) | $19,020,495 |
| State and Political Subdivisions | $ 6,527,226 | $ 30,399 | $ (50,333) | $ 6,507,292 | $ 4,805,053 | $ 9,970 | $ (89,397) | $ 4,725,626 |
| Mortgage-Backed Securities | $25,148,131 | $207,770 | $ (97,050) | $25,258,851 | $19,340,821 | $ 20,303 | $(328,828) | $19,032,296 |
| Total | $55,772,671 | $481,868 | $(147,383) | $56,107,156 | $43,239,939 | $ 33,302 | $(494,824) | $42,778,417 |

The amortized cost, estimated fair value, and weighted average yield for investment securities available for sale based on maturity date are set forth in the table below. The weighted average yield is based on the amortized cost of the securities using a method that approximates the level yield method:

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | |
| | Book Value | Market Value | Weighted Average Yield | Book Value | Market Value | Weighted Average Yield |
| **Available-for-Sale Securities:** | | | | | | |
| U.S. Government and Agency Securities | | | | | | |
| One Year or Less | 8,002,724 | 8,026,354 | 5.27% | 8,998,769 | 8,924,794 | 3.59% |
| One to Five Years | 14,094,590 | 14,310,616 | 5.07% | 8,095,296 | 8,095,701 | 5.03% |
| Five to Ten Years | 2,000,000 | 2,004,043 | 5.00% | 2,000,000 | 2,000,000 | 5.10% |
| Over Ten Years | — | — | | — | — | |
| Total U.S. Agency | 24,097,314 | 24,341,013 | 5.13% | 19,094,065 | 19,020,495 | 4.36% |
| **State and Political Subdivisions:** | | | | | | |
| One Year or Less | 1,061,296 | 1,070,745 | 6.23% | 708,100 | 702,151 | 4.36% |
| One to Five Years | 3,020,931 | 2,998,510 | 4.99% | 3,859,382 | 3,790,725 | 5.20% |
| Five to Ten Years | 2,444,999 | 2,438,037 | 6.26% | 237,571 | 232,750 | 5.74% |
| Over Ten Years | — | — | | — | — | |
| Total State & Political | 6,527,226 | 6,507,292 | 5.67% | 4,805,053 | 4,725,626 | 5.10% |

| | | | | | | |
|---|---|---|---|---|---|---|
| Subdivisions | | | | | | |
| **Mortgage Backed Securities:** | | | | | | |
| One Year or Less | 3,430,820 | 3,441,374 | 4.70% | 3,650,978 | 3,590,877 | 4.26% |
| One to Five Years | 14,849,863 | 14,894,034 | 4.66% | 11,261,147 | 11,033,390 | 4.20% |
| Five to Ten Years | 3,869,173 | 3,907,814 | 5.05% | 2,711,676 | 2,695,483 | 4.63% |
| Over Ten Years | 2,998,275 | 3,015,629 | 4.90% | 1,717,020 | 1,712,546 | 4.71% |
| Total Mortgage Backed Securities | 25,148,131 | 25,258,851 | 4.75% | 19,340,821 | 19,032,296 | 4.32% |
| Total Available-for-Sale Securities | $55,772,671 | $56,107,156 | 5.02% | $43,239,939 | $42,778,417 | 4.42% |

### *Deposits*

Total average deposits increased $3,020,000 or 1.4% during 2007, compared to an increase of $4,391,000 or 2.1% in 2006 and an increase of $24,109,000 or 13.1% in 2005. Average noninterest-bearing deposits decreased $7,669,000 or 8.6% in 2007, compared to an increase of $1,017,000 or 1.2% in 2006 and an increase of $10,896,000 or 14.1% in 2005. Average interest-bearing deposits increased $10,689,000 or 8.7% in 2007 compared to an increase of $3,374,000 or 2.8% in 2006 and an increase of $13,213,000, or 12.5% in 2005.

The chart below indicates a shift in lower interest-bearing deposits (NOW, Money Market and Savings) to higher interest rate Time Certificates of Deposit. This appears to be a trend that is common throughout the local banking industry and is expected to continue in 2008. This was management's strategy to retain and attract deposits to offset loss of funds to non-bank competition.

The following table summarizes the distribution of average deposits and the average rates paid for the period indicated:

| | December 31 | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2006 | | 2005 | |
| | Average Balance | Average Rate | Average Balance | Average Rate | Average Balance | Average Rate |
| | (dollars in thousands) | | | | | |
| Noninterest-bearing demand deposits | $ 81,714 | | $ 89,383 | | $ 88,366 | |
| Money Market Accounts | 24,929 | 2.90% | 24,103 | 2.09% | 30,186 | 1.48% |
| NOW accounts | 13,391 | 0.41% | 14,696 | 0.26% | 17,834 | 0.24% |
| Savings deposits | 27,076 | 1.07% | 28,074 | 0.79% | 30,560 | 0.44% |
| Time deposits of $100,000 or more | 39,242 | 4.67% | 29,800 | 4.21% | 19,859 | 2.93% |
| Other time deposits | 28,777 | 4.60% | 26,053 | 4.08% | 20,913 | 2.94% |
| Total deposits | $215,129 | 1.96% | $212,109 | 1.45% | $207,718 | 0.87% |

The remaining maturities of the Company's certificates of deposit in the amount of $100,000 or more as of December 31, 2007 are indicated in the table below. Interest expense on these certificates of deposit totaled $1,834,000 in 2007:

| Deposits Maturing in | December 31, 2007 |
|---|---|
| Three months or less | $ 15,967,166 |
| Over three months through six months | 10,750,684 |
| Over six months through twelve months | 8,958,008 |
| Over twelve months | 3,153,935 |
| Total | $ 38,829,793 |

### *Capital*

The Bank is required to maintain a minimum leverage-capital ratio of Tier I (as defined) to total assets based on the Bank's ratings under the regulatory rating system. At the end of 2007, all Bank capital ratios were above all current Federal capital guidelines for a "well capitalized" bank. As of December 31, 2007 the regulatory total capital to risk-weighted assets ratio was 13.8% compared to 13.1% as of December 31, 2006 and 11.3% as of December 31, 2005. The regulatory Tier I capital to risk-weighted assets ratio was 12.3% on December 31, 2007 compared to 11.4% on December 31, 2006 and 9.3% as of December 31, 2005. The regulatory Tier I capital to average assets ratio was 9.9% as of December 31, 2007 compared to 9.1% as of December 31, 2006 and 7.2% as of December 31, 2005.

The Bank's Tier I Capital ratio increased 74 basis points and the Bank's Total Capital to Risk Weighted Assets ratio increased 67 basis points, due to the strong earnings of $3.2 million for 2007.

### *Short-term Borrowings*

The Bank has two borrowing arrangements with the Federal Home Loan Bank of San Francisco. The first allows the Bank to borrow up to approximately $41 million against which the Bank has pledged approximately $100 million of its real estate secured loans. The second arrangement allows the Bank to borrow up to approximately $12 million against which the Bank has pledged approximately $12 million of its investment securities.

As of December 31, 2007 the Bank has borrowed $5,900,000 under these arrangements. This amount is due on January 2, 2008 and includes interest at 3.25%. During 2007 the bank had average borrowings outstanding of $1,100,000 at an effective rate of 4.55%.

### *Long-term Borrowings*

Santa Lucia Bancorp issued $5,155,000 in junior subordinated debt securities (the “debt securities”) to the Santa Lucia Bancorp (CA) Capital Trust, a statutory trust created under the laws of the State of Delaware. These debt securities are subordinated to effectively all borrowings of the Company and are due and payable on July 7, 2036. These debt securities may be redeemed for 105% of the principal balance through July 7, 2011 and then at par thereafter. Interest is payable quarterly beginning July 7, 2006 at 1.48% over the quarterly adjustable 3-month LIBOR. Of this $5.2 million, the Company contributed $3.0 million to the Bank and retained $2.0 million at the Company level. The securities do not entitle the holders to voting rights in the Company but will contain certain restrictive covenants, including restrictions on the payment of dividends to the holders of the Company’s common stock in the event that interest payments on the trust preferred securities are postponed. The capital received from the trust preferred issuance is designated as Tier 1 capital for regulatory purposes.

During the third quarter of 2003, the Bank undertook and completed a private placement of subordinated debentures (“notes”) to augment its Tier 2 capital. The total principal amount of the notes issued was $2,000,000. The notes were sold pursuant to an applicable exemption from registration under the Securities Act of 1933 to certain accredited investors, including some of the Company’s directors and executive officers. The notes include quarterly payment of interest at prime plus 1.5% and quarterly principal installments of approximately $166,666 commencing on September 30, 2008 until paid in full on June 30, 2011.

### *Interest Rate Sensitivity and Liquidity*

The Company closely follows the maturities and repricing opportunities of both assets and liabilities to reduce gaps in interest spreads. An analysis is performed quarterly to determine the various interest sensitivity gaps that exist. In general, the Company is asset sensitive, meaning that when interest rates change, assets (loans) will reprice faster than short-term liabilities (deposits). Therefore, higher interest rates improve short-term profits and lower rates decrease short-term profits. Currently, management’s analysis indicates that the Company’s asset sensitive position would not materially affect income for interest rate changes of one percent or less in one year.

The following table presents the Bank’s Rate Sensitivity Gap Report as of December 31, 2007.

| | 0-3 months | 3-12 months | 1-3 years | 3-5 years | Beyond | Non-Rate Sensitive | Total |
|---|---|---|---|---|---|---|---|
| | | | (dollars in thousands) | | | | |
| **Interest sensitive assets:** | | | | | | | |
| Investment securities | $ 5,183 | $ 3,857 | $ 17,594 | $ 21,189 | $ 9,405 | $ — | $ 57,228 |
| Loan receivables | 90,316 | 27,823 | 32,983 | 14,578 | 3,268 | — | 168,968 |
| Federal funds sold | — | — | — | — | — | — | — |
| Non-earning assets | — | — | — | — | — | 21,847 | 21,847 |
| **Total assets** | $ 95,499 | $ 31,680 | $ 50,577 | $ 35,767 | $ 12,673 | $ 21,847 | $248,043 |
| **Interest sensitive liabilities:** | | | | | | | |
| Demand deposits | $ — | $ — | $ — | $ — | $ — | $ 76,829 | $ 76,829 |
| NOW accounts | 349 | 1,048 | 2,796 | 2,795 | 5,008 | — | 11,996 |
| Money Market Accounts | 2,522 | 7,565 | 16,811 | — | — | — | 26,898 |
| Savings deposits | 930 | 2,789 | 7,436 | 7,436 | 7,746 | — | 26,337 |
| Time deposits | 26,851 | 37,950 | 6,189 | 705 | 149 | — | 71,844 |
| Total saving and time deposits | $ 30,652 | $ 49,352 | $ 33,232 | $ 10,936 | $ 12,903 | $ 76,829 | $213,904 |
| Short-term borrowing | 5,900 | — | — | — | — | — | 5,900 |
| Long-term borrowing | 2,000 | — | — | — | — | — | 2,000 |
| Non-funding liabilities and capital | — | — | — | — | — | 26,239 | 26,239 |
| Total liabilities and capital | $ 38,552 | $ 49,352 | $ 33,232 | $ 10,936 | $ 12,903 | $103,068 | $248,043 |
| Interest rate sensitivity gap | $ 56,947 | $ (17,672) | $ 17,345 | $ 24,831 | $ (230) | | |
| **Risk Indicators from GAP** | | | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| **Analysis:** | | | | | |
| Cumulative GAP | $ 56,947 | $ 39,275 | $ 56,620 | $ 81,451 | $ 81,221 |
| Cumulative GAP (% of total assets) | 22.96% | 15.83% | 22.83% | 32.84% | 32.74% |

The asset liability reports indicate that the Bank has an actual dollar risk exposure of $574,000 if interest rates fall 100 basis points. This represents a -4.5% risk to interest income.

| | Interest Income and Expense Under Rate Shock | | | | |
|---|---|---|---|---|---|
| | -200bp | -100bp | 0bp | +100bp | +200bp |
| Net Interest Income | | | | | |
| Earnings at Risk | $ (1,088) | $ (574) | $ 0 | $ 471 | $ 931 |
| Percent of Risk | -8.5% | -4.5% | 0.00% | 3.7% | 7.3% |
| Equity Ratio | 14.3% | 15.1% | 16.0% | 16.7% | 17.3% |

The Company closely monitors its liquidity so that the cash requirements for loans and deposit withdrawals are met in an orderly manner. Management monitors liquidity in relation to trends of loans and deposits for short term and long-term requirements. Liquidity sources are cash, deposits with other banks, overnight Federal Fund investments, investment securities and the ability to sell loans. As of December 31, 2007, the Bank’s liquidity ratio was 25.0% compared to 24.5% at December 31, 2006 and 27.7% at December 31, 2005. The 25.0% liquidity ratio at December 31, 2007 is well within the Company’s policy limit.

## Critical Accounting Policies

This discussion should be read in conjunction with the consolidated financial statements of the Company, including the notes thereto.

Our accounting policies are integral to understanding the 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 applied consistently from period to period. In addition, the 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.

### *Use of Estimates in the Preparation of Financial Statements*

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

### *Allowance for Loan Losses*

The allowance for loan losses represents management’s best estimate of losses inherent in the existing loan portfolio. The allowance for loan losses is increased by the provision for loan losses charged to expense and reduced by loans charged off, net of recoveries. The provision for loan losses is determined based on management’s assessment of several factors: reviews and evaluation of specific loans, changes in the nature and volume of the loan portfolio, current economic conditions and the related impact on specific borrowers and industry groups, historical loan loss experiences, the level of classified and nonperforming loans and the results of regulatory examinations.

Loans are considered impaired if, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. The measurement of impaired loans is generally based on the present value of expected future cash flows discounted at the historical effective interest rate stipulated in the loan agreement, except that all collateral-dependent loans are measured for impairment based on the fair value of the collateral. In measuring the fair value of the collateral, management uses assumptions and methodologies consistent with those that would be utilized by unrelated third parties.

Changes in the financial condition of individual borrowers, in economic conditions, in historical loss experience and in the condition of the various markets in which collateral may be sold may all affect the required level of the allowance for loan losses and the associated provision for loan losses.

***Available-for-Sale Securities***

The fair value of most securities classified as available-for-sale are based on quoted market prices. If quoted market prices are not available, fair values are extrapolated from the quoted prices of similar instruments.

### *Deferred Tax Assets*

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.

### *Deferred Compensation Liabilities*

Management estimates the life expectancy of the participants and the accrual methods used to accrue compensation expense. If individuals outlive their assumed expectancies the amounts accrued for the payment of their benefits will be inadequate and additional changes to income will be required.

## Availability of Form 10-KSB

If any shareholder would like a copy of the Company's Annual Report on Form 10-KSB for the fiscal year ending December 31, 2007, they can be obtained without charge by sending a written request to John C. Hansen, Executive Vice President and Chief Financial Officer, P. O. Box 6047, Atascadero, California 93423.

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders
Santa Lucia Bancorp and Subsidiary

We have audited the consolidated balance sheets of Santa Lucia Bancorp and Subsidiary (the Company) as of December 31, 2007 and 2006, and the related consolidated statements of earnings, cash flows and shareholders' equity for the three years ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Santa Lucia Bancorp and Subsidiary as of December 31, 2007 and 2006, and the results of its operations and cash flows for the three years ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.

Laguna Hills, California
January 16, 2008

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**Santa Lucia Bancorp and Subsidiary**
**Consolidated Balance Sheets**

*December 31, 2007 and 2006*

| | 2007 | 2006 |
|---|---|---|
| **ASSETS** | | |
| Cash and due from banks | $ 7,399,412 | $ 10,139,526 |
| Federal funds sold | — | — |
| TOTAL CASH AND CASH EQUIVALENTS | 7,399,412 | 10,139,526 |
| Securities available for sale | 56,107,156 | 42,778,417 |
| Loans, net | 166,619,494 | 169,680,473 |
| Premises and equipment, net | 8,868,507 | 9,258,207 |
| Deferred income tax assets | 814,000 | 941,000 |
| Cash surrender value of life insurance | 5,005,357 | 3,336,076 |
| Federal Reserve Bank and Federal Home Loan Bank stock, at cost | 1,453,850 | 1,397,700 |
| Accrued interest and other assets | 2,371,999 | 3,206,685 |
| TOTAL ASSETS | $ 248,639,775 | $ 240,738,084 |

| | 2007 | 2006 |
|---|---|---|
| **LIABILITIES & SHAREHOLDERS' EQUITY** | | |
| Deposits | | |
| Noninterest-bearing demand | $ 77,100,561 | $ 86,252,426 |
| Interest-bearing demand and NOW accounts | 11,996,402 | 12,968,951 |
| Money market | 25,440,394 | 20,465,756 |
| Savings | 26,336,827 | 27,383,605 |
| Time certificates of deposit of $100,000 or more | 38,829,793 | 37,226,189 |
| Other time certificates | 33,014,401 | 28,691,525 |
| TOTAL DEPOSITS | 212,718,378 | 212,988,452 |
| Short-term borrowings | 5,900,000 | — |
| Long-term borrowings | 7,155,000 | 7,155,000 |
| Accrued interest and other liabilities | 1,677,551 | 1,457,716 |
| TOTAL LIABILITIES | 227,450,929 | 221,601,168 |
| *Commitments and contingencies (Note M)* | — | _ |
| Shareholders' equity | | |
| Common stock – no par value; 20,000,000 shares authorized; issued and outstanding: 1,924,873 shares at December 31, 2007 and 1,928,097 shares at December 31, 2006 | 9,851,392 | 9,566,563 |
| Additional paid-in capital | 358,203 | 216,558 |
| Retained earnings | 10,782,741 | 9,624,939 |
| Accumulated other comprehensive income-net unrealized losses on available-for-sale securities, net of taxes of $137,975 in 2007 and $190,378 in 2006 | 196,510 | (271,144) |
| TOTAL SHAREHOLDERS' EQUITY | 21,188,846 | 19,136,916 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | $ 248,639,775 | $ 240,738,084 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statements of Earnings**

*Years Ended December 31, 2007, 2006 and 2005*

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Interest income | | | |
| Interest and fees on loans | $ 15,030,928 | $ 15,397,450 | $ 11,747,437 |
| Federal funds sold | 249,434 | 145,314 | 173,515 |
| Investment securities – taxable | 2,232,966 | 1,352,675 | 1,476,915 |
| Investment securities – nontaxable | 205,285 | 131,233 | 148,368 |
| | 17,718,613 | 17,026,672 | 13,546,235 |
| Interest expense | | | |
| Time certificates of deposit of $100,000 or more | 1,833,831 | 1,254,951 | 581,566 |
| Other deposits | 2,389,580 | 1,824,577 | 1,234,377 |
| Long-term debt and other borrowings | 600,727 | 497,610 | 167,979 |
| | 4,824,138 | 3,577,138 | 1,983,922 |
| Net interest income | 12,894,475 | 13,449,534 | 11,562,313 |
| Provision for loan losses | — | 240,000 | 300,000 |
| Net interest income after provision for loan losses | 12,894,475 | 13,209,534 | 11,262,313 |
| Noninterest income | | | |
| Service charges and fees | 583,445 | 615,917 | 602,809 |
| Dividends on cash surrender value of life insurance | 222,071 | 138,181 | 132,319 |
| Mortgage fees | — | 48,487 | 94,972 |
| Gain (loss) on sale of investment securities | — | — | (5,877) |
| Other income | 265,798 | 207,676 | 227,727 |
| | 1,071,314 | 1,010,261 | 1,051,950 |
| Noninterest expense | | | |
| Salaries and employee benefits | 5,259,456 | 4,743,094 | 4,241,897 |
| Occupancy | 627,685 | 664,482 | 565,467 |
| Equipment | 666,003 | 691,028 | 583,772 |
| Professional services | 426,667 | 538,282 | 465,661 |
| Data processing | 488,636 | 468,211 | 439,591 |
| Office expenses | 362,057 | 359,588 | 374,478 |
| Marketing | 422,914 | 407,638 | 397,907 |
| Regulatory assessments | 64,436 | 63,851 | 65,793 |
| Directors' fees and expenses | 328,801 | 263,444 | 261,338 |
| Messenger and courier expenses | 156,870 | 148,335 | 143,834 |
| Other | 225,445 | 241,571 | 268,705 |
| | 9,028,970 | 8,589,524 | 7,808,443 |
| Earnings before income taxes | 4,936,819 | 5,630,271 | 4,505,820 |
| Income taxes | 1,934,000 | 2,242,000 | 1,759,000 |
| Net earnings | $ 3,002,819 | $ 3,388,271 | $ 2,746,820 |
| Per share data: | | | |
| Net earnings – basic | $ 1.55 | $ 1.77 | $ 1.46 |
| Net earnings – diluted | $ 1.51 | $ 1.68 | $ 1.38 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statements of Cash Flows**

*Years Ended December 31, 2007, 2006 and 2005*

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Net earnings | $ 3,002,819 | $ 3,388,271 | $ 2,746,820 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | | |
| Depreciation and amortization | 652,290 | 669,159 | 556,907 |
| Provision for loan losses | — | 240,000 | 300,000 |
| Amortization of investment securities | — | 5,450 | 32,240 |
| Loss (gain) on sale of investment securities | — | — | 5,877 |
| Deferred income taxes | (201,000) | (147,000) | (25,000) |
| Dividends in cash value of life insurance | (222,071) | (138,181) | (132,319) |
| Other items, net | 1,101,676 | (1,131,715) | (432,992) |
| Net cash provided by operating activities | 4,333,714 | 2,885,984 | 3,051,533 |
| Cash flows from investing activities: | | | |
| Proceeds from maturities of investment securities | 14,202,010 | 18,962,594 | 11,007,571 |
| Proceeds from sale of investment securities | — | — | 6,016,550 |
| Purchases of investment securities | (26,658,965) | (19,391,969) | (2,001,378) |
| Purchase of Federal Reserve Bank and Federal Home Loan Bank stock | — | (155,550) | (194,450) |
| Net change in loans | 3,060,979 | (17,357,365) | (27,277,292) |
| Purchases of bank premises and equipment | (262,590) | (466,782) | (347,532) |
| Proceeds from sale of bank premises and equipment | | — | — |
| Proceeds from (purchase of) life insurance | (1,485,000) | — | 132,255 |
| Proceeds from sale of other real estate owned | — | — | — |
| Net cash used in investing activities | (11,143,566) | (18,409,072) | (12,664,276) |
| Cash flows from financing activities: | | | |
| Net change in deposits | (270,074) | 6,109,373 | 12,011,229 |
| Proceeds and tax benefit from exercise of stock options | 164,275 | 372,781 | 416,562 |
| Stock repurchases | (853,351) | — | — |
| Net (repayments) proceeds from borrowings | 5,900,000 | (345,000) | 5,500,000 |
| Cash dividends paid | (871,112) | (767,587) | (729,550) |
| Net cash provided by financing activities | 4,069,738 | 5,369,567 | 17,198,241 |
| Net increase (decrease) in cash and cash equivalents | (2,740,114) | (10,153,521) | 7,585,498 |
| Cash and cash equivalents at beginning of year | 10,139,526 | 20,293,047 | 12,707,549 |
| Cash and cash equivalents at end of year | $ 7,399,412 | $ 10,139,526 | $ 20,293,047 |
| Supplemental disclosure of cash flow information: | | | |
| Interest paid | $ 4,824,138 | $ 3,415,383 | $ 1,957,610 |
| Income taxes paid | $ 1,865,000 | $ 2,415,000 | $ 1,720,000 |
| Cashless exercise of stock options | $ 120,554 | $ 48,034 | $ 32,515 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statement of Shareholders' Equity**

*Years Ended December 31, 2007, 2006 and 2005*

| | Comprehensive Income | Common Stock Shares Outstanding | Common Stock Amount | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2005** | | $1,861,764 | $8,849,671 | $ — | $ 5,067,534 | $ (110,291) |
| Cash dividends – $0.3875 per share | | | | | (729,550) | |
| Exercise of stock options, including the realization of tax benefits of $226,000 | | 37,779 | 449,077 | | (32,515) | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 2,746,820 | | | | 2,746,820 | |
| Change in unrealized loss on available-for-sale securities, net of taxes of $265,409 | (378,040) | | | | | (378,040) |
| Less reclassification adjustments for gains included in the net income, net of taxes or $2,410 | 3,467 | | | | | 3,467 |
| **Total Comprehensive Income** | $ 2,372,247 | | | | | |
| **Balance at December 31, 2005** | | 1,899,543 | 9,298,748 | — | 7,052,289 | (484,864) |
| Cash dividends – $0.40 per share | | | | | (767,587) | |
| Exercise of stock options, including the realization of tax benefits of $153,000 | | 28,554 | 267,815 | 153,000 | (48,034) | |
| Stock Option Compensation Expense | | | | 63,558 | | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 3,388,271 | | | | 3,388,271 | |
| Change in unrealized loss on available-for-sale securities, net of taxes or $150,059 | 213,720 | | | | | 213,720 |
| **Total Comprehensive Income** | $ 3,601,991 | | | | | |
| **Balance at December 31, 2006** | | 1,928,097 | $9,566,563 | 216,558 | 9,624,939 | (271,144) |
| Cash dividends – $0.45 per share | | | | | (871,112) | |
| Exercise of stock options, including the realization of tax benefits of $19,000 | | 29,247 | 284,829 | 19,000 | (120,554) | |
| Repurchase and retirement of stock | | (32,471) | | | (853,351) | |
| Stock Option Compensation Expense | | | | 122,645 | | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 3,002,819 | | | | 3,002,819 | |
| Change in unrealized loss on available-for-sale securities, net of taxes of $328,353 | 467,654 | | | | | 467,654 |
| **Total Comprehensive** | $ 3,470,473 | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Income | | | | | | |
| **Balance at December 31, 2007** | | 1,924,873 | $9,851,392 | $358,203 | $10,782,741 | $ 196,510 |

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

**NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES –** The consolidated financial statements include the accounts of Santa Lucia Bancorp and its wholly owned subsidiary Santa Lucia Bank (the “Bank”), collectively referred to herein as the “Company.” All significant intercompany transactions have been eliminated.

The accounting and reporting policies of the Company are in accordance with accounting principles generally accepted in the Unites States of America and prevailing practices within the banking industry. A summary of the significant accounting policies consistently applied in preparation of the accompanying financial statements follows:

**Nature of Operations –** The Company has been organized as a single operating segment and maintains four branches in the San Luis Obispo and northern Santa Barbara Counties. The Company’s primary source of revenue is interest income from loans to customers. The Company’s customers are predominantly small and middle-market businesses and individuals.

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

**Presentation of Cash Flows –** For the purposes of reporting cash flows, cash and cash equivalents includes cash, noninterest-earning deposits and federal funds sold. Generally, federal funds are sold for one day periods.

**Cash and Due From Banks –** Banking regulations require that all banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Bank was in compliance with the reserve requirements as of December 31, 2007 and 2006.

The Company periodically maintains amounts due from banks that exceed federally insured limits. The Company has not experienced any losses in such accounts.

**Investment Securities –** Bonds, notes, and debentures for which the Company has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity.

Investments not classified as trading securities nor as held-to-maturity securities are classified as available-for-sale securities and recorded at fair value. Unrealized gains or losses on available-for-sale securities are excluded from net income and reported as an amount net of taxes as a separate component of other comprehensive income included in shareholders’ equity. Premiums or discounts on held-to-maturity and available-for-sale securities are amortized or accreted into income using the interest method. Realized gains or losses on sales of held-tomaturity or available-for-sale securities are recorded using the specific identification method.

Declines in the fair value of individual held-to-maturity and availablefor-sale securities below their cost that are other-than-temporary result in write-downs of the individual securities to their fair value. The related write-downs are included in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

**Provision and Allowance for Loan Losses –** The determination of the balance in the allowance for loan losses is based on an analysis of the loan portfolio and reflects an amount which, in management's judgment, is adequate to provide for potential credit losses after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience and such other factors as deserve current recognition in estimating credit losses. The provision for loan losses is charged to expenses.

The Company considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Measurement of impairment is based on the expected future cash flows of an impaired loan, which are to be discounted at the loan's effective interest rate, or measured by reference to an observable market value, if one exists, or the fair value of the collateral for a collateral-dependent loan. The Company selects the measurement method on a loan-by-loan basis except that collateral-dependent loans for which foreclosure is probable are measured at the fair value of the collateral. The Company recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans.

**Interest and Fees on Loans –** Interest income is accrued daily as earned on all 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 based on contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectibility. 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. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to all principal and interest. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan.

**Premises and Equipment –** Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives, which ranges from three to ten years for furniture and fixtures and forty years for buildings. Expenditures for betterments or major repairs are capitalized and those for ordinary repairs and maintenance are charged to operations as incurred.

**Other Real Estate Owned –** Other real estate owned represents real estate acquired through foreclosure and is carried at the lower of the recorded investment in the property or its fair value. Prior to foreclosure, the value of the underlying loan is written down to the fair market value of the real estate to be acquired by a charge to the allowance for credit losses, if necessary. Any subsequent write-downs are charged against operating expenses. Operating expenses of such properties, net of related income, are included in other expenses.

**Income Taxes –** Deferred income taxes are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Realization of tax benefits of deductible temporary differences and operating loss carryforwards depends on having sufficient taxable income of an appropriate character within the carryforward periods.

The Company has adopted Financial Accounting Standards Interpretation No. 48 ("Fin 48"), Accounting for Uncertainty in Income Taxes. Fin 48 clarifies the accounting for uncertainty in tax positions taken or expected to be taken on a tax return and provides that the tax effects from an uncertain tax position can be recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Management believes that all tax positions taken to date are highly certain and, accordingly, no accounting adjustment has been made to the financial statements. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

**Advertising Costs –** The Company expenses the costs of advertising in the period incurred.

**Comprehensive Income –** Beginning in 1998, the Company adopted Statement of Financial Accounting Standard ("SFAS") No. 130, *"Reporting Comprehensive Income*" (SFAS No. 130), which requires the disclosure of comprehensive income and its components. Changes in unrealized gain or loss on available-for-sale securities net of income taxes is the only component of accumulated other comprehensive income for the Company.

**Financial Instruments –** In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit as described in Note M. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

**Earnings Per Shares (EPS) –** 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 shared in the earnings of the entity.

**Stock-Based Compensation –** The Company has adopted SFAS No. 123(R) "Shared-Based Payment." This Statement generally requires entities to recognize the cost of employee services received in exchange for awards of stock options, or other equity instruments, based on the grant-date fair value of those awards. This cost is recognized over the period which an employee is required to provide services in exchange for the award, generally the vesting period.

**Change in Accounting Principle –** The Company adopted SFAS No. 123 (R) on January 1, 2006 using the "modified prospective method." Under this method compensation expense is recognized using the fair-value method for all new stock option awards as well as any existing awards that are modified, repurchased or cancelled after January 1, 2006 and prior periods are not restated. In addition, the unvested portion of previously awarded options outstanding as of January 1, 2006 will also be recognized as expense over the requisite service period based on the fair value of those options as previously calculated at the grant date under the pro-forma disclosures of SFAS No. 123. The fair value of each grant is estimated using the Black-Scholes option pricing model. During 2007 and 2006 the Company recognized pre-tax stock-based compensation expense of $122,645 and $63,558, respectively, as a result of adopting SFAS No. 123 (R).

Prior to the adoption of SFAS No. 123 (R), the Company accounted for stock-based awards using the intrinsic value method prescribed in Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Accordingly, compensation cost for stock options was measured as the excess, if any, of the quoted market price of the Company's stock at the date of the grant over the amount an employee must pay to acquire the stock. All of the Company's stock option grants included exercise prices equal to the Company’s current market price per share; accordingly, no compensation expense was reported using the intrinsic value method of APB Opinion No. 25.

Had compensation cost for the Company’s stock option plans been determined based on the fair value at the grant dates for awards under those plans consistent with the method of SFAS No. 123, the Company’s net income and income per share for 2005 would have changed to the pro forma amounts indicated below:

| | | 2005 |
|---|---|---|
| Net income: | | |
| As reported | $ | 2,746,820 |
| Stock-Based Compensation using the Intrinsic Value Method | | — |
| Stock-Based Compensation that would have been reported using the Fair Value Method of SFAS 123 | | (43,436) |
| Pro Forma | $ | 2,703,384 |
| Per share: | | |
| Net Income - Basic | | |
| As Reported | $ | 1.46 |
| Pro Forma | $ | 1.44 |
| Net Income - Diluted | | |
| As Reported | $ | 1.38 |
| Pro Forma | $ | 1.36 |

**Disclosure about Fair Value of Financial Instruments –** SFAS No. 107 specifies the disclosure of the estimated fair value of financial instruments. The Company’s estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies.

However, considerable judgment is required to develop the estimates of fair value. Accordingly, the estimates are not necessarily indicative of the amounts the Company could have realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since the balance sheet date and, therefore, current estimates of fair value may differ significantly from the amounts presented in the accompanying notes.

**New Accounting Pronouncements –** In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements”, effective for the Company January 1, 2008. This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This Statement defines fair value, establishes a fair value hierarchy that distinguishes between valuations obtained from sources independent of the entity and those from the entity’s own observable inputs that are not corroborated by observable market data. SFAS No. 157 expands disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value, and for recurring fair value measurements using significant unobservable inputs, the effect of the measurements on earnings or changes inn net assets for the period. The Company is currently assessing the impact of this pronouncement on its financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115. SFAS 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS 159 are elective; however, the amendments to SFAS 115, Accounting for Certain Investments in Debt and Equity Securities, applies to all entities with available-for-sale or trading securities. For financial instruments elected to be accounted for at fair value, an entity will report the unrealized gains and losses in earnings. SFAS 159 is effective as the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company is currently assessing the impact of this pronouncement on its financial statements.

In September 2006, the FASB ratified the FASB's Emerging Issues Task Force (or EITF) consensus on EITF Issue No. 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements" and in March 2007 the FASB ratified EITF Issue No. 06-10, "Accounting for Collateral Assignment Split-Dollar Life Insurance Arrangements" The EITF's consensus on both of these issues focuses on the accounting for arrangements in which a company has agreed to share a portion of the value of the insurance policy with the employee. These arrangements are referred to as "split-dollar" arrangements. Entities with split-dollar life insurance policies will have to accrue, for years beginning after December 15, 2007, liabilities and associated expense for those insurance benefits under the same rules that apply when such benefits are provided by means other than life insurance. The provisions of the consensus would be applied through a cumulative effect adjustment to retained earnings with the option of retrospective application. The Company has estimated the charged to retained earnings effective January 1, 2008 to be approximately $196,000 net of taxes.

**Reclassification –** Certain reclassifications have been made in the 2006 and 2005 financial statements to conform to the presentation used in 2007. These reclassifications had no impact on the Company's previously reported financial statements.

**NOTE B – INVESTMENT SECURITIES –** The amortized cost, carrying value and estimated fair values of investment securities available for sale as of December 31, are as follows:

| | **December 31, 2007** | | | |
|---|---|---|---|---|
| | **Amortized cost** | **Unrealized gains** | **Unrealized (losses)** | **Estimated fair value** |
| U.S. Government and Agency Securities | $ 24,097,314 | $ 243,699 | $ — | $ 24,341,013 |
| States and Political Subdivisions | 6,527,226 | 30,399 | (50,333) | 6,507,292 |
| Mortgage-Backed Securities | 25,148,131 | 207,770 | (97,050) | 25,258,851 |
| | $ 55,772,671 | $ 481,868 | $ (147,383) | $ 56,107,156 |

| | **December 31, 2006** | | | |
|---|---|---|---|---|
| | **Amortized cost** | **Unrealized gains** | **Unrealized (losses)** | **Estimated fair value** |
| U.S. Government and Agency Securities | $ 19,094,065 | $ 3,029 | $ (76,599) | $ 19,020,495 |
| States and Political Subdivisions | 4,805,053 | 9,970 | (89,397) | 4,725,626 |
| Mortgage-Backed Securities | 19,340,821 | 20,303 | (328,828) | 19,032,296 |
| | $ 43,239,939 | $ 33,302 | $ (494,824) | $ 42,778,417 |

The carrying value of investment securities pledged to secure public funds, borrowings and for other purposes as required or permitted by law amounts to approximately $14,025,000 and $14,316,000 at December 31, 2007 and 2006, respectively. During 2007 and 2006 the Bank had no proceeds from the sale of available for sale securities. During 2005 the Bank had proceeds from the sale of available for sale securities of $6,016,550, gross gains of $1,298 and gross losses of $7,175.

The amortized cost and estimated fair value of debt securities at December 31, 2007, by contractual maturity, are shown below. Mortgage-backed securities are classified in accordance with their estimated lives. Expected maturities may differ from contractual maturities because borrowers may have the right to prepay obligations.

| | **Amortized** | **Estimated** |
|---|---|---|

| | cost | fair value |
|---|---|---|
| Securities available-for-sale: | | |
| Due in one year or less | $ 12,494,840 | $ 12,538,473 |
| Due after one year through five years | 31,965,384 | 32,203,159 |
| Due after five years through ten years | 8,314,172 | 8,349,895 |
| Due after ten years | 2,998,275 | 3,015,629 |
| | $ 55,772,671 | $ 56,107,156 |

The gross unrealized loss and related estimated fair value of investment securities that have been in a continuous loss position for less than twelve months and over twelve months at December 31, are as follows:

| | Less than Twelve Months | | Over Twelve Months | | Total | |
|---|---|---|---|---|---|---|
| | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value |
| December 31, 2007: | | | | | | |
| U.S. Government & Agency Securities | $ — | $ — | $ — | $ — | $ — | $ — |
| States and Political Subdivisions | (22,168) | 968,403 | (28,165) | 2,224,642 | (50,333) | 3,193,045 |
| Mortgage-Backed Securities | (4,626) | 2,971,470 | (92,424) | 7,118,850 | (97,050) | 10,090,320 |
| | $ (26,794) | $ 3,939,873 | $ (120,589) | $ 9,343,492 | $ (147,383) | $13,283,365 |

| | Less than Twelve Months | | Over Twelve Months | | Total | |
|---|---|---|---|---|---|---|
| | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value |
| December 31, 2006: | | | | | | |
| U.S. Government & Agency Securities | $ (2,954) | $ 4,000,971 | $ (73,645) | $ 6,924,317 | $ (76,599) | $10,925,288 |
| States and Political Subdivisions | (493) | 352,419 | (88,905) | 3,587,649 | (89,398) | 3,940,068 |
| Mortgage-Backed Securities | — | — | (328,827) | 12,473,837 | (328,827) | 12,473,837 |
| | $ (3,447) | $ 4,353,390 | $ (491,377) | $22,985,803 | $ (494,824) | $27,339,193 |

As of December 31, 2007, the Company has 21 investment securities where estimated fair market value had decreased 1.13% from amortized cost. Management evaluates investment securities for other-than-temporary impairment taking into consideration the extent and length of time the fair value has been less than cost, the financial condition of the issuer and whether the Bank has the intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. As of December 31, 2007, no declines are deemed to be other than temporary.

**NOTE C – LOANS –** The Bank's loan portfolio consists primarily of loans to borrowers within San Luis Obispo and northern Santa Barbara Counties, California. Although the Bank seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, real estate and real estate associated businesses are among the principal industries in the Bank's market areas. As a result, the Bank's loan and collateral portfolios are, to some degree, concentrated in those industries.

The composition of the loan portfolio at December 31, is as follows:

| | 2007 | 2006 |
|---|---|---|
| Real estate – construction | $ 47,819,615 | $ 55,307,210 |
| Real estate – other | 81,895,109 | 78,757,513 |
| Commercial | 38,016,713 | 36,406,663 |
| Consumer | 1,237,325 | 1,603,836 |
| | 168,968,762 | 172,075,222 |
| Deferred loan fees | (675,858) | (741,054) |
| Allowance for loan losses | (1,673,410) | (1,653,695) |
| | $ 166,619,494 | $ 169,680,473 |

The allowance for loan losses is increased by the provision to income and decreased by net charge-offs. Management's periodic evaluation of the adequacy of the allowance is based on the Company's past loan experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and current economic conditions.

Transactions in the allowance for credit losses are summarized as follows:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Balance at beginning of year | $ 1,653,695 | $ 1,470,261 | $ 1,200,036 |
| Provision charged to expense | — | 240,000 | 300,000 |
| Loans charged off | (60,779) | (84,002) | (46,355) |
| Recoveries on loans previously charged off | 80,494 | 27,436 | 16,580 |
| Balance at end of year | $ 1,673,410 | $ 1,653,695 | $ 1,470,261 |

The following is a summary of the investment in impaired loans, the related allowance for loan losses, income recognized and information pertaining to nonaccrual and past due loans as of December 31:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Recorded investment in impaired loans | $ 2,175,694 | $ — | $ 134,872 |
| Related allowance for loan losses | $ 144,000 | $ — | $ — |
| Average recorded investment in impaired loans | $ 591,000 | $ 250,000 | $ 459,000 |
| Interest income recognized for cash payments | $ — | $ 3,045 | $ 28,581 |
| Total nonaccrual loans | $ 2,175,694 | $ — | $ 134,872 |
| Total loans past-due ninety days or more and still accruing | $ — | $ 550,000 | $ — |

**NOTE D – RELATED PARTY TRANSACTIONS –** In the ordinary course of business, the Bank has granted loans to certain executive officers, directors and the businesses with which they are associated. All such loans and commitments to lend were made under terms which are consistent with the Bank's normal lending policies.

The following is an analysis of the activity of all such loans:

| | 2007 | 2006 |
|---|---|---|
| Beginning balance | $ 3,734,153) | $ 2,976,502) |
| Credits granted, including renewals | 5,515,322) | 2,797,483) |
| Repayments | (4,484,643) | (2,039,832) |
| | $ 4,764,832) | $ 3,734,153) |

Undisbursed loans amount to approximately $894,712 and $2,337,163 at December 31, 2007 and 2006, respectively.

Deposits from related parties held by the Bank at December 31, 2007 and 2006 amounted to $2,367,291 and $3,323,903, respectively.

**NOTE E – PREMISES AND EQUIPMENT –** The composition of premises and equipment at December 31 is as follows:

| | 2007 | 2006 |
|---|---|---|
| Premises | $ 7,497,978 | $ 7,411,967 |
| Furniture, fixtures and equipment | 3,990,273 | 4,149,808 |
| | 11,488,251 | 11,561,775 |
| Less accumulated depreciation | 4,650,509 | 4,334,333 |
| | 6,837,742 | 7,227,442 |
| Land | 2,030,765 | 2,030,765 |
| | $ 8,868,507 | $ 9,258,207 |

**NOTE F – DEPOSITS –** At December 31, 2007, the scheduled maturities of time deposits are as follows:

| | |
|---|---|
| Due in one year | $ 64,801,857 |
| Due in one to three years | 6,188,863 |
| Due after three years | 853,474 |
| | $ 71,844,194 |

**NOTE G – SHORT-TERM BORROWINGS –** The Bank has two borrowing arrangements with the Federal Home Loan Bank of San Francisco. The first allows the Bank to borrow up to approximately $41 million against which the Bank has pledged approximately $100 million of its real estate secured loans. The second arrangement allows the Bank to borrow up to approximately $12 million against which the Bank has pledged approximately $12 million of its investment securities.

As of December 31, 2007 the Bank has borrowed $5,900,000 under these arrangements. This amount is due on January 2, 2008 and includes interest at 3.25%. During 2007 the bank had average borrowings outstanding of $1,100,000 at an effective rate of 4.55%.

The Bank may also borrow up to $5,900,000 overnight on an unsecured basis from two correspondent banks.

**NOTE H – LONG-TERM BORROWINGS –** During the third quarter of 2003, the Bank issued Subordinated Debentures to nineteen investors including executive officers and members of the Bank's Board of Directors, in the total sum of $2,000,000 ("Debentures"). The total amount issued to executive officers and directors was $1,100,000. The Debentures include quarterly payment of interest at prime plus 1.5% and quarterly principal installments of $166,666 commencing on September 30, 2008 until paid in full on June 30, 2011. The Debentures, which are subordinated to the right of payment to depositors and other creditors, partially qualify as Tier 2 Capital.

On April 28, 2006, the Company issued $5,155,000 in junior subordinated debt securities (the "debt securities") to the Santa Lucia Bancorp (CA) Capital Trust, a statutory trust created under the laws of the State of Delaware. These debt securities are subordinated to effectively all borrowings of the Company and are due and payable on July 7, 2036. These debt securities may be redeemed for 105% of the principal balance through July 7, 2011 and then at par thereafter. Interest is payable quarterly beginning July 7, 2006 at 1.48% over the quarterly adjustable 3-month LIBOR.

The Company also purchased a 3% minority interest in Santa Lucia Bancorp (CA) Capital Trust. The balance of the equity of Santa Lucia Bancorp (CA) Capital Trust is comprised of mandatorily redeemable preferred securities.

**NOTE I – INCOME TAXES –** The asset and liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company’s deferred tax liabilities and assets as of December 31 are as follows:

| | 2007 | 2006 |
|---|---|---|
| Deferred liabilities: | | |
| Tax over book depreciation | $ 425,000 | $ 493,000 |
| Market value adjustment on investment securities | 138,000 | — |
| Other | 111,000 | 107,000 |
| Total deferred tax liabilities | 674,000 | 600,000 |
| Deferred tax assets: | | |
| Allowance for loan losses | 673,000 | 673,000 |
| Deferred compensation plans | 498,000 | 390,000 |
| Market value adjustment on investment securities | — | 190,000 |
| State taxes | 191,000 | 224,000 |
| Net loss carryforward | 41,000 | 55,000 |
| Other | 85,000 | 9,000 |
| Total deferred tax assets | 1,488,000 | 1,541,000 |
| Net deferred tax assets | $ 814,000 | $ 941,000 |

The provision for income taxes consists of the following:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Currently payable | $ 2,135,000) | $ 2,389,000 | $ 1,784,000 |
| Deferred taxes (benefits) | (201,000) | (147,000) | (25,000) |
| | $ 1,934,000 | $ 2,242,000 | $ 1,759,000 |

The principal sources of deferred income taxes and the tax effect of eachare as follows:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Tax over book depreciation | $ (68,000) | $ 6,000) | $ 173,000 |
| Provision for loan losses | — | (75,000) | (118,000) |
| State taxes | 33,000 | (75,000) | (46,000) |
| Net loss carryforward | 14,000 | 14,000 | 14,000 |
| Deferredcompensationplans | (108,000) | (42,000) | (41,000) |
| Other | (72,000) | (25,000) | (7,000) |
| Net deferred taxes | $ (201,000) | $ (147,000) | $ (25,000) |

As of December 31, 2007, the Bank had federal net operating loss carryforwards available to reduce future taxable income of approximately $163,000. These net operating loss carryforwards expire in 2010. The 1995 merger with Central Coast National Bank resulted in an ownership change as defined in the Internal Revenue Code Section 382. Accordingly, the utilization of the net operating loss will be subject to the limitations prescribed in Section 382.

As a result of the following items, the total tax expense was different from the amount computed by applying the statutory income tax rate to earnings before income taxes:

| | 2007 | | 2006 | | 2005 | |
|---|---|---|---|---|---|---|
| Federal “expected” tax | $1,679,000 | 34.0% | $1,914,000 | 34.0% | $1,532,000 | 34.0% |
| State franchise tax, net | 347,000 | 7.0 | 396,000 | 7.0 | 318,000 | 7.0 |
| Tax exempt income | (122,000) | (2.5) | (80,000) | (1.3) | (82,000) | (1.8) |
| Other | 30,000 | 0.6 | 12,000 | 0.2 | (9,000) | (0.2) |
| Total expense | $1,934,000 | 39.1% | $2,242,000 | 39.9% | $1,759,000 | 39.0% |

The Company is subject to Federal income tax and California franchise tax. Federal income tax returns for the years ended December 31, 2006, 2005 and 2004 are open to audit by the Federal authorities and California returns for the years ended December 31, 2006, 2005, 2004 and 2003 are open to audit by state authorities.

**NOTE J – EMPLOYEE PROFIT SHARING AND DEFERRED COMPENSATION –** The Bank sponsors a 401 (k) plan for the benefit of its employees. In 1994 the Bank also approved the creation of an Employee Stock Ownership Plan for the benefit of its employees. Contributions to these plans are determined by the Board of Directors. For income tax purposes, the annual contribution is limited to 15% of the compensation of eligible employees. The Bank contributed $203,000 in 2007, $210,000 in 2006, and $240,000 in 2005, to the Employee Stock Ownership Plan. The Bank contributed $57,000 to the 401 (k) plan in 2007 and $50,000 in 2006. There were no contributions to the 401 (k) plan in 2005.

The Bank has entered into deferred compensation agreements with key officers and board members. Under these agreements, the Bank is obligated to provide, upon retirement, a lifetime benefit for the officers and directors. The annual benefits ranging from $25,000 to $75,000 for key officers and $4,000 to $6,000 for directors. The estimated present value of future benefits to be paid is being accrued over the period from the effective date of the agreements until the expected retirement dates of the participants. The expense incurred and amount accrued for this plan for the years ended December 31, 2007, 2006, and 2005 totaled $292,385, $131,454, and $120,715, respectively. The Bank is a beneficiary of life insurance policies that have been purchased as a method of financing the benefits under the agreements.

**NOTE K – STOCK OPTIONS –** The Company sponsors one compensatory incentive and non-qualified stock option plan which provides certain key employees and the Board of Directors with the option to purchase shares of common stock, and one Equity Based Compensation Plan which provides certain key employees and the Board of Directors with the award of any Option, Stock Appreciation Right, Restricted Stock Award, Restricted Share Unit, Performance Share Award, Dividend Equivalent, or any combination thereof. In 1999, the Bank adopted a stock option plan (the 2000 plan) under which up to 360,000 shares of the Bank's common stock may be issued to directors, officers, and key employees. In 2006, the Company adopted the 2006 Equity Based Compensation Plan (the Plan), which the maximum number of shares of common stock that may be awarded under this Plan shall not exceed 200,000 shares, including 38,200 shares rolled over from the Company's 2000 Stock Option Plan. Option prices may not be less than 100% of the fair market value of the stock at the date of grant. Options became exercisable at the rate of 20% per year beginning at various dates and expire not more than ten years from the date of grant. The Company recognized stock-based compensation costs of $122,645 and $63,558 and related tax benefits of $18,450 and $7,193 for 2007 and 2006, respectively.

The fair value of each option granted was estimated on the date of grant using the Black-Scholes options pricing model with the following assumptions:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Risk-free rates | 4.65% | 4.77% | 3.75% |
| Expected volatility | 20.00% | 20.00% | 17.00% |
| Expected dividened yield | 1.40% | 1.40% | 2.10% |
| Expected term | 6.0 years | 6.0 years | 6.5 years |
| Weighted-average grant date fair value | $ 6.72 | $ 6.43 | $ 4.47 |

A summary of the status of the Company's fixed stock option plan as of December 31, 2007 and changes during the year then ended is presented below:

| | December 31, 2007 | | | |
|---|---|---|---|---|
| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value |
| Outstanding at the beginning of the year | 243,176 | $ 15.55 | | |
| Granted | 34,000 | 26.15 | | |
| Exercised | (36,916) | 10.23 | | |
| Foreited or expired | (16,500) | 23.04 | | |
| Outstanding at the end of the year | 223,760 | 17.48 | 6.5 years | $ 1,730,000 |
| Options Exercisable | 126,260 | $ 13.04 | 4.9 years | $ 1,518,000 |

The total intrinsic value of options exercised during the years ended December 31, 2007, 2006, and 2005 were approximately $638,000, $539,000, and $760,000 respectively. As of December 31, 2007 there was $503,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted average period of 2.4 years.

**NOTE L – EARNINGS PER SHARE (EPS) –** The following is a reconciliation of net income and shares outstanding to the income and number of shares used to compute EPS:

| | December 31, 2007 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 3,002,819 | |
| Average shares outstanding | | 1,933,231 |
| Used in Basic EPS | 3,002,819 | 1,933,231 |
| Dilutive effect of outstanding stock options | | 59,823 |
| Used in Diluted EPS | $ 3,002,819 | 1,993,054 |

| | December 31, 2006 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 3,388,271 | |
| Average shares outstanding | | 1,916,253 |
| Used in Basic EPS | 3,388,271 | 1,916,253 |
| Dilutive effect of outstanding stock options | | 98,413 |
| Used in Diluted EPS | $ 3,388,271 | 2,014,666 |

| | December 31, 2005 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 2,746,820 | |
| Average shares outstanding | | 1,878,949 |
| Used in Basic EPS | 2,746,820 | 1,878,949 |
| Dilutive effect of outstanding stock options | | 105,289 |
| Used in Diluted EPS | $ 2,746,820 | 1,984,238 |

**NOTE M – COMMITMENTS AND CONTINGENCIES –** The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those commitments. Commitments to extend credit (such as the unfunded portion on lines of credit and commitments to fund new loans) as of December 31, 2007 and 2006 amounts to approximately $57,326,000 and $56,557,000, respectively, of which approximately $4,286,000 and

$2,603,000 are related standby letters of credit, respectively. The Company uses the same credit policies in these commitments as is done for all of its lending activities. As such, the credit risk involved in these transactions is essentially the same as that involved in extending loan facilities to customers.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Company evaluates each client's credit worthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Company is based on management's credit evaluation of the customer. The majority of the Company's commitments to extend credit and standby letters of credit are secured by real estate.

In the normal course of business, the Company is involved in various litigation. In the opinion of management, and based on the advise of the Company's legal counsel, the disposition of all pending litigation will not have a material effect on the Company's financial position.

**NOTE N – FAIR VALUES OF FINANCIAL INSTRUMENTS –** The fair value of a financial instrument is the amount at which the asset or obligation could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire holdings of a particular financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The following methods and assumptions were used to estimate the fair value of significant financial instruments:

**Financial Assets –** The carrying amounts of cash, short term investments, due from customers on acceptances, and bank acceptances outstanding are considered to approximate fair value. Short term investments include federal funds sold, securities purchased under agreements to resell, and interest bearing deposits with banks. The fair values of investment securities, including available for sale, are generally based on quoted market prices. The fair value of loans are estimated using a combination of techniques, including discounting estimated future cash flows and quoted market prices of similar instruments where available.

**Financial Liabilities –** The carrying amounts of deposit liabilities payable on demand, commercial paper, and other borrowed funds are considered to approximate fair value. For fixed maturity deposits, fair value is estimated by discounting estimated future cash flows using currently offered rates for deposits of similar remaining maturities. The fair value of long term debt is based on rates currently available for debt with similar terms and remaining maturities.

**Off-Balance Sheet Financial Instruments –** The fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements. The fair values of these financial instruments are not deemed to be material.

The estimated fair value of financial instruments at December 31, 2007 and 2006 are summarized as follows:

| | December 31, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| | Carrying Value | Market Value | Carrying Value | Market Value |
| Financial Assets: | | | | |
| Cash and cash equivalents | $ 7,399,412 | $ 7,399,412 | $10,139,526 | $10,139,526 |
| Investment securities | 56,107,156 | 56,107,156 | 42,778,417 | 42,778,417 |
| Loans receivable, net | 166,619,494 | 167,422,617 | 169,680,473 | 170,091,100 |
| Cash surrender value of life insurance | 5,005,376 | 5,005,376 | 3,336,076 | 3,336,076 |
| Federal Reserve Bank FHLB Stock | 1,453,850 | 1,453,850 | 1,397,700 | 1,397,700 |
| Accrued interest receivable | 1,465,402 | 1,465,402 | 1,559,551 | 1,559,551 |
| Financial Liabilities: | | | | |
| Time deposits | $71,844,194 | $72,612,333 | $65,917,714 | $65,838,613 |
| Other deposits | 140,874,184 | 141,374,184 | 147,070,738 | 147,070,738 |
| Other borrowings | 5,900,000 | 5,900,000 | — | — |
| Long-term debt | 7,155,000 | 7,155,000 | 7,155,000 | 7,155,000 |
| Accrued interest and other liabilities | 1,677,551 | 1,677,551 | 1,457,716 | 1,457,716 |

**NOTE O – REGULATORY MATTERS –** The Company and the Bank are 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 material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain offbalance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2007, the most recent notification from the Federal Reserve Bank (FRB) 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 have changed the Bank's category). To be categorized as well capitalized, the Bank must maintain minimum ratios as set forth in the table below. The following table also sets forth the Company's and Bank's actual capital amounts and ratios (dollar amounts in thousands):

| | Actual | | For capital adequacy purposes | | To be well capitalized under prompt corrective action provisions | |
|---|---|---|---|---|---|---|
| | Amount (thousands) | Ratio | Amount (thousands) | Ratio | Amount (thousands) | Ratio |
| **As of December 31, 2007:** | | | | | | |
| **Company** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 29,075 | 14.6% | $ 15,912 | 8.0% | $ 19,890 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 26,147 | 13.2% | $ 7,956 | 4.0% | $ 11,934 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 26,147 | 10.5% | $ 9,794 | 4.0% | $ 12,243 | 5.0% |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Bank** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 27,410 | 13.8% | $ 15,888 | 8.0% | $ 19,860 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 24,482 | 12.3% | $ 7,944 | 4.0% | $ 11,916 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 24,482 | 9.9% | $ 9,941 | 4.0% | $ 12,427 | 5.0% |
| **As of December 31, 2006:** | | | | | | |
| **Company** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 27,872 | 14.4% | $ 14,026 | 8.0% | $ 17,533 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 24,563 | 12.7% | $ 7,013 | 4.0% | $ 10,520 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 24,563 | 10.0% | $ 9,794 | 4.0% | $ 12,243 | 5.0% |
| **Bank** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 25,575 | 13.1% | $ 15,588 | 8.0% | $ 19,485 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 22,266 | 11.4% | $ 7,794 | 4.0% | $ 11,691 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 22,266 | 9.1% | $ 9,777 | 4.0% | $ 12,221 | 5.0% |

The California Financial Code provides that a bank may not make a cash distribution to its shareholders in excess of the lesser of the Bank's undivided profits or the Bank's net income for its last three fiscal years less the amount of any distribution made by the Bank to shareholders during the same period.

With certain exceptions the Company may not pay a dividend to its shareholders unless its retained earnings equal at least the amount of the proposed dividend.

**NOTE P – HOLDING COMPANY –** On April 3, 2006 Santa Lucia Bancorp acquired all the outstanding shares of Santa Lucia Bank by issuing 1,909,837 shares of common stock in exchange for the surrender of all outstanding shares of the Bank's common stock. There was no cash involved in this transaction. The acquisition was accounted for like a pooling of interest and the consolidated financial statements contained herein have been restated to give full effect to this transaction.

Santa Lucia Bancorp has no significant business activities other than its investment in Santa Lucia Bank and its investment and related borrowings from Santa Lucia (CA) Capital Trust as discussed in Note H. Accordingly, no separate financial information on the Company is provided.

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## SANTA LUCIA BANCORP

**SANTA LUCIA BANCORP BOARD OF DIRECTORS**

| | |
|---|---|
| **JERRY W. DECOU III** | CHAIRMAN |
| **DOUGLAS C. FILIPPONI** | VICE CHAIRMAN |
| **KHATCHIK H. ACHADJIAN** | |
| **STANLEY R. CHERRY** | |
| **JOHN C. HANSEN** | |
| **JEAN HAWKINS** | |
| **PAUL G. MOERMAN** | |
| **LARRY H. PUTNAM** | |
| **D. JACK STINCHFIELD** | |

**SANTA LUCIA BANCORP EXECUTIVE OFFICERS**

| | |
|---|---|
| **LARRY H. PUTNAM** | PRESIDENT AND CHIEF EXECUTIVE OFFICER |
| **JOHN C. HANSEN** | EXECUTIVE VICE PRESIDENT, CHIEF FINANCIAL OFFICER |

**SANTA LUCIA BANK BOARD OF DIRECTORS**

| | |
|---|---|
| **JERRY W. DECOU III** | CHAIRMAN |
| **DOUGLAS C. FILIPPONI** | VICE CHAIRMAN |
| **KHATCHIK H. ACHADJIAN** | |
| **STANLEY R. CHERRY** | |
| **JOHN C. HANSEN** | |
| **JEAN HAWKINS** | |
| **PAUL G. MOERMAN** | |
| **LARRY H. PUTNAM** | |
| **D. JACK STINCHFIELD** | |

## SANTA LUCIA BANK

**EXECUTIVE OFFICERS**

| | |
|---|---|
| **LARRY H. PUTNAM** | Chief Executive Officer |
| **JOHN C. HANSEN** | President and Chief Operating Officer |
| **JAMES M. COWAN** | Executive Vice President, Chief Credit Officer |

**SENIOR VICE PRESIDENTS**

| | |
|---|---|
| **MELODEE FONTANA** | Senior Vice President, Operations Administrator |
| **ROBERT COVARRUBIAS** | Senior Vice President, Manager |

**VICE PRESIDENTS**

| | |
|---|---|
| **TERI DAVIS** | Vice President, Loan Officer |
| **SHARON SATTERTHWAITE** | Vice President, Controller |
| **LEAH T. WEST** | Vice President, Manager |
| **JIM KELLEY** | Vice President, Loan Officer |
| **MICHAEL W. McKENZIE** | Vice President, Manager |
| **LARRY WOMACK** | Vice President, Loan Officer |
| **JAMES P. BURUBELTZ** | Vice President, Loan Officer |
| **RICHARD ALLEN** | Vice President, Loan Officer |
| **JULIE A. JOSLIN** | Vice President, Cashier |

**ASSISTANT VICE PRESIDENTS**

| | |
|---|---|
| **JENNIFER BASSI GINDER** | Assistant Vice President, Operations Officer |
| **KRISTIE KELLER** | Assistant Vice President, Central Operations |

| | |
|---|---|
| **KIM DONALDSON** | Assistant Vice President, Operations Officer |
| **CHERYL MUMFORD** | Assistant Vice President, Operations Officer |
| **RYUN McCRORY** | Assistant Vice President, Loan Officer |
| **J. DARREN BARNES** | Assistant Vice President, Loan Officer |
| **REGINA M. SHELDON** | Assistant Vice President, Loan Officer |

**OFFICERS**

| | |
|---|---|
| **KAREN SAMPSON** | Assistant Operations Officer |
| **STELLA MARTINEZ** | Operations Officer |
| **ROBERT McCONAGHY** | Loan Officer |

| **ATASCADERO** | **PASO ROBLES** | **ARROYO GRANDE** | **SANTA MARIA** |
|---|---|---|---|
| 7480 EL CAMINO REAL | 1240 SPRING STREET | 1530 E. GRAND AVENUE | 1825 S. BROADWAY |
| ATASCADERO, CA 93422 | PASO ROBLES, CA 93446 | ARROYO GRANDE, CA 93420 | SANTA MARIA, CA 93454 |
| 805-466-7087 | 805-239-1140 | 805-473-1988 | 805-614-9100 |

**MARKET MAKERS**

| | |
|---|---|
| **GEORGE CROSBY, MAGUIRE INVESTMENTS – SANTA MARIA, CA** | 805/922-6901 or 800/244-4183 |
| **LISA GALLO, WEDBUSH MORGAN SECURITIES – LAKE OSWEGO, OR** | 503/675-3100 or 866/491-7828 |
| **MICHAEL S. HEDREI, HOWE BARNES HOEFER & ARNETT, INC. – SAN FRANCISCO, CA** | 415/538-5749 or 800/774-8723 |
| **RANDY KRUMLAND, EDWARD JONES – ATASCADERO, CA** | 805/466-0244 or 800/467-0244 |
| **JIM MOFFATT, MORGAN STANLEY – PASO ROBLES, CA** | 805/239-0920 or 800/733-0920 |
| **TREVOR MORRIS, UBS FINANCIAL SERVICES, INC. – LOS ANGELES, CA** | 213/972-1511 or 800/443-5203 |
| **JOEY J. WARMENHOVEN, McADAMS WRIGHT RAGEN – PORTLAND, OR** | 503/922-4888 or 866/662-0351 |

**Exhibit 13.1**

**Santa Lucia Bancorp 2007 Annual Report**

**2007**

**Santa Lucia Bancorp**
7480 El Camino Real
Atascadero, California 93422

*Stock Symbol* – SLBA.OB

**Santa Lucia Bank**
7480 El Camino Real
Atascadero, California 93422

**www.santaluciabank.com**

| | | | |
|---|---|---|---|
| **Atascadero** | **Paso Robles** | **Arroyo Grande** | **Santa Maria** |
| 7480 El Camino Real | 1240 Spring St. | 1530 E. Grand Ave. | 1825 S. Broadway |
| (805) 466-7087 | (805) 239-1140 | (805) 473-1988 | (805) 614-9100 |

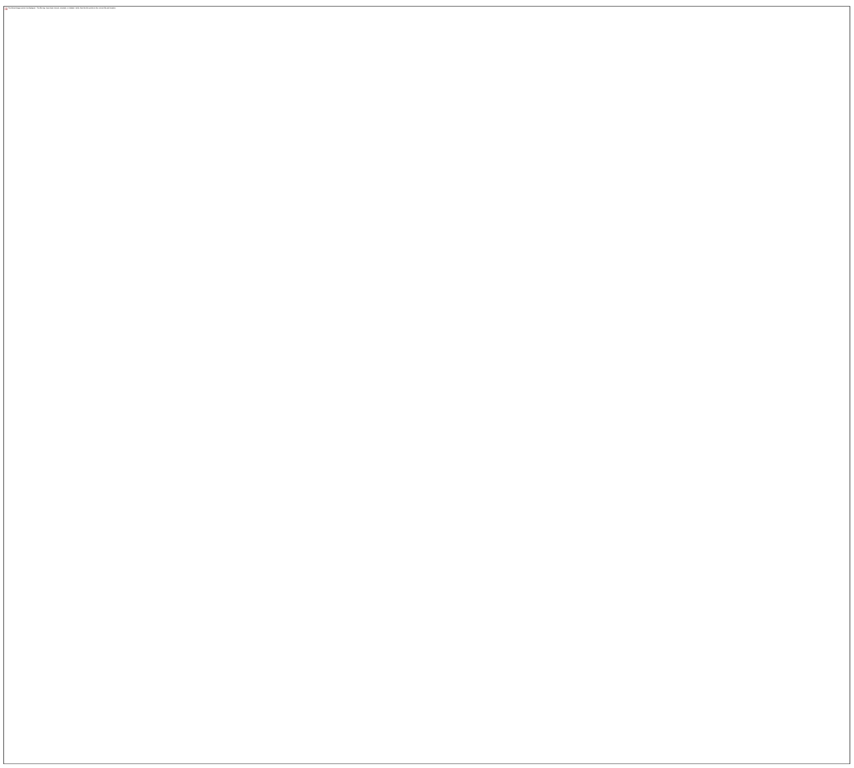
**Santa Lucia Bancorp**

***Message from the President***

Dear Shareholders, Customers and Friends,

Santa Lucia Bancorp (“The Company”) is pleased to report the results from operations for 2007. The economy and more specifically, “The Real Estate Market”, went through some difficult times in 2007, and are still in the process of recovering. We are pleased to report that these events, neither directly, nor indirectly have had a significant affect on The Company or Santa Lucia Bank (“The Bank”), its wholly owned subsidiary.

Net profits for The Company were $3,002,819 for the year 2007. This compares to 2006’s net income of $3,388,271, which was an all time high for The Company. The net income for 2007 is down 11.38% from 2006.



Larry H. Putnam, President and Chief Executive Officer

Due to the change in the economic conditions we operate in, our customers have reinvested funds in their businesses and have less excess funds, which have had a negative effect on the Company’s deposits. The trend of depositing excess funds into Time Certificates of Deposit or other interest bearing accounts that started in 2006 has continued into 2007. Despite this trend, the Bank has 36.25% of total deposits in non-interest bearing deposits. This compares to 40.50% in non-interest bearing deposits as of December 31, 2006. Non-interest bearing deposits at these levels continue to be well above industry averages.

The Company was able to effectively reallocate funds from real estate lending, specifically construction lending into loans for general commercial credit purposes. The Bank was pleased to see the significant growth in loans for general commercial credit purposes, which increased 11.73% between December 31, 2006 and 2007. This is an area we have been concentrating on for the last several years, as a significant change was anticipated in the real estate construction industry. We would expect this trend to continue.

Despite the fact that we have seen some changes in our business, we have a strong core deposit and loan base. We remain committed to providing quality customer service on a consistent basis in the markets we serve. Building solid relationships with our customers allows us to continue to build on our core business.

Santa Lucia Bancorp continues the practice of paying cash dividends to our shareholders. Two cash dividends were paid in 2007 for a total of $0.45 per share. The dividend payable to

Santa Lucia Bancorp's Board of Directors. Standing left to right—John C. Hansen, Executive Vice President - Chief Financial Officer, Jerry W. DeCou III, Chairman of the Board, Larry H. Putnam, President and Chief Executive Officer, Douglas C. Filipponi, Vice Chairman. Seated left to right—Paul G. Moerman, D. Jack Stinchfield, Jean Hawkins, Stanley R. Cherry and Khatchik H. Achadjian.

shareholders as of September 30, 2007 was increased by 25% to $0.25 per share compared to the dividend of $0.20 per share paid to shareholders of record as of March 31, 2007. This is the eighteenth consecutive year that cash dividends have been paid to our shareholders.

On June 30, 2005, the Company split its stock on a 4 to 1 basis. Since the stock split, the marketability and activity has increased in the companies stock, which was anticipated. Prior to the split, the companies stock was selling for $81.00 per share, resulting in a post split price of $20.25 per share compared to the current price of $25.00. Despite the recent decline in price, the stock has increased in value $4.75 per share or 23.46% in the past 2-1/2 years.

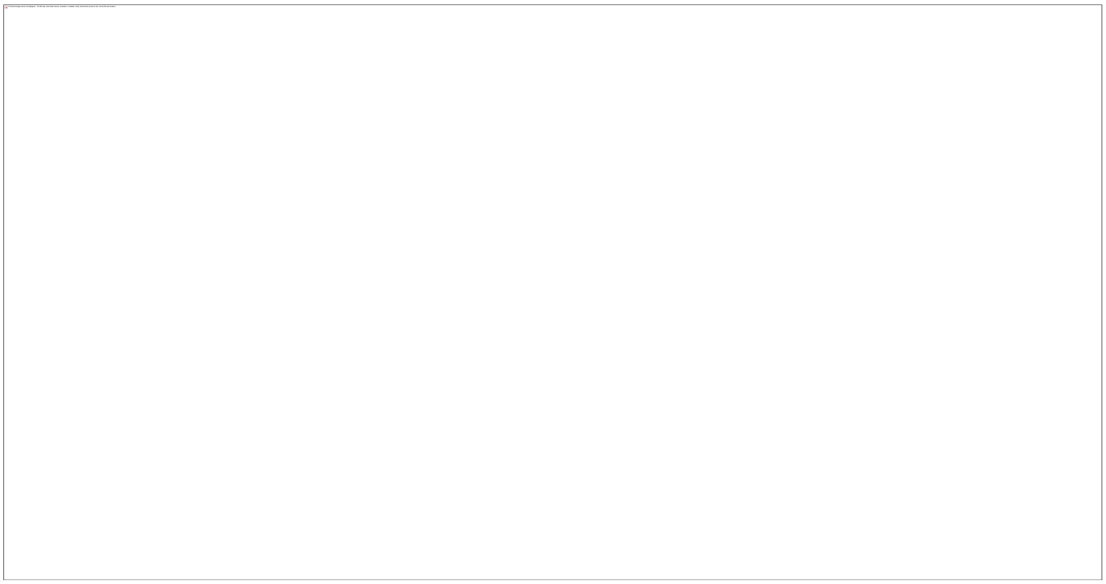
We look forward to the challenges of 2008 and are very optimistic about the future. We have effectively weathered the economic challenges of 2007. Our Board of Directors, Officers and Staff remain committed to building a solid banking franchise.

I would like to thank our shareholders for your support and trust over the years. This coupled with our loyal customer base, strategic locations on the Central Coast of California and dedicated staff will ensure that we continue to enhance the Company's performance and value in years to come.

**Larry H. Putnam**
President and Chief Executive Officer

**SANTA LUCIA BANK**
*(a wholly owned subsidiary of Santa Lucia Bancorp)*

**Senior Management Team**



John C. Hansen, Larry H. Putnam, James M. Cowan

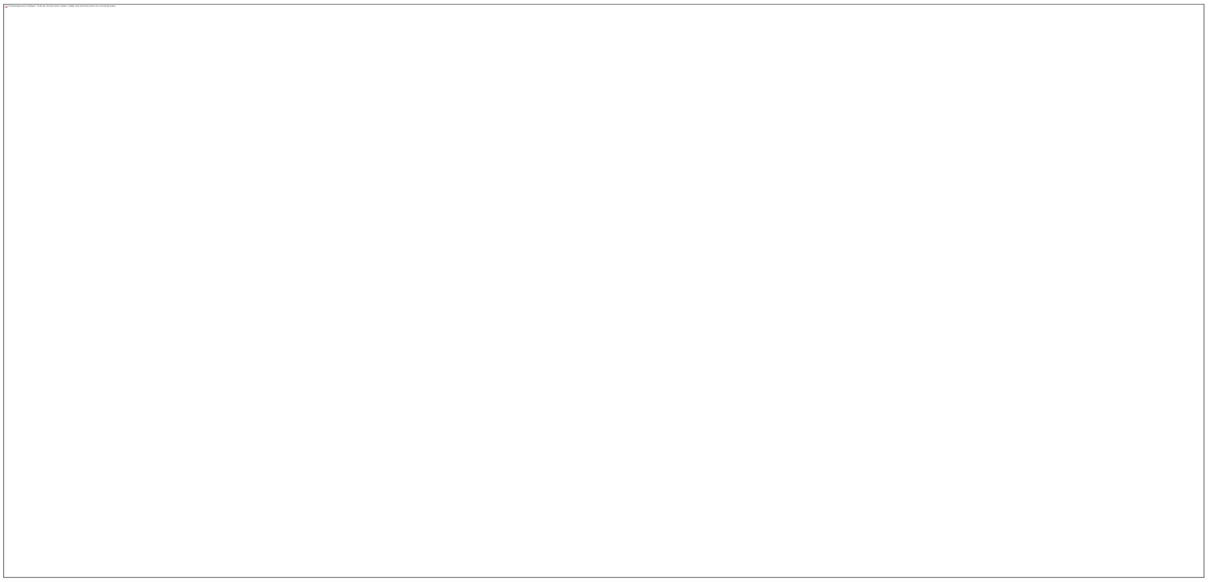
LARRY H. PUTNAM
Chief Executive Officer

JOHN C. HANSEN
President and
Chief Operating Officer

JAMES M. COWAN
Executive Vice President
Chief Credit Officer

***Eager to service your banking needs***

**Administrative Team**



Melodee Fontana, John C. Hansen, Larry H. Putnam, Julie A. Joslin, Kristie Keller, James M. Cowan, Larry Womack, Sharon Satterthwaite

LARRY H. PUTNAM
Chief Executive Officer

JOHN C. HANSEN
President and Chief Operating Officer

JAMES M. COWAN
Executive Vice President
Chief Credit Officer

MELODEE FONTANA
Senior Vice President
Operations Administrator

SHARON SATTERTHWAITE
Vice President
Controller

LARRY WOMACK
Vice President
Assistant Credit Administrator

JULIE A. JOSLIN
Vice President
Cashier

KRISTIE KELLER
Assistant Vice President
Central Operations

**Atascadero Office**

7480 El Camino Real, Atascadero, California

**Atascadero Officer Team**

Jim Kelley, Karen Sampson, Kim Donaldson, J. Darren Barnes, Teri Davis

TERI DAVIS
Vice President
Loan Officer

JIM KELLEY

Vice President
Loan Officer

KIM DONALDSON
Assistant Vice President
Operations Officer

J. DARREN BARNES
Assistant Vice President
Loan Officer

KAREN SAMPSON
Assistant Operations Officer

**Paso Robles Office**
1240 Spring Street, Paso Robles, California

**Paso Robles Officer Team**

Robert Covarrubias, Cheryl Mumford, Ryun McCrory

ROBERT COVARRUBIAS
Senior Vice President
Manager

CHERYL MUMFORD
Assistant Vice President

Operations Officer

RYUN McCRORY
Assistant Vice President
Loan Officer

**Arroyo Grande Office**
1530 East Grand Avenue, Arroyo Grande, California

**Arroyo Grande Officer Team**

Richard Allen, Michael W. McKenzie, Regina M. Sheldon, Jennifer Bassi Ginder

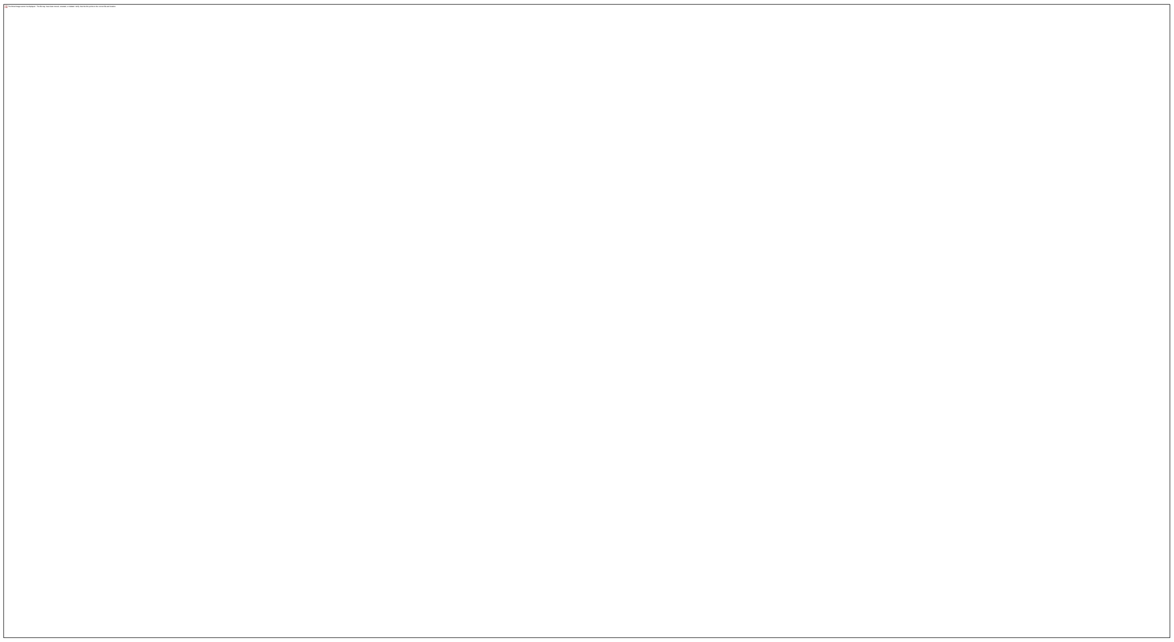
**MICHAEL W. McKENZIE**
Vice President
Manager

**RICHARD ALLEN**
Vice President
Loan Officer

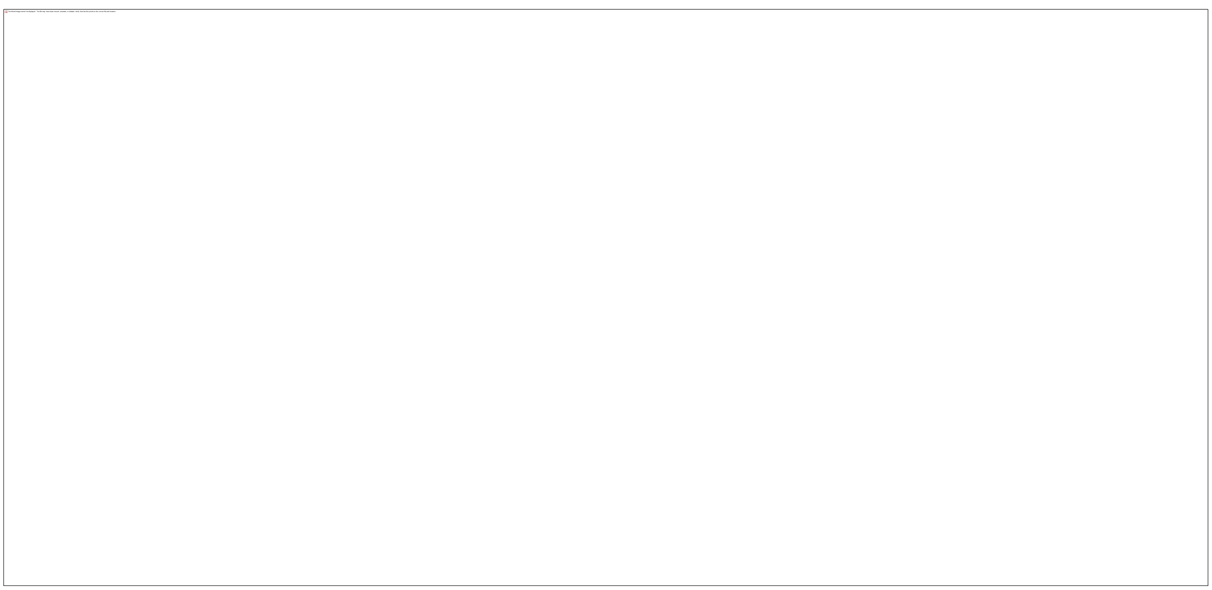
**JENNIFER BASSI GINDER**
Assistant Vice President
Operations Officer

**REGINA M. SHELDON**
Assistant Vice President
Loan Officer

**Santa Maria Office**
1825 South Broadway, Santa Maria, California



**Santa Maria Officer Team**



Leah T. West, James P. Burubeltz, Stella Martinez, Robert J. McConaghy

**LEAH T. WEST**
Vice President
Manager

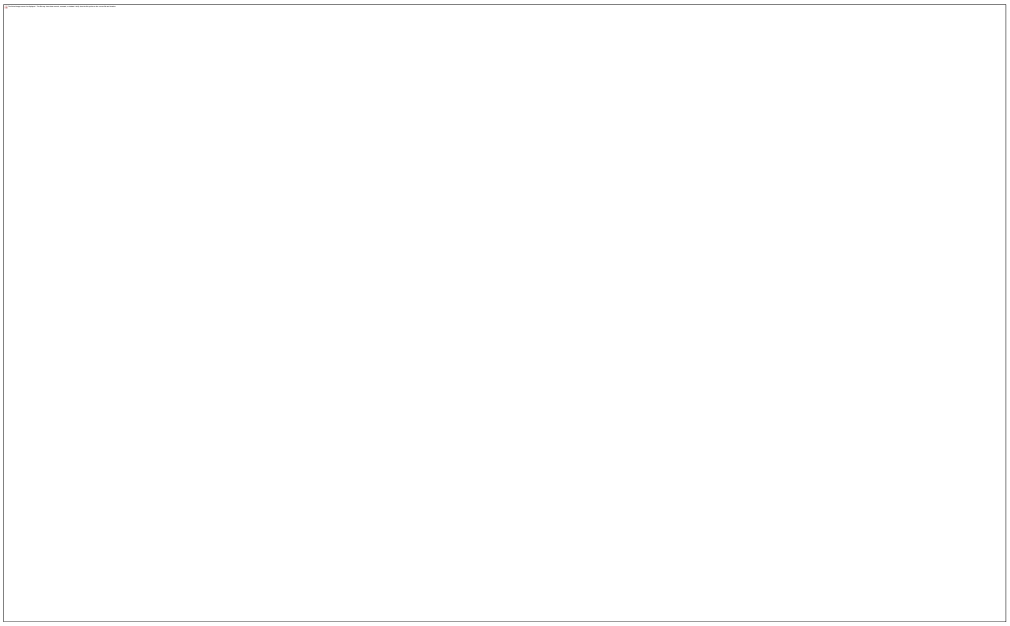
**JAMES P. BURUBELTZ**
Vice President

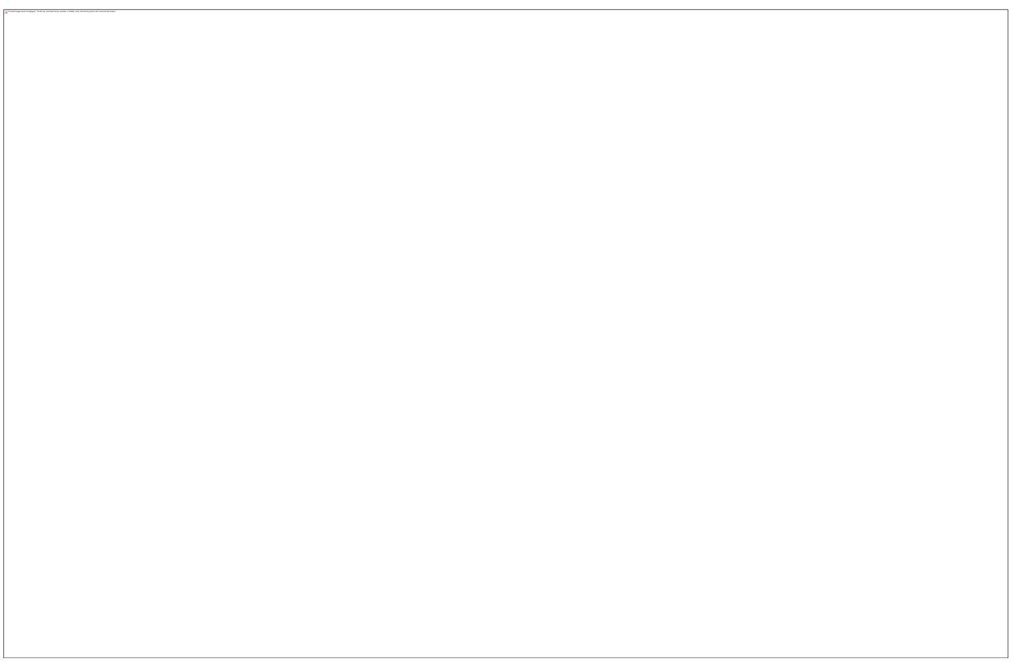
Loan Officer

**STELLA MARTINEZ**
Operations Officer

**ROBERT J. McCONAGHY**
Loan Officer

**SANTA LUCIA BANCORP**
**FINANCIAL HIGHLIGHTS**
*As of Years Ended December 31,*





The Company has only one class of securities, common stock, which is traded on the over-the-counter market. Our stock is quoted on the OTC Bulletin Board under the symbol SLBA.OB. The information in the following table indicates the high and low bid prices of the Company's common stock for each quarterly period during the last two years based upon information provided by the Company market makers. These prices do not include retail mark ups, mark downs or commissions, but have been adjusted to reflect the Bank's 4-for-1 stock split that was effective June 2006.

| Quarter Ended 2007 | Low | High |
| --- | --- | --- |

| | | |
|---|---|---|
| December 31 | $ 23.25 | $ 26.25 |
| September 30 | 25.00 | 29.00 |
| June 30 | 26.00 | 28.99 |
| March 31 | 26.00 | 29.00 |

| **Quarter Ended 2006** | **Low** | **High** |
|---|---|---|
| December 31 | $ 24.00 | $ 29.00 |
| September 30 | 24.05 | 27.00 |
| June 30 | 26.55 | 34.50 |
| March 31 | 25.05 | 30.25 |

**Santa Lucia Bancorp and Subsidiary**

**Consolidated Selected Financial Information**

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (dollars in thousands, except per share data) | | | | |
| **Summary of Operations:** | | | | | |
| Interest Income | $ 17,719 | $ 17,027 | $ 13,546 | $ 10,220 | $ 9,157 |
| Interest Expense | 4,824 | 3,577 | 1,984 | 1,343 | 1,324 |
| Net Interest Income | 12,895 | 13,450 | 11,562 | 8,877 | 7,833 |
| Provision for Loan Loss | — | 240 | 300 | 110 | 115 |
| Net Interest Income After Provision for Loan Losses | 12,895 | 13,210 | 11,262 | 8,767 | 7,718 |
| Noninterest Income | 1,071 | 1,010 | 1,052 | 1,191 | 1,376 |
| Noninterest Expense | 9,029 | 8,590 | 7,808 | 7,060 | 6,609 |
| Income Before Income Taxes | 4,937 | 5,630 | 4,506 | 2,898 | 2,485 |
| Income Taxes | 1,934 | 2,242 | 1,759 | 1,076 | 873 |
| Net Income | $ 3,003 | $ 3,388 | $ 2,747 | $ 1,822 | $ 1,612 |
| Cash Dividends Paid | $ 871 | $ 768 | $ 730 | $ 697 | $ 685 |
| **Per Share Data:** | | | | | |
| Net Income – Basic | $ 1.55 | $ 1.77 | $ 1.46 | $ 0.98 | $ 0.89 |
| Net Income – Diluted | $ 1.51 | $ 1.68 | $ 1.38 | $ 0.94 | $ 0.86 |
| Dividends | $ 0.450 | $ 0.400 | $ 0.388 | $ 0.375 | $ 0.375 |
| Book Value | $ 11.01 | $ 9.93 | $ 8.35 | $ 7.42 | $ 6.96 |
| **Common Outstanding Shares:** | 1,924,873 | 1,928,097 | 1,899,543 | 1,861,764 | 1,844,708 |
| **Statement of Financial Condition Summary:** | | | | | |
| Total Assets | $ 248,640 | $ 240,738 | $ 231,532 | $ 211,684 | $ 183,827 |
| Total Deposits | 212,718 | 212,988 | 206,879 | 194,868 | 168,033 |
| Total Net Loans | 166,619 | 169,680 | 152,563 | 125,586 | 109,949 |
| Allowance for Loan Losses | 1,673 | 1,654 | 1,470 | 1,200 | 1,112 |
| Total Shareholders’ Equity | 21,189 | 19,137 | 15,866 | 13,807 | 12,845 |
| **Selected Ratios:** | | | | | |
| Return on Average Assets | 1.22% | 1.42% | 1.21% | 0.91% | 0.94% |
| Return on Average Equity | 14.87% | 19.45% | 18.67% | 13.71% | 13.00% |
| Average Loans as a Percentage of Average Deposits | 76.11% | 79.74% | 69.90% | 62.77% | 68.93% |
| Allowance for Loan Losses to Total Loans | 0.99% | 0.96% | 0.95% | 0.94% | 1.00% |
| **Company:** | | | | | |
| Tier I Capital to Average Assets | 10.50% | 10.00% | — | — | — |
| Tier I Capital to Risk-Weighted Assets | 13.20% | 12.70% | — | — | — |
| Total Capital to Risk-Weighted Assets | 14.60% | 14.40% | — | — | — |
| **Bank:** | | | | | |
| Tier I Capital to Average Assets | 9.85% | 9.11% | 7.16% | 6.53% | 7.00% |
| Tier I Capital to Risk-Weighted Assets | 12.33% | 11.43% | 9.33% | 8.80% | 9.34% |
| Total Capital to Risk-Weighted Assets | 13.80% | 13.13% | 11.34% | 10.85% | 11.66% |

**Santa Lucia Bancorp and Subsidiary**

## General

Santa Lucia Bancorp (the "Company") (OTC Bulletin Board SLBA.OB) is a California corporation organized April 3, 2006 to act as the holding company for its wholly owned subsidiary Santa Lucia Bank (the "Bank"), collectively referred to herein as the "Company." The Bank was organized as a national banking association on December 19, 1984 and commenced operations on August 5, 1985. The Bank converted from a national to a California state-chartered bank on May 30, 1997.

The Bank is a commercial banking business, operating from offices located at 7480 El Camino Real, Atascadero, California, 1240 Spring Street, Paso Robles, California, 1530 East Grand Avenue, Arroyo Grande, California and 1825 South Broadway, Santa Maria, California.

The Bank's operating policy since its inception has emphasized general commercial banking. Most of the Bank's customers are small to mid-sized businesses and individuals. The business of the Bank emphasizes serving the needs of local businesses, professionals, and wage earners. The Bank provides services designed to meet the needs of the various segments of the markets it serves. These services include a full line of business loans, business leases, personal loans and deposit products.

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

Certain statements contained in this report, including, without limitation, statements containing the words "believes", "anticipates", "intends", "expects", and words of similar import, constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions in those areas in which the Company operates, demographic changes, competition, fluctuations in interest rates, changes in business strategy or developmental plans, changes in governmental regulations, credit quality, the availability of capital to fund the expansion of the Company's business, and other factors referenced in the Company's reports filed pursuant to the Exchange Act. Given these uncertainties, shareholders are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

This discussion should be read in conjunction with the Company's audited financial statements and notes thereto which appear elsewhere in this report.

***Overview***

The following sections set forth an analysis of the significant operating changes, business trends, financial condition, earnings, capital position and liquidity that have occurred in the three-year period ended December 31, 2007.

## Consolidated Results of Operations

In 2007 the Company recorded earnings of $3,003,000, which reflects a decrease of $385,000 or 11.4% over the previous year. In 2006, earnings were $3,388,000, an increase of 23.3% from 2005's earnings of $2,747,000, which reflected an increase of 50.8% from earnings posted in 2004. Basic earnings per share in 2007 were $1.55 compared with $1.77 and $1.46 for 2006 and 2005, respectively. This reflects a decrease from 2006 to 2007 of 12.4%. The earnings per share (diluted) for 2007, 2006, and 2005 were $1.51, $1.68, and $1.38, respectively, a 10.1% decrease from 2006 to 2007. The Company paid cash dividends totaling $0.45 per share during 2007 compared to $0.40 paid in 2006 and $0.388 paid in 2005. Return on average shareholder's equity was 14.9% in 2007 compared to 19.5% in

2006 and 18.7% in 2005. Return on average assets was 1.22% in 2007 compared to 1.42% in 2006 and 1.21% in 2005.

The decrease in the Company's net earnings from 2006 to 2007 was due to four major events: a decrease in average loans of $7,105,000 or 4.2%; a 100 basis point decrease in the prime lending rate; an increase of $10,689,000 in average interest bearing deposits or 8.7%; and a 65 basis point increase in interest bearing deposit rates.

The Company believes that the local economies, in which it operates, Atascadero, Paso Robles, Arroyo Grande, and Santa Maria continue to remain relatively stable. Competition for deposits continues to be very strong both from traditional sources as well as alternative investments such as mutual funds, money market accounts and the stock market. The Bank's decline in the loan portfolio has been affected by the slow down in the demand for construction lending and real estate related markets.

***Net Interest Income***

Net interest income is the Company's largest source of operating income and is derived from interest and fees received on interest earning assets, less interest expense incurred on interest bearing liabilities. The most significant impact on the Company's net interest income between periods is derived from the interaction of changes in the volume of and rates earned or paid on interest earning assets and interest bearing liabilities. The volume of loans, investment securities and other interest earning assets, compared to the volume of interest bearing deposits and indebtedness, combined with the spread, produces changes in the net interest income between periods.

Interest income increased $692,000 or 4.1% in 2007 from $17,027,000 in 2006 to $17,719,000 in 2007. This is compared to an increase of $3,481,000 or 25.7% from 2005 to 2006 and an increase of $3,326,000 or 32.5% from 2004 to 2005. The slowdown in the increase in interest income is again attributable to the slowdown in real estate lending. The increase in 2007 was primarily due to the increase in average investments of $10,451,000 or 27.1% from 2006 and an increase in the average investment yield from 3.9% in 2006 to 5.0% in 2007.

Total interest and fees produced an 8.1% yield on average earning assets for 2007, 8.1% for 2006 and 6.8% in 2005. The average loan to deposit ratio for 2007 was 76.11%, which represents a decrease of 4.6% over the 79.74% average for 2006.

Total interest expense increased $1,247,000 or 34.9% from $3,577,000 in 2006 to $4,824,000 in 2007 compared to an increase of $1,593,000 or 80.3% from 2005 to 2006. The increase in total interest expense in 2007 was due to a combination of rising rates for all deposit categories coupled with an increase in interest bearing funds. In 2007, total interest bearing liabilities increased $12.1 million or 9.3%. These factors increased our rate paid on interest-bearing liabilities 65 basis points from 2.76% in 2006 to 3.41% in 2007.

Net interest margin decreased 46 basis points from 6.38% in 2006 to 5.92% in 2007. As noted above, this decrease was primarily due to changes in our asset mix and an increase in our cost of funds. In our asset mix, we experienced migration from higher yielding loans to lower yielding investments while in our liability mix, we experienced migration from lower costing NOW, Money Market and Savings accounts to higher costing time certificates of deposits and long-term debt.

We expect this trend of reduction in our net interest margin to continue into 2008 as anticipated prime rate decreases will impact our interest earning assets faster than we can reprice our interest-bearing deposits.

The following table shows the composition of average earning assets and average interest-bearing liabilities, average yields and rates, and the net interest margin for the years ended December 31, 2007, 2006 and 2005. Nonaccrual loans are included in the calculation of the average balances of loans, and nonaccrued interest is excluded.

| | Year Ended December 31 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | | 2005 | | |
| | Average Balance | Interest | Yield/ Rate | Average Balance | Interest | Yield/ Rate | Average Balance | Interest | Yield/ Rate |
| | (dollars in thousands) | | | | | | | | |
| Assets: | | | | | | | | | |
| Loans | $ 163,741 | $ 15,031 | 9.18% | $ 169,139 | $ 15,397 | 9.10% | $ 145,195 | $ 11,747 | 8.09% |
| Investment securities | 49,024 | 2,438 | 4,97% | 38,573 | 1,485 | 3.85% | 48,660 | 1,625 | 3.34% |
| Federal funds sold | 4,954 | 250 | 5.05% | 2,941 | 145 | 4.93% | 5,685 | 174 | 3.06% |
| Total average interest-earning assets | 217,719 | 17,719 | 8.14% | 210,653 | 17,027 | 8.08% | 199,540 | 13,546 | 6.79% |
| Other assets | 29,278 | | | 28,808 | | | 27,913 | | |
| Less allowance for loan losses | (1,707) | | | (1,593) | | | (1,332) | | |
| Total average assets | $ 245,290 | | | $ 237,868 | | | $ 226,121 | | |
| | | | | | | | | | |
| Liabilities and Shareholders' Equity: | | | | | | | | | |
| Interest-bearing demand - NOW | $ 13,391 | $ 55 | 0.41% | $ 14,696 | $ 38 | 0.26% | $ 17,834 | $ 42 | 0.24% |
| Money Market | 24,929 | 722 | 2.90% | 24,103 | 503 | 2.09% | 30,186 | 446 | 1.48% |
| Savings | 27,076 | 289 | 1.07% | 28,074 | 222 | 0.79% | 30,560 | 133 | 0.44% |
| Time certificate of deposits | 68,019 | 3,157 | 4.64% | 55,853 | 2,316 | 4.15% | 40,772 | 1,195 | 2.93% |
| Total average interest- | 133,415 | 4,223 | 3.17% | 122,726 | 3,079 | 2.51% | 119,352 | 1,816 | 1.52% |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| bearing deposits | | | | | | | | | |
| Short-term borrowings | 1,059 | 51 | 4.82% | 1,356 | 65 | 4.79% | 439 | 16 | 3.64% |
| Long-term borrowings | 7,155 | 550 | 7.69% | 5,465 | 433 | 7.92% | 2,000 | 152 | 7.60% |
| Total interest-bearing liabilities | 141,629 | 4,824 | 3.41% | 129,547 | 3,577 | 2.76% | 121,791 | 1,984 | 1.63% |
| Demand deposits | 81,714 | | | 89,383 | | | 88,366 | | |
| Other liabilities | 1,749 | | | 1,515 | | | 1,253 | | |
| Sharholder's equity | 20,198 | | | 17,423 | | | 14,711 | | |
| Total average liabilities and shareholders' equity | $ 245,290 | | | $ 237,868 | | | $ 226,121 | | |
| Net interest income | | $ 12,895 | | | $ 13,450 | | | $ 11,562 | |
| Net interest margin | | | 5.92% | | | 6.38% | | | 5.79% |

The Company's net yield on interest-earning assets is affected by changes in the rates earned and paid and the volume of interest-earning assets and interest-bearing liabilities. The impact of changes in volume and rate on net interest income are shown in the following table:

| | Year Ended December 31, 2007 over Year Ended December 31, 2006 | | | Year Ended December 31, 2006 over Year Ended December 31, 2005 | | |
|---|---|---|---|---|---|---|
| | Increase (Decrease) Due to Change in (000's) | | | Increase (Decrease) Due to Change in (000's) | | |
| | Volume | Rate | Change | Volume | Rate | Change |
| Interest-bearing Assets: | | | | | | |
| Net Loans | (495) | 129 | (366) | 2,075 | 1,575 | 3,650 |
| Investment Securities | 459 | 494 | 953 | (366) | 226 | (140) |
| Federal funds sold | 102 | 3 | 105 | (107) | 78 | (29) |
| Interest-earning deposits | — | — | — | — | — | — |
| Total interest income | 66 | 626 | 692 | 1,602 | 1,879 | 3,481 |
| Interest-bearing Liabilities: | | | | | | |
| Interest bearing demand - NOW | (3) | 20 | 17 | (8) | 4 | (4) |
| Money Market | 18 | 201 | 219 | (102) | 159 | 57 |
| Savings | — | 67 | 67 | 1 | 88 | 89 |
| Time Certificates of deposit | 542 | 299 | 841 | 528 | 593 | 1,121 |
| Short-term borrowings | (14) | — | (14) | 43 | 6 | 49 |
| Long-term borrowings | 16 | 101 | 117 | 16 | 265 | 281 |
| Total interest expense | 559 | 688 | 1,247 | 478 | 1,115 | 1,593 |
| Interest differential or net interest income | $ (493) | $ (62) | $ (555) | $ 1,124 | $ 764 | $ 1,888 |

***Noninterest Income***

Noninterest income totaled $1,071,000 compared to $1,010,000 for the same period in 2006. That represents an increase of $61,000 or 6.0%. The increase was primarily due to the recovery of legal fees and costs on a previously charged off loan and an increase in interest income derived from the investment in bank owned life insurance.

Service charges on deposit accounts totaled $583,000, which represents a decrease of $33,000 or 5.4% over the same period in 2006. The decrease in service charges was primarily due to the decrease in non sufficient fund fees collected.

Other noninterest income totaled $488,000 compared to $394,000 for the same period in 2006. That represents an increase of $94,000 or 23.9%. The increase is primarily due to the recovery of legal fees and costs on a previously charged off loan and an increase in interest income derived from the investment in bank owned life insurance.

Refer to the "Statement of Earnings" for a breakdown of noninterest income.

***Noninterest Expense***

Noninterest expense increased $439,000 or 5.1% in 2007 over 2006 to $9,029,000 as compared to an increase of $782,000 or 10.0% in 2006 over 2005. The overall increase can be largely attributed to the continued growth of the Company.

Salaries and related expenses increased $516,000 or 10.9% from 2006 to 2007 compared to an increase of $501,000 or 11.8% between 2005 and 2006. This increase is attributed to normal staff related increases, coupled with a 17.7% increase in group health insurance and a $54,000 shared-based payment, which is part of SFAS 123(R), "Share-Based Payment." SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values.

Occupancy expense for the year ended December 31, 2007 totaled $628,000, which reflects a decrease of $36,000 or 5.4% over the same period in 2006. This was primarily due to a decrease in real estate taxes coupled with fewer maintenance and repair costs.

Equipment expense for the year ended December 31, 2007 totaled $666,000, which reflects a decrease of $25,000 or 3.6% over the same period in 2006. This was primarily due to the eliminations of depreciation expense associated with fully depreciated equipment in the Santa Maria office.

Professional services for the year ended December 31, 2007 totaled $427,000, which reflects a decrease of $111,000 or 20.6% over the same period in 2006. This was primarily due to the decreases in legal and other professional services.

Data processing expense for the year ended December 31, 2007 totaled $489,000, which reflects an increase of $21,000 or 4.5% from the same period in 2006. This was primarily due to a 5.1% increase in contracted fees coupled with the continued growth of the Company.

Office expenses increased $2,000 from $360,000 in 2006 to $362,000 in 2007.

Marketing expense increased $15,000 or 3.7% from $408,000 in 2006 to $423,000 in 2007.

Director fees and expenses for the year ended December 31, 2007 totaled $329,000, which reflects an increase of $66,000 or 25.1% over the like period in 2006. The primary reason for the increase was a $56,000 stock option expense recognized for new option grants made in late 2006.

Messenger and courier expenses increased $9,000 or 6.1% from $148,000 in 2006 to $157,000 in 2007.

Other expense decreased $17,000 or 7.0% from $242,000 in 2006 to $225,000 in 2007. This decrease was due to $9,000 decrease in inspection fees associated with construction loans.

The Company's efficiency ratio for 2007 was 64.7%. This represents an increase from the 2006 efficiency ratio of 60.4%, which was a decrease from the 2005 ratio of 63.4%. The increase in the efficiency ratio was primarily due to the decrease in the net interest margin, and the increase in non interest expense.

Refer to the "Statement of Earnings" for a breakdown of noninterest expense.

***Income Taxes***

The provision for income taxes was $1,934,000 in 2007, $2,242,000 in 2006 and $1,759,000 in 2005. The effective tax rate was 39.1% in 2007 as compared to 39.9% in 2006 and 39.0% in 2005. This decrease was partially due to an increasing percentage of tax-free investments.

**Financial Condition**

In 2007, the Company's consolidated total assets increased to $248,640,000 compared to $240,738,000 in 2006 and $231,532,000 in 2005 for increases of 3.3%, 4.0% and 9.4% respectively.

Total deposits decreased $270,000 to $212,718,000 compared to $212,988,000 in 2006 and $206,879,000 in 2005 for a decrease of 0.1% for 2007, and increases of 3.0% and 6.2% for 2006 and 2005 respectively. Deposit competition continues to be very strong in both the traditional bank deposits and alternative investments available in the market place.

Securities available for sale totaled $56,107,000 at December 31, 2007, compared to $42,778,000 at December 31, 2006 and $41,830,000 at December 31, 2005. This represents an increase of 31.2% over December 31, 2006. The increase in securities was primarily due to the decrease in loan demand, which is the result of the softening in the construction and real estate markets.

***Loan Portfolio***

Total loans outstanding averaged $163,741,000 in 2007 compared to $169,139,000 in 2006. This represents a decrease of $5,398,000 or 3.2% in 2007 compared to an increase of $23,944,000 or 16.5% in 2006. Actual net loans at December 31, 2007 equaled $166,619,000 for a decrease of $3,060,000 or 1.8 % over 2006.

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

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (dollars in thousands) | | | | |
| Commercial | $ 38,017 | $ 36,407 | $ 34,139 | $ 32,797 | $ 30,490 |
| Real Estate – construction | 47,819 | 55,307 | 52,696 | 29,707 | 25,446 |
| Real Estate – other | 81,895 | 78,757 | 66,390 | 63,433 | 53,931 |
| Consumer | 1,237 | 1,604 | 1,533 | 1,570 | 1,645 |
| Total gross loans | 168,968 | 172,075 | 154,758 | 127,507 | 111,512 |
| Less: unearned fees | (676) | (741) | (725) | (721) | (451) |
| Less: allowance for loan losses | (1,673) | (1,654) | (1,470) | (1,200) | (1,112) |
| Total net loans | $ 166,619 | $ 169,680 | $ 152,563 | $ 125,586 | $ 109,949 |

| | | | | | |
|---|---|---|---|---|---|
| Weighted average yield on loans for the year | 9.2% | 9.1% | 8.1% | 7.3% | 7.3% |

The following table sets forth the amount of total loans outstanding at December 31, 2007 by contractual maturity date:

| | One Year or Less | After One Year Through Five Years | After Five Years | Total |
|---|---|---|---|---|
| | | (dollars in thousands) | | |
| Commercial | $ 24,140 | $ 6,865 | $ 7,011 | $ 38,016 |
| Real Estate – construction | 42,862 | 4,505 | 453 | 47,820 |
| Real Estate – other | 5,307 | 7,310 | 69,278 | 81,895 |
| Consumer | 607 | 466 | 164 | 1,237 |
| | $ 72,916 | $ 19,146 | $ 76,906 | $ 168,968 |

A significant portion of the loan portfolio of the Company is dependent on real estate. At December 31, 2007, real estate served as the principal source of collateral with respect to 78.5% of the Company’s loan portfolio. A decline in current economic conditions could have an adverse effect on the demand for new loans even if rates continue to decline. It is also understood that the ability of borrowers to repay outstanding loans, the value of real estate and other collateral securing loans and the value of real estate owned by the Company, could affect the Company’s financial condition and results of operations in general and the market value of the Company’s common stock. Acts of nature, including earthquakes and floods, which may cause uninsured damage and other loss of value to real estate that secures these loans, may also negatively impact the Company’s financial condition.

Real estate construction and other real estate loans equaled $129,715,000 or 78.5% of the total loan portfolio and $134,065,000 or 77.9% of the total loan portfolio at December 31, 2007 and 2006, respectively. Other real estate loans are comprised of loans to individuals for their businesses, consumer real estate loans including home equity lines of credit and loans for farmland, including vineyards. The Company has known for some time that it has a concentration in commercial real estate loans. As a means to more closely monitor this concentration, the Company has instituted the use of NAICS codes to monitor industry trends within its commercial real estate portfolio. As of December 31, 2007, the Company had $72,608,000 or 43.0% of its loans in commercial real estate. Of this number, $45,960,000 or 63.3% is commercial real estate for owners use. No industry type exceeds 5.0% of total loans. The remaining $26,648,000 or 36.7% is commercial real estate for non-owners use. Commercial real estate loans for non-owners use as a percentage of total loans equates to 16.0%. We watch the commercial real estate loans for non-owners use along with changes within our owners use very closely and are familiar with the individuals and projects and at this time we do not foresee any problems or undue risk in this segment of our portfolio. Total real estate loans decreased $4,350,000 or 3.2% in 2007 over 2006 compared to an increased of $14,705,000 or 12.3% in 2006 over 2005. The decrease is spread throughout construction of residential units held for resale or for the borrower’s personal residence, off-site development, or land held for future development of commercial or residential properties. The Company has seen a significant decrease in the number of residential construction loans, due to the softening in the real estate market. The Company has loans to customers with a long history of successful developments in our market areas, as well as a long-term relationship with Santa Lucia Bank. The Company has experience and knowledge in construction lending and does not feel that there is any undue risk to the Company. These loans are secured by real estate, and in general, do not exceed 75% of the appraised value on commercial residential real estate or 80% on an individual’s personal residence.

The Company makes commercial loans to small and mid-size businesses for various reasons, including working capital, inventory and equipment. Commercial loans equaled $38,017,000 or 22.5% of the total loan portfolio and $36,407,000 or 21.2% of the total loan portfolio at December 31, 2007 and 2006, respectively. Commercial loans increased $1,610,000 or 4.4% from 2006 to 2007 compared to an increase of $2,268,000 or 6.6% in 2006 over 2005.

It has always been a part of our business banking practice to loan to small businesses for their facilities as well as their other business needs.

Consumer and other loans equaled $1,237,000 or 0.7% of the total loan portfolio at December 31, 2007 compared to $1,604,000 or 0.9% at December 31, 2006. Consumer loans decreased $367,000 or 22.9% in 2007 over 2006 compared to an increase of $71,000 or 4.6% in 2006 over 2005.

The Company had undisbursed loans totaling $57,326,000, $56,557,000, and $53,280,000 as of December 31, 2007, December 31, 2006 and December 31, 2005, respectively. Standby Letters of Credit accounted for $4,286,000, $2,603,000 and $1,546,000 of the undisbursed loans as of December 31, 2007, December 31, 2006 and December 31, 2005, respectively. The Company uses the same credit policies in making these commitments as is done for all of its lending activities. As such, the credit risk involved in these transactions is the same as that involved in extending loan facilities to customers.

Loans with maturities greater than one year at December 31, 2007 include approximately $40,803,000 of fixed rate loans or 24.2% of the total loan portfolio compared to $11,060,000 or 6.4% of the total loan portfolio as of December 31, 2006 and $7,642,000 or 4.9% of the total loan portfolio as of December 31, 2005. The balance of the loans that have maturities of one year or less, or are variable rate loans at December 31, 2007 totaled $128,165,000 or 31.8% compared to $161,015,000 or 93.6% as of December 31, 2006 and $147,116,000 or 95.1% as of

December 31, 2005. The $69.3 million in other real estate loans with five years or greater maturities are primarily owner occupied commercial properties. The Company has attempted to lengthen the maturities of loans in its portfolio to add additional stability to the loan portfolio.

***Nonperforming loans***

Interest income is accrued daily as earned on all 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 based on the contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectibility. 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.

The composition of nonperforming loans as of the end of the last five fiscal years is summarized in the following table:

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | **2007** | **2006** | **2005** | **2004** | **2003** |
| | (dollars in thousands) | | | | |
| Nonaccrual loans: | | | | | |
| Commercial | $ 113 | $ — | $ — | $ — | $ 23 |
| Real estate | 2,062 | — | 135 | 758 | 805 |
| Consumer | — | — | — | — | — |
| Total | 2,175 | — | 135 | 758 | 828 |
| Loans 90 days or more past due and still accruing: | | | | | |
| Real estate | — | — | — | — | — |
| Consumer | — | — | — | — | — |
| Commercial | — | 550 | — | — | — |
| Total | — | 550 | — | — | — |
| Total nonperforming loans: | 2,175 | 550 | 135 | 758 | 828 |
| OREO | — | — | — | — | — |
| Total nonperforming assets: | $ 2,175 | $ 550 | $ 135 | $ 758 | $ 828 |
| Nonperforming assets as a percentage of total gross loans | 1.29% | 0.32% | 0.09% | 0.59% | 0.74% |
| Nonperforming assets as a percentageof total assets | 0.87% | 0.23% | 0.06 % | 0.36% | 0.45% |
| Allowance for loan losses to nonperforming loans | 76.92% | 300.73% | 1088.89 % | 158.31% | 134.30% |

The Company had three nonperforming loans totaling $2,175,000 as of December 31, 2007, compared to one nonperforming loan totaling $550,000 at December 31, 2006 and one nonperforming loan totaling $135,000 at December 31, 2005. Of the Company's nonperforming loans, two are well secured by residential real estate with minimal loss exposure. The commercial loan for $113,000 is 50% guaranteed by the U. S. Small Business Administration, and is secured by business assets of the borrower in addition to the personal residence of the guarantor. The Company is in the process of assessing the value of its collateral and any actual loss is unknown at this time. The Company has however, assigned loan loss reserves in an amount it feels is adequate to satisfy any potential loss based on the collateral.

There were no significant loans that were current as of December 31, 2007, where serious doubt existed as to the ability of the borrower to comply with the present loan repayment terms or that represent a "troubled debt restructuring."

The Company had no "Other Real Estate Owned" (OREO) property as of December 31, 2007.

The Company experienced net charge-offs (recoveries) of ($19,000), $56,000 and $30,000 in 2007, 2006 and 2005 respectively.

***Quality of loans***

Inherent in lending is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan extended and the creditworthiness of the borrower. To reflect the estimated risks of loss associated with its loan portfolio, provisions are made to the Company’s allowance for possible loan losses. As an integral part of this process, the allowance for possible loan losses is subject to review and possible adjustment as a result of regulatory examinations conducted by governmental agencies and through management’s assessment of risk. The Company’s entire allowance is a valuation allocation; that is, it has been created by direct charges against operations through the provision for possible loan losses.

The Company evaluates the allowance for possible loan losses based upon an individual analysis of specific categories of loans, specific categories of classified loans and individual classified assets. The adequacy of the allowance is determinable only on an approximate basis, since estimates as to the magnitude and timing of loan losses are not predictable because of the impact of external events. In addition, the Company contracts with an independent loan review firm to evaluate overall credit quality on an ongoing basis. Management then considers the adequacy of the allowance for possible loan losses in relation to the total loan portfolio.

The provision for possible loan losses charged against operating expense is based upon an analysis of the actual migration of loans to losses plus an amount for other factors that, in management’s judgment, deserve recognition in estimating possible loan losses. These factors include numerous items among which are: specific loan conditions as determined by management; the historical relationship between charge-offs and the level of the allowance; the estimated future loss in all significant loans; known deterioration in concentrations of credit; certain classes of loans or pledged collateral; historical loss experience based on volume and type of loan; the results of any independent review or evaluation of the loan portfolio quality conducted by or at the direction of the Company's management or by bank regulatory agencies; trends in portfolio volume, maturity, and composition; off-balance sheet credit risk; volume and trends in delinquencies and nonaccruals; lending policies and procedures including those for charge-off, collection, and recovery; national and local economic conditions and downturns in specific local industries; and the experience, ability, and depth of the lending staff and management. The Company evaluates the adequacy of its allowance for possible loan losses quarterly.

It was management's decision that no additional loan loss provision was needed during 2007 primarily based on the foregoing analysis and due to the decline of $10.3 million in real estate and construction loans during the first nine months ended September 30, 2007. During the last quarter of 2007, real estate and construction loans increased approximately $6.0 million however; year to date gross loans have decreased $3.1 million or 1.8%.

The following table summarizes the allocation of the allowance for loan losses by type for the years indicated and the percent loans in each category to total loans:

| | Year Ended December 31 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | 2006 | | 2005 | | 2004 | | 2003 | |
| | (dollars in thousands) | | | | | | | | | |
| | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent | Amount | Loan Percent |
| Commerical | $ 525 | 22.50% | $ 495 | 21.16% | $ 536 | 22.06% | $ 502 | 25.72% | $ 460 | 27.34% |
| Real Estate - construction | 229 | 28.30% | 126 | 32.14% | 118 | 34.05% | 71 | 23.30% | 55 | 22.82% |
| Real Estate - other | 572 | 48.47% | 362 | 45.77% | 274 | 42.90% | 281 | 49.75% | 224 | 48.36% |
| Consumer | 32 | 0.73% | 38 | 0.93% | 36 | 0.99% | 39 | 1.23% | 155 | 1.48% |
| Unallocated | 315 | n/a | 633 | n/a | 506 | n/a | 307 | n/a | 218 | n/a |
| Total | $ 1,673 | 100.00% | $ 1,654 | 100.00% | $ 1,470 | 100.00% | $ 1,200 | 100.00% | $ 1,112 | 100.00% |

Management views the allowance for loan losses of $1,673,000 or .99% of total loans as of December 31, 2007 to be adequate after considering the above factors. This allowance is compared to $1,654,000 or .96% in 2006 and $1,470,000 or .95% in 2005. However, there can be no assurance that in any given period the Company will not sustain charge-offs that are substantial in relation to the size of the allowance.

The allocation of the allowance for possible loan losses as of the end of the last five fiscal years is summarized in the following table:

| | Year Ended December 31 | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (dollars in thousands) | | | | |
| **Outstanding loans:** | | | | | |
| Average for the year (net) | $ 163,741 | $ 169,139 | $ 145,195 | $ 115,255 | $ 109,148 |
| End of the year (net) | 166,619 | 169,680 | 152,563 | 125,586 | 109,949 |
| Allowance for loan losses: | | | | | |
| Balance at beginning of year | $ 1,654 | $ 1,470 | $ 1,200 | $ 1,112 | $ 1,026 |
| Actual charge-offs: | | | | | |
| Commercial | 51 | 77 | 43 | 22 | 16 |
| Real estate | — | — | — | — | — |
| Consumer | — | — | — | — | — |
| All other (including overdrafts) | 10 | 6 | 3 | 1 | 17 |
| Total charge-offs | 61 | 83 | 46 | 23 | 33 |
| **Less Recoveries:** | | | | | |
| Commercial | 4 | 26 | 15 | — | 4 |
| Real estate | 76 | — | — | — | — |
| Consumer | — | — | — | — | — |

| | | | | | |
|---|---|---|---|---|---|
| All other (including overdrafts) | — | 1 | 1 | 1 | — |
| Total recoveries | 80 | 27 | 16 | 1 | 4 |
| Net loan charge-offs (recoveries) | (19) | 56 | 30 | 22 | 29 |
| Provision for loan loss | — | 240 | 300 | 110 | 115 |
| Balance at end of period | $ 1,673 | $ 1,654 | $ 1,470 | $ 1,200 | $ 1,112 |
| **Ratios:** | | | | | |
| Net loan charge-offs (recoveries) to average loans | -0.01% | 0.03% | 0.02% | 0.02% | 0.03% |
| Allowance for loan losses to end of year loans | 0.99% | 0.96% | 0.95% | 0.94% | 1.00% |
| Net loan charge-offs (recoveries) to allowance for loan losses | -1.14% | 3.39% | 2.04% | 1.83% | 2.61% |
| Net loan charge-offs (recoveries) to provision charged to operating expense | 0.00% | 23.33% | 10.00% | 20.00% | 25.22% |

***Investment Securities***

The average balance of Federal Funds Sold (overnight investments with other banks) was $4,954,000 in 2007, $2,941,000 in 2006, and $5,685,000 in 2005. These investments are maintained primarily for the short-term liquidity needs of the Company. The major factors influencing the levels of required liquidity are the loan demand of the Company's customers and fluctuations in the Company's deposits. The Company's loan-to-deposit ratio averaged 76.1% in 2007, compared to 79.7% in 2006, and 69.9% in 2005.

Average total investment securities increased by $10,451,000 or 27.1% during 2007, compared to a decrease of $10,087,000 or 20.7% in 2006. The Company focused on maximizing investment opportunities during 2007, due to the softening of the loan demand which decreased by $7,105,000 in average loans or 4.2%. The aggregate market value of the investment portfolio was $334,000 over the amortized cost as of December 31, 2007. As of December 31, 2007, the Company had the ability and intent to hold securities to maturity and saw a significant market value increase of $796,000 over 2006. It is the Company's policy not to engage in securities trading transactions. There are no investments in the portfolio deemed to be permanently impaired. The Company has classified all of its investment securities as available for sale. The exposure to sub prime loans in the Mortgage-Backed securities portfolio is minimal due to the fact these securities are guaranteed by United States Government Agencies and, as such, can be viewed as having credit risk comparable to United States Treasury securities.

| | December 31 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2007 | | | | 2006 | | | |
| | Amortized Cost | Unrealized Gains | Unrealized (Losses) | Estimated Fair Value | Amortized Cost | Unrealized Gains | Unrealized (Losses) | Estimated Fair Value |
| Securities available for sale: | | | | | | | | |
| U.S. Government and Agency securities | $24,097,314 | $243,699 | $ — | $24,341,013 | $19,094,065 | $ 3,029 | $ (76,599) | $19,020,495 |
| State and Political Subdivisions | $ 6,527,226 | $ 30,399 | $ (50,333) | $ 6,507,292 | $ 4,805,053 | $ 9,970 | $ (89,397) | $ 4,725,626 |
| Mortgage-Backed Securities | $25,148,131 | $207,770 | $ (97,050) | $25,258,851 | $19,340,821 | $ 20,303 | $(328,828) | $19,032,296 |
| Total | $55,772,671 | $481,868 | $(147,383) | $56,107,156 | $43,239,939 | $ 33,302 | $(494,824) | $42,778,417 |

The amortized cost, estimated fair value, and weighted average yield for investment securities available for sale based on maturity date are set forth in the table below. The weighted average yield is based on the amortized cost of the securities using a method that approximates the level yield method:

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | |
| | Book Value | Market Value | Weighted Average Yield | Book Value | Market Value | Weighted Average Yield |
| **Available-for-Sale Securities:** | | | | | | |
| U.S. Government and Agency Securities | | | | | | |
| One Year or Less | 8,002,724 | 8,026,354 | 5.27% | 8,998,769 | 8,924,794 | 3.59% |
| One to Five Years | 14,094,590 | 14,310,616 | 5.07% | 8,095,296 | 8,095,701 | 5.03% |
| Five to Ten Years | 2,000,000 | 2,004,043 | 5.00% | 2,000,000 | 2,000,000 | 5.10% |
| Over Ten Years | — | — | | — | — | |
| Total U.S. Agency | 24,097,314 | 24,341,013 | 5.13% | 19,094,065 | 19,020,495 | 4.36% |
| **State and Political Subdivisions:** | | | | | | |
| One Year or Less | 1,061,296 | 1,070,745 | 6.23% | 708,100 | 702,151 | 4.36% |
| One to Five Years | 3,020,931 | 2,998,510 | 4.99% | 3,859,382 | 3,790,725 | 5.20% |
| Five to Ten Years | 2,444,999 | 2,438,037 | 6.26% | 237,571 | 232,750 | 5.74% |
| Over Ten Years | — | — | | — | — | |
| Total State & Political | 6,527,226 | 6,507,292 | 5.67% | 4,805,053 | 4,725,626 | 5.10% |

| | | | | | | |
|---|---|---|---|---|---|---|
| Subdivisions | | | | | | |
| **Mortgage Backed Securities:** | | | | | | |
| One Year or Less | 3,430,820 | 3,441,374 | 4.70% | 3,650,978 | 3,590,877 | 4.26% |
| One to Five Years | 14,849,863 | 14,894,034 | 4.66% | 11,261,147 | 11,033,390 | 4.20% |
| Five to Ten Years | 3,869,173 | 3,907,814 | 5.05% | 2,711,676 | 2,695,483 | 4.63% |
| Over Ten Years | 2,998,275 | 3,015,629 | 4.90% | 1,717,020 | 1,712,546 | 4.71% |
| Total Mortgage Backed Securities | 25,148,131 | 25,258,851 | 4.75% | 19,340,821 | 19,032,296 | 4.32% |
| Total Available-for-Sale Securities | $55,772,671 | $56,107,156 | 5.02% | $43,239,939 | $42,778,417 | 4.42% |

***Deposits***

Total average deposits increased $3,020,000 or 1.4% during 2007, compared to an increase of $4,391,000 or 2.1% in 2006 and an increase of $24,109,000 or 13.1% in 2005. Average noninterest-bearing deposits decreased $7,669,000 or 8.6% in 2007, compared to an increase of $1,017,000 or 1.2% in 2006 and an increase of $10,896,000 or 14.1% in 2005. Average interest-bearing deposits increased $10,689,000 or 8.7% in 2007 compared to an increase of $3,374,000 or 2.8% in 2006 and an increase of $13,213,000, or 12.5% in 2005.

The chart below indicates a shift in lower interest-bearing deposits (NOW, Money Market and Savings) to higher interest rate Time Certificates of Deposit. This appears to be a trend that is common throughout the local banking industry and is expected to continue in 2008. This was management's strategy to retain and attract deposits to offset loss of funds to non-bank competition.

The following table summarizes the distribution of average deposits and the average rates paid for the period indicated:

| | December 31 | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2006 | | 2005 | |
| | Average Balance | Average Rate | Average Balance | Average Rate | Average Balance | Average Rate |
| | (dollars in thousands) | | | | | |
| Noninterest-bearing demand deposits | $ 81,714 | | $ 89,383 | | $ 88,366 | |
| Money Market Accounts | 24,929 | 2.90% | 24,103 | 2.09% | 30,186 | 1.48% |
| NOW accounts | 13,391 | 0.41% | 14,696 | 0.26% | 17,834 | 0.24% |
| Savings deposits | 27,076 | 1.07% | 28,074 | 0.79% | 30,560 | 0.44% |
| Time deposits of $100,000 or more | 39,242 | 4.67% | 29,800 | 4.21% | 19,859 | 2.93% |
| Other time deposits | 28,777 | 4.60% | 26,053 | 4.08% | 20,913 | 2.94% |
| Total deposits | $215,129 | 1.96% | $212,109 | 1.45% | $207,718 | 0.87% |

The remaining maturities of the Company's certificates of deposit in the amount of $100,000 or more as of December 31, 2007 are indicated in the table below. Interest expense on these certificates of deposit totaled $1,834,000 in 2007:

| Deposits Maturing in | December 31, 2007 |
|---|---|
| Three months or less | $ 15,967,166 |
| Over three months through six months | 10,750,684 |
| Over six months through twelve months | 8,958,008 |
| Over twelve months | 3,153,935 |
| Total | $ 38,829,793 |

***Capital***

The Bank is required to maintain a minimum leverage-capital ratio of Tier I (as defined) to total assets based on the Bank's ratings under the regulatory rating system. At the end of 2007, all Bank capital ratios were above all current Federal capital guidelines for a "well capitalized" bank. As of December 31, 2007 the regulatory total capital to risk-weighted assets ratio was 13.8% compared to 13.1% as of December 31, 2006 and 11.3% as of December 31, 2005. The regulatory Tier I capital to risk-weighted assets ratio was 12.3% on December 31, 2007 compared to 11.4% on December 31, 2006 and 9.3% as of December 31, 2005. The regulatory Tier I capital to average assets ratio was 9.9% as of December 31, 2007 compared to 9.1% as of December 31, 2006 and 7.2% as of December 31, 2005.

The Bank's Tier I Capital ratio increased 74 basis points and the Bank's Total Capital to Risk Weighted Assets ratio increased 67 basis points, due to the strong earnings of $3.2 million for 2007.

***Short-term Borrowings***

The Bank has two borrowing arrangements with the Federal Home Loan Bank of San Francisco. The first allows the Bank to borrow up to approximately $41 million against which the Bank has pledged approximately $100 million of its real estate secured loans. The second arrangement allows the Bank to borrow up to approximately $12 million against which the Bank has pledged approximately $12 million of its investment securities.

As of December 31, 2007 the Bank has borrowed $5,900,000 under these arrangements. This amount is due on January 2, 2008 and includes interest at 3.25%. During 2007 the bank had average borrowings outstanding of $1,100,000 at an effective rate of 4.55%.

***Long-term Borrowings***

Santa Lucia Bancorp issued $5,155,000 in junior subordinated debt securities (the “debt securities”) to the Santa Lucia Bancorp (CA) Capital Trust, a statutory trust created under the laws of the State of Delaware. These debt securities are subordinated to effectively all borrowings of the Company and are due and payable on July 7, 2036. These debt securities may be redeemed for 105% of the principal balance through July 7, 2011 and then at par thereafter. Interest is payable quarterly beginning July 7, 2006 at 1.48% over the quarterly adjustable 3-month LIBOR. Of this $5.2 million, the Company contributed $3.0 million to the Bank and retained $2.0 million at the Company level. The securities do not entitle the holders to voting rights in the Company but will contain certain restrictive covenants, including restrictions on the payment of dividends to the holders of the Company’s common stock in the event that interest payments on the trust preferred securities are postponed. The capital received from the trust preferred issuance is designated as Tier 1 capital for regulatory purposes.

During the third quarter of 2003, the Bank undertook and completed a private placement of subordinated debentures (“notes”) to augment its Tier 2 capital. The total principal amount of the notes issued was $2,000,000. The notes were sold pursuant to an applicable exemption from registration under the Securities Act of 1933 to certain accredited investors, including some of the Company’s directors and executive officers. The notes include quarterly payment of interest at prime plus 1.5% and quarterly principal installments of approximately $166,666 commencing on September 30, 2008 until paid in full on June 30, 2011.

***Interest Rate Sensitivity and Liquidity***

The Company closely follows the maturities and repricing opportunities of both assets and liabilities to reduce gaps in interest spreads. An analysis is performed quarterly to determine the various interest sensitivity gaps that exist. In general, the Company is asset sensitive, meaning that when interest rates change, assets (loans) will reprice faster than short-term liabilities (deposits). Therefore, higher interest rates improve short-term profits and lower rates decrease short-term profits. Currently, management’s analysis indicates that the Company’s asset sensitive position would not materially affect income for interest rate changes of one percent or less in one year.

The following table presents the Bank’s Rate Sensitivity Gap Report as of December 31, 2007.

| | 0-3 months | 3-12 months | 1-3 years | 3-5 years | Beyond | Non-Rate Sensitive | Total |
|---|---|---|---|---|---|---|---|
| | | | (dollars in thousands) | | | | |
| **Interest sensitive assets:** | | | | | | | |
| Investment securities | $ 5,183 | $ 3,857 | $ 17,594 | $ 21,189 | $ 9,405 | $ — | $ 57,228 |
| Loan receivables | 90,316 | 27,823 | 32,983 | 14,578 | 3,268 | — | 168,968 |
| Federal funds sold | — | — | — | — | — | — | — |
| Non-earning assets | — | — | — | — | — | 21,847 | 21,847 |
| **Total assets** | $ 95,499 | $ 31,680 | $ 50,577 | $ 35,767 | $ 12,673 | $ 21,847 | $248,043 |
| **Interest sensitive liabilities:** | | | | | | | |
| Demand deposits | $ — | $ — | $ — | $ — | $ — | $ 76,829 | $ 76,829 |
| NOW accounts | 349 | 1,048 | 2,796 | 2,795 | 5,008 | — | 11,996 |
| Money Market Accounts | 2,522 | 7,565 | 16,811 | — | — | — | 26,898 |
| Savings deposits | 930 | 2,789 | 7,436 | 7,436 | 7,746 | — | 26,337 |
| Time deposits | 26,851 | 37,950 | 6,189 | 705 | 149 | — | 71,844 |
| Total saving and time deposits | $ 30,652 | $ 49,352 | $ 33,232 | $ 10,936 | $ 12,903 | $ 76,829 | $213,904 |
| Short-term borrowing | 5,900 | — | — | — | — | — | 5,900 |
| Long-term borrowing | 2,000 | — | — | — | — | — | 2,000 |
| Non-funding liabilities and capital | — | — | — | — | — | 26,239 | 26,239 |
| Total liabilities and capital | $ 38,552 | $ 49,352 | $ 33,232 | $ 10,936 | $ 12,903 | $103,068 | $248,043 |
| Interest rate sensitivity gap | $ 56,947 | $ (17,672) | $ 17,345 | $ 24,831 | $ (230) | | |
| **Risk Indicators from GAP** | | | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| **Analysis:** | | | | | |
| Cumulative GAP | $ 56,947 | $ 39,275 | $ 56,620 | $ 81,451 | $ 81,221 |
| Cumulative GAP (% of total assets) | 22.96% | 15.83% | 22.83% | 32.84% | 32.74% |

The asset liability reports indicate that the Bank has an actual dollar risk exposure of $574,000 if interest rates fall 100 basis points. This represents a -4.5% risk to interest income.

| | Interest Income and Expense Under Rate Shock | | | | |
|---|---|---|---|---|---|
| | -200bp | -100bp | 0bp | +100bp | +200bp |
| Net Interest Income | | | | | |
| Earnings at Risk | $ (1,088) | $ (574) | $ 0 | $ 471 | $ 931 |
| Percent of Risk | -8.5% | -4.5% | 0.00% | 3.7% | 7.3% |
| Equity Ratio | 14.3% | 15.1% | 16.0% | 16.7% | 17.3% |

The Company closely monitors its liquidity so that the cash requirements for loans and deposit withdrawals are met in an orderly manner. Management monitors liquidity in relation to trends of loans and deposits for short term and long-term requirements. Liquidity sources are cash, deposits with other banks, overnight Federal Fund investments, investment securities and the ability to sell loans. As of December 31, 2007, the Bank's liquidity ratio was 25.0% compared to 24.5% at December 31, 2006 and 27.7% at December 31, 2005. The 25.0% liquidity ratio at December 31, 2007 is well within the Company's policy limit.

**Critical Accounting Policies**

This discussion should be read in conjunction with the consolidated financial statements of the Company, including the notes thereto.

Our accounting policies are integral to understanding the 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 applied consistently from period to period. In addition, the 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.

***Use of Estimates in the Preparation of Financial Statements***

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

***Allowance for Loan Losses***

The allowance for loan losses represents management's best estimate of losses inherent in the existing loan portfolio. The allowance for loan losses is increased by the provision for loan losses charged to expense and reduced by loans charged off, net of recoveries. The provision for loan losses is determined based on management's assessment of several factors: reviews and evaluation of specific loans, changes in the nature and volume of the loan portfolio, current economic conditions and the related impact on specific borrowers and industry groups, historical loan loss experiences, the level of classified and nonperforming loans and the results of regulatory examinations.

Loans are considered impaired if, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. The measurement of impaired loans is generally based on the present value of expected future cash flows discounted at the historical effective interest rate stipulated in the loan agreement, except that all collateral-dependent loans are measured for impairment based on the fair value of the collateral. In measuring the fair value of the collateral, management uses assumptions and methodologies consistent with those that would be utilized by unrelated third parties.

Changes in the financial condition of individual borrowers, in economic conditions, in historical loss experience and in the condition of the various markets in which collateral may be sold may all affect the required level of the allowance for loan losses and the associated provision for loan losses.

***Available-for-Sale Securities***

The fair value of most securities classified as available-for-sale are based on quoted market prices. If quoted market prices are not available, fair values are extrapolated from the quoted prices of similar instruments.

***Deferred Tax Assets***

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.

***Deferred Compensation Liabilities***

Management estimates the life expectancy of the participants and the accrual methods used to accrue compensation expense. If individuals outlive their assumed expectancies the amounts accrued for the payment of their benefits will be inadequate and additional changes to income will be required.

**Availability of Form 10-KSB**

If any shareholder would like a copy of the Company's Annual Report on Form 10-KSB for the fiscal year ending December 31, 2007, they can be obtained without charge by sending a written request to John C. Hansen, Executive Vice President and Chief Financial Officer, P. O. Box 6047, Atascadero, California 93423.

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders
Santa Lucia Bancorp and Subsidiary

We have audited the consolidated balance sheets of Santa Lucia Bancorp and Subsidiary (the Company) as of December 31, 2007 and 2006, and the related consolidated statements of earnings, cash flows and shareholders' equity for the three years ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Santa Lucia Bancorp and Subsidiary as of December 31, 2007 and 2006, and the results of its operations and cash flows for the three years ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.

Laguna Hills, California
January 16, 2008

25231 Paseo De Alicia, Suite 100 Laguna Hills, CA 92653 Tel: 949.768.0833 Fax: 949.768.8408 www.vtdcpa.com

**FRESNO • LAGUNA HILLS • PALO ALTO • PLEASANTON • RANCHO CUCAMONGA**

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Balance Sheets**

*December 31, 2007 and 2006*

| | 2007 | 2006 |
|---|---|---|
| **ASSETS** | | |
| Cash and due from banks | $ 7,399,412 | $ 10,139,526 |
| Federal funds sold | — | — |
| TOTAL CASH AND CASH EQUIVALENTS | 7,399,412 | 10,139,526 |
| Securities available for sale | 56,107,156 | 42,778,417 |
| Loans, net | 166,619,494 | 169,680,473 |
| Premises and equipment, net | 8,868,507 | 9,258,207 |
| Deferred income tax assets | 814,000 | 941,000 |
| Cash surrender value of life insurance | 5,005,357 | 3,336,076 |
| Federal Reserve Bank and Federal Home Loan Bank stock, at cost | 1,453,850 | 1,397,700 |
| Accrued interest and other assets | 2,371,999 | 3,206,685 |
| TOTAL ASSETS | $ 248,639,775 | $ 240,738,084 |

| | 2007 | 2006 |
|---|---|---|
| **LIABILITIES & SHAREHOLDERS' EQUITY** | | |
| Deposits | | |
| Noninterest-bearing demand | $ 77,100,561 | $ 86,252,426 |
| Interest-bearing demand and NOW accounts | 11,996,402 | 12,968,951 |
| Money market | 25,440,394 | 20,465,756 |
| Savings | 26,336,827 | 27,383,605 |
| Time certificates of deposit of $100,000 or more | 38,829,793 | 37,226,189 |
| Other time certificates | 33,014,401 | 28,691,525 |
| TOTAL DEPOSITS | 212,718,378 | 212,988,452 |
| Short-term borrowings | 5,900,000 | — |
| Long-term borrowings | 7,155,000 | 7,155,000 |
| Accrued interest and other liabilities | 1,677,551 | 1,457,716 |
| TOTAL LIABILITIES | 227,450,929 | 221,601,168 |
| *Commitments and contingencies (Note M)* | — | _ |
| Shareholders' equity | | |
| Common stock – no par value; 20,000,000 shares authorized; issued and outstanding: 1,924,873 shares at December 31, 2007 and 1,928,097 shares at December 31, 2006 | 9,851,392 | 9,566,563 |
| Additional paid-in capital | 358,203 | 216,558 |
| Retained earnings | 10,782,741 | 9,624,939 |
| Accumulated other comprehensive income-net unrealized losses on available-for-sale securities, net of taxes of $137,975 in 2007 and $190,378 in 2006 | 196,510 | (271,144) |
| TOTAL SHAREHOLDERS' EQUITY | 21,188,846 | 19,136,916 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | $ 248,639,775 | $ 240,738,084 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statements of Earnings**

*Years Ended December 31, 2007, 2006 and 2005*

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Interest income | | | |
| Interest and fees on loans | $ 15,030,928 | $ 15,397,450 | $ 11,747,437 |
| Federal funds sold | 249,434 | 145,314 | 173,515 |
| Investment securities – taxable | 2,232,966 | 1,352,675 | 1,476,915 |
| Investment securities – nontaxable | 205,285 | 131,233 | 148,368 |
| | 17,718,613 | 17,026,672 | 13,546,235 |
| Interest expense | | | |
| Time certificates of deposit of $100,000 or more | 1,833,831 | 1,254,951 | 581,566 |
| Other deposits | 2,389,580 | 1,824,577 | 1,234,377 |
| Long-term debt and other borrowings | 600,727 | 497,610 | 167,979 |
| | 4,824,138 | 3,577,138 | 1,983,922 |
| Net interest income | 12,894,475 | 13,449,534 | 11,562,313 |
| Provision for loan losses | — | 240,000 | 300,000 |
| Net interest income after provision for loan losses | 12,894,475 | 13,209,534 | 11,262,313 |
| | | | |
| Noninterest income | | | |
| Service charges and fees | 583,445 | 615,917 | 602,809 |
| Dividends on cash surrender value of life insurance | 222,071 | 138,181 | 132,319 |
| Mortgage fees | — | 48,487 | 94,972 |
| Gain (loss) on sale of investment securities | — | — | (5,877) |
| Other income | 265,798 | 207,676 | 227,727 |
| | 1,071,314 | 1,010,261 | 1,051,950 |
| Noninterest expense | | | |
| Salaries and employee benefits | 5,259,456 | 4,743,094 | 4,241,897 |
| Occupancy | 627,685 | 664,482 | 565,467 |
| Equipment | 666,003 | 691,028 | 583,772 |
| Professional services | 426,667 | 538,282 | 465,661 |
| Data processing | 488,636 | 468,211 | 439,591 |
| Office expenses | 362,057 | 359,588 | 374,478 |
| Marketing | 422,914 | 407,638 | 397,907 |
| Regulatory assessments | 64,436 | 63,851 | 65,793 |
| Directors' fees and expenses | 328,801 | 263,444 | 261,338 |
| Messenger and courier expenses | 156,870 | 148,335 | 143,834 |
| Other | 225,445 | 241,571 | 268,705 |
| | 9,028,970 | 8,589,524 | 7,808,443 |
| Earnings before income taxes | 4,936,819 | 5,630,271 | 4,505,820 |
| | | | |
| Income taxes | 1,934,000 | 2,242,000 | 1,759,000 |
| Net earnings | $ 3,002,819 | $ 3,388,271 | $ 2,746,820 |
| | | | |
| Per share data: | | | |
| Net earnings – basic | $ 1.55 | $ 1.77 | $ 1.46 |
| Net earnings – diluted | $ 1.51 | $ 1.68 | $ 1.38 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statements of Cash Flows**

*Years Ended December 31, 2007, 2006 and 2005*

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Net earnings | $ 3,002,819 | $ 3,388,271 | $ 2,746,820 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | | |
| Depreciation and amortization | 652,290 | 669,159 | 556,907 |
| Provision for loan losses | — | 240,000 | 300,000 |
| Amortization of investment securities | — | 5,450 | 32,240 |
| Loss (gain) on sale of investment securities | — | — | 5,877 |
| Deferred income taxes | (201,000) | (147,000) | (25,000) |
| Dividends in cash value of life insurance | (222,071) | (138,181) | (132,319) |
| Other items, net | 1,101,676 | (1,131,715) | (432,992) |
| Net cash provided by operating activities | 4,333,714 | 2,885,984 | 3,051,533 |
| | | | |
| Cash flows from investing activities: | | | |
| Proceeds from maturities of investment securities | 14,202,010 | 18,962,594 | 11,007,571 |
| Proceeds from sale of investment securities | — | — | 6,016,550 |
| Purchases of investment securities | (26,658,965) | (19,391,969) | (2,001,378) |
| Purchase of Federal Reserve Bank and Federal Home Loan Bank stock | — | (155,550) | (194,450) |
| Net change in loans | 3,060,979 | (17,357,365) | (27,277,292) |
| Purchases of bank premises and equipment | (262,590) | (466,782) | (347,532) |
| Proceeds from sale of bank premises and equipment | | — | — |
| Proceeds from (purchase of) life insurance | (1,485,000) | — | 132,255 |
| Proceeds from sale of other real estate owned | — | — | — |
| Net cash used in investing activities | (11,143,566) | (18,409,072) | (12,664,276) |
| | | | |
| Cash flows from financing activities: | | | |
| Net change in deposits | (270,074) | 6,109,373 | 12,011,229 |
| Proceeds and tax benefit from exercise of stock options | 164,275 | 372,781 | 416,562 |
| Stock repurchases | (853,351) | — | — |
| Net (repayments) proceeds from borrowings | 5,900,000 | (345,000) | 5,500,000 |
| Cash dividends paid | (871,112) | (767,587) | (729,550) |
| Net cash provided by financing activities | 4,069,738 | 5,369,567 | 17,198,241 |
| Net increase (decrease) in cash and cash equivalents | (2,740,114) | (10,153,521) | 7,585,498 |
| | | | |
| Cash and cash equivalents at beginning of year | 10,139,526 | 20,293,047 | 12,707,549 |
| Cash and cash equivalents at end of year | $ 7,399,412 | $ 10,139,526 | $ 20,293,047 |
| | | | |
| Supplemental disclosure of cash flow information: | | | |
| Interest paid | $ 4,824,138 | $ 3,415,383 | $ 1,957,610 |
| Income taxes paid | $ 1,865,000 | $ 2,415,000 | $ 1,720,000 |
| Cashless exercise of stock options | $ 120,554 | $ 48,034 | $ 32,515 |

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

**Santa Lucia Bancorp and Subsidiary**
**Consolidated Statement of Shareholders' Equity**

*Years Ended December 31, 2007, 2006 and 2005*

| | Comprehensive Income | Common Stock Shares Outstanding | Common Stock Amount | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2005** | | $1,861,764 | $8,849,671 | $ — | $ 5,067,534 | $ (110,291) |
| Cash dividends – $0.3875 per share | | | | | (729,550) | |
| Exercise of stock options, including the realization of tax benefits of $226,000 | | 37,779 | 449,077 | | (32,515) | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 2,746,820 | | | | 2,746,820 | |
| Change in unrealized loss on available-for-sale securities, net of taxes of $265,409 | (378,040) | | | | | (378,040) |
| Less reclassification adjustments for gains included in the net income, net of taxes or $2,410 | 3,467 | | | | | 3,467 |
| **Total Comprehensive Income** | $ 2,372,247 | | | | | |
| **Balance at December 31, 2005** | | 1,899,543 | 9,298,748 | — | 7,052,289 | (484,864) |
| Cash dividends – $0.40 per share | | | | | (767,587) | |
| Exercise of stock options, including the realization of tax benefits of $153,000 | | 28,554 | 267,815 | 153,000 | (48,034) | |
| Stock Option Compensation Expense | | | | 63,558 | | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 3,388,271 | | | | 3,388,271 | |
| Change in unrealized loss on available-for-sale securities, net of taxes or $150,059 | 213,720 | | | | | 213,720 |
| **Total Comprehensive Income** | $ 3,601,991 | | | | | |
| **Balance at December 31, 2006** | | 1,928,097 | $9,566,563 | 216,558 | 9,624,939 | (271,144) |
| Cash dividends – $0.45 per share | | | | | (871,112) | |
| Exercise of stock options, including the realization of tax benefits of $19,000 | | 29,247 | 284,829 | 19,000 | (120,554) | |
| Repurchase and retirement of stock | | (32,471) | | | (853,351) | |
| Stock Option Compensation Expense | | | | 122,645 | | |
| **Comprehensive Income:** | | | | | | |
| Net earnings for the year | $ 3,002,819 | | | | 3,002,819 | |
| Change in unrealized loss on available-for-sale securities, net of taxes of $328,353 | 467,654 | | | | | 467,654 |
| **Total Comprehensive** | $ 3,470,473 | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Income** | | | | | | |
| **Balance at December 31, 2007** | | 1,924,873 | $9,851,392 | $358,203 | $10,782,741 | $ 196,510 |

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

**NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES –** The consolidated financial statements include the accounts of Santa Lucia Bancorp and its wholly owned subsidiary Santa Lucia Bank (the "Bank"), collectively referred to herein as the "Company." All significant intercompany transactions have been eliminated.

The accounting and reporting policies of the Company are in accordance with accounting principles generally accepted in the Unites States of America and prevailing practices within the banking industry. A summary of the significant accounting policies consistently applied in preparation of the accompanying financial statements follows:

**Nature of Operations –** The Company has been organized as a single operating segment and maintains four branches in the San Luis Obispo and northern Santa Barbara Counties. The Company's primary source of revenue is interest income from loans to customers. The Company's customers are predominantly small and middle-market businesses and individuals.

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

**Presentation of Cash Flows –** For the purposes of reporting cash flows, cash and cash equivalents includes cash, noninterest-earning deposits and federal funds sold. Generally, federal funds are sold for one day periods.

**Cash and Due From Banks –** Banking regulations require that all banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Bank was in compliance with the reserve requirements as of December 31, 2007 and 2006.

The Company periodically maintains amounts due from banks that exceed federally insured limits. The Company has not experienced any losses in such accounts.

**Investment Securities –** Bonds, notes, and debentures for which the Company has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity.

Investments not classified as trading securities nor as held-to-maturity securities are classified as available-for-sale securities and recorded at fair value. Unrealized gains or losses on available-for-sale securities are excluded from net income and reported as an amount net of taxes as a separate component of other comprehensive income included in shareholders' equity. Premiums or discounts on held-to-maturity and available-for-sale securities are amortized or accreted into income using the interest method. Realized gains or losses on sales of held-tomaturity or available-for-sale securities are recorded using the specific identification method.

Declines in the fair value of individual held-to-maturity and availablefor-sale securities below their cost that are other-than-temporary result in write-downs of the individual securities to their fair value. The related write-downs are included in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

**Provision and Allowance for Loan Losses –** The determination of the balance in the allowance for loan losses is based on an analysis of the loan portfolio and reflects an amount which, in management's judgment, is adequate to provide for potential credit losses after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience and such other factors as deserve current recognition in estimating credit losses. The provision for loan losses is charged to expenses.

The Company considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Measurement of impairment is based on the expected future cash flows of an impaired loan, which are to be discounted at the loan's effective interest rate, or measured by reference to an observable market value, if one exists, or the fair value of the collateral for a collateral-dependent loan. The Company selects the measurement method on a loan-by-loan basis except that collateral-dependent loans for which foreclosure is probable are measured at the fair value of the collateral. The Company recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans.

**Interest and Fees on Loans –** Interest income is accrued daily as earned on all 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 based on contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectibility. 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. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to all principal and interest. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan.

**Premises and Equipment –** Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives, which ranges from three to ten years for furniture and fixtures and forty years for buildings. Expenditures for betterments or major repairs are capitalized and those for ordinary repairs and maintenance are charged to operations as incurred.

**Other Real Estate Owned –** Other real estate owned represents real estate acquired through foreclosure and is carried at the lower of the recorded investment in the property or its fair value. Prior to foreclosure, the value of the underlying loan is written down to the fair market value of the real estate to be acquired by a charge to the allowance for credit losses, if necessary. Any subsequent write-downs are charged against operating expenses. Operating expenses of such properties, net of related income, are included in other expenses.

**Income Taxes –** Deferred income taxes are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Realization of tax benefits of deductible temporary differences and operating loss carryforwards depends on having sufficient taxable income of an appropriate character within the carryforward periods.

The Company has adopted Financial Accounting Standards Interpretation No. 48 ("Fin 48"), Accounting for Uncertainty in Income Taxes. Fin 48 clarifies the accounting for uncertainty in tax positions taken or expected to be taken on a tax return and provides that the tax effects from an uncertain tax position can be recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Management believes that all tax positions taken to date are highly certain and, accordingly, no accounting adjustment has been made to the financial statements. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

**Advertising Costs –** The Company expenses the costs of advertising in the period incurred.

**Comprehensive Income –** Beginning in 1998, the Company adopted Statement of Financial Accounting Standard ("SFAS") No. 130, *"Reporting Comprehensive Income*" (SFAS No. 130), which requires the disclosure of comprehensive income and its components. Changes in unrealized gain or loss on available-for-sale securities net of income taxes is the only component of accumulated other comprehensive income for the Company.

**Financial Instruments –** In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit as described in Note M. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

**Earnings Per Shares (EPS) –** 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 shared in the earnings of the entity.

**Stock-Based Compensation –** The Company has adopted SFAS No. 123(R) "Shared-Based Payment." This Statement generally requires entities to recognize the cost of employee services received in exchange for awards of stock options, or other equity instruments, based on the grant-date fair value of those awards. This cost is recognized over the period which an employee is required to provide services in exchange for the award, generally the vesting period.

**Change in Accounting Principle –** The Company adopted SFAS No. 123 (R) on January 1, 2006 using the "modified prospective method." Under this method compensation expense is recognized using the fair-value method for all new stock option awards as well as any existing awards that are modified, repurchased or cancelled after January 1, 2006 and prior periods are not restated. In addition, the unvested portion of previously awarded options outstanding as of January 1, 2006 will also be recognized as expense over the requisite service period based on the fair value of those options as previously calculated at the grant date under the pro-forma disclosures of SFAS No. 123. The fair value of each grant is estimated using the Black-Scholes option pricing model. During 2007 and 2006 the Company recognized pre-tax stock-based compensation expense of $122,645 and $63,558, respectively, as a result of adopting SFAS No. 123 (R).

Prior to the adoption of SFAS No. 123 (R), the Company accounted for stock-based awards using the intrinsic value method prescribed in Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Accordingly, compensation cost for stock options was measured as the excess, if any, of the quoted market price of the Company's stock at the date of the grant over the amount an employee must pay to acquire the stock. All of the Company's stock option grants included exercise prices equal to the Company's current market price per share; accordingly, no compensation expense was reported using the intrinsic value method of APB Opinion No. 25.

Had compensation cost for the Company's stock option plans been determined based on the fair value at the grant dates for awards under those plans consistent with the method of SFAS No. 123, the Company's net income and income per share for 2005 would have changed to the pro forma amounts indicated below:

| | 2005 |
|---|---|
| Net income: | |
| As reported | $ 2,746,820 |
| Stock-Based Compensation using the Intrinsic Value Method | — |
| Stock-Based Compensation that would have been reported using the Fair Value Method of SFAS 123 | (43,436) |
| Pro Forma | $ 2,703,384 |
| Per share: | |
| Net Income - Basic | |
| As Reported | $ 1.46 |
| Pro Forma | $ 1.44 |
| Net Income - Diluted | |
| As Reported | $ 1.38 |
| Pro Forma | $ 1.36 |

**Disclosure about Fair Value of Financial Instruments –** SFAS No. 107 specifies the disclosure of the estimated fair value of financial instruments. The Company's estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies.

However, considerable judgment is required to develop the estimates of fair value. Accordingly, the estimates are not necessarily indicative of the amounts the Company could have realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since the balance sheet date and, therefore, current estimates of fair value may differ significantly from the amounts presented in the accompanying notes.

**New Accounting Pronouncements –** In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements", effective for the Company January 1, 2008. This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This Statement defines fair value, establishes a fair value hierarchy that distinguishes between valuations obtained from sources independent of the entity and those from the entity's own observable inputs that are not corroborated by observable market data. SFAS No. 157 expands disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value, and for recurring fair value measurements using significant unobservable inputs, the effect of the measurements on earnings or changes inn net assets for the period. The Company is currently assessing the impact of this pronouncement on its financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115. SFAS 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS 159 are elective; however, the amendments to SFAS 115, Accounting for Certain Investments in Debt and Equity Securities, applies to all entities with available-for-sale or trading securities. For financial instruments elected to be accounted for at fair value, an entity will report the unrealized gains and losses in earnings. SFAS 159 is effective as the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company is currently assessing the impact of this pronouncement on its financial statements.

In September 2006, the FASB ratified the FASB's Emerging Issues Task Force (or EITF) consensus on EITF Issue No. 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements" and in March 2007 the FASB ratified EITF Issue No. 06-10, "Accounting for Collateral Assignment Split-Dollar Life Insurance Arrangements" The EITF's consensus on both of these issues focuses on the accounting for arrangements in which a company has agreed to share a portion of the value of the insurance policy with the employee. These arrangements are referred to as "split-dollar" arrangements. Entities with split-dollar life insurance policies will have to accrue, for years beginning after December 15, 2007, liabilities and associated expense for those insurance benefits under the same rules that apply when such benefits are provided by means other than life insurance. The provisions of the consensus would be applied through a cumulative effect adjustment to retained earnings with the option of retrospective application. The Company has estimated the charged to retained earnings effective January 1, 2008 to be approximately $196,000 net of taxes.

**Reclassification –** Certain reclassifications have been made in the 2006 and 2005 financial statements to conform to the presentation used in 2007. These reclassifications had no impact on the Company's previously reported financial statements.

**NOTE B – INVESTMENT SECURITIES –** The amortized cost, carrying value and estimated fair values of investment securities available for sale as of December 31, are as follows:

| | **December 31, 2007** | | | |
|---|---|---|---|---|
| | **Amortized cost** | **Unrealized gains** | **Unrealized (losses)** | **Estimated fair value** |
| U.S. Government and Agency Securities | $ 24,097,314 | $ 243,699 | $ — | $ 24,341,013 |
| States and Political Subdivisions | 6,527,226 | 30,399 | (50,333) | 6,507,292 |
| Mortgage-Backed Securities | 25,148,131 | 207,770 | (97,050) | 25,258,851 |
| | $ 55,772,671 | $ 481,868 | $ (147,383) | $ 56,107,156 |

| | **December 31, 2006** | | | |
|---|---|---|---|---|
| | **Amortized cost** | **Unrealized gains** | **Unrealized (losses)** | **Estimated fair value** |
| U.S. Government and Agency Securities | $ 19,094,065 | $ 3,029 | $ (76,599) | $ 19,020,495 |
| States and Political Subdivisions | 4,805,053 | 9,970 | (89,397) | 4,725,626 |
| Mortgage-Backed Securities | 19,340,821 | 20,303 | (328,828) | 19,032,296 |
| | $ 43,239,939 | $ 33,302 | $ (494,824) | $ 42,778,417 |

The carrying value of investment securities pledged to secure public funds, borrowings and for other purposes as required or permitted by law amounts to approximately $14,025,000 and $14,316,000 at December 31, 2007 and 2006, respectively. During 2007 and 2006 the Bank had no proceeds from the sale of available for sale securities. During 2005 the Bank had proceeds from the sale of available for sale securities of $6,016,550, gross gains of $1,298 and gross losses of $7,175.

The amortized cost and estimated fair value of debt securities at December 31, 2007, by contractual maturity, are shown below. Mortgage-backed securities are classified in accordance with their estimated lives. Expected maturities may differ from contractual maturities because borrowers may have the right to prepay obligations.

| | **Amortized** | **Estimated** |
|---|---|---|

| | cost | fair value |
|---|---|---|
| Securities available-for-sale: | | |
| Due in one year or less | $ 12,494,840 | $ 12,538,473 |
| Due after one year through five years | 31,965,384 | 32,203,159 |
| Due after five years through ten years | 8,314,172 | 8,349,895 |
| Due after ten years | 2,998,275 | 3,015,629 |
| | $ 55,772,671 | $ 56,107,156 |

The gross unrealized loss and related estimated fair value of investment securities that have been in a continuous loss position for less than twelve months and over twelve months at December 31, are as follows:

| | Less than Twelve Months | | Over Twelve Months | | Total | |
|---|---|---|---|---|---|---|
| | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value |
| December 31, 2007: | | | | | | |
| U.S. Government & Agency Securities | $ — | $ — | $ — | $ — | $ — | $ — |
| States and Political Subdivisions | (22,168) | 968,403 | (28,165) | 2,224,642 | (50,333) | 3,193,045 |
| Mortgage-Backed Securities | (4,626) | 2,971,470 | (92,424) | 7,118,850 | (97,050) | 10,090,320 |
| | $ (26,794) | $ 3,939,873 | $ (120,589) | $ 9,343,492 | $ (147,383) | $ 13,283,365 |

| | Less than Twelve Months | | Over Twelve Months | | Total | |
|---|---|---|---|---|---|---|
| | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated fair value |
| December 31, 2006: | | | | | | |
| U.S. Government & Agency Securities | $ (2,954) | $ 4,000,971 | $ (73,645) | $ 6,924,317 | $ (76,599) | $ 10,925,288 |
| States and Political Subdivisions | (493) | 352,419 | (88,905) | 3,587,649 | (89,398) | 3,940,068 |
| Mortgage-Backed Securities | — | — | (328,827) | 12,473,837 | (328,827) | 12,473,837 |
| | $ (3,447) | $ 4,353,390 | $ (491,377) | $ 22,985,803 | $ (494,824) | $ 27,339,193 |

As of December 31, 2007, the Company has 21 investment securities where estimated fair market value had decreased 1.13% from amortized cost. Management evaluates investment securities for other-than-temporary impairment taking into consideration the extent and length of time the fair value has been less than cost, the financial condition of the issuer and whether the Bank has the intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. As of December 31, 2007, no declines are deemed to be other than temporary.

**NOTE C – LOANS –** The Bank's loan portfolio consists primarily of loans to borrowers within San Luis Obispo and northern Santa Barbara Counties, California. Although the Bank seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, real estate and real estate associated businesses are among the principal industries in the Bank's market areas. As a result, the Bank's loan and collateral portfolios are, to some degree, concentrated in those industries.

The composition of the loan portfolio at December 31, is as follows:

| | 2007 | 2006 |
|---|---|---|
| Real estate – construction | $ 47,819,615 | $ 55,307,210 |
| Real estate – other | 81,895,109 | 78,757,513 |
| Commercial | 38,016,713 | 36,406,663 |
| Consumer | 1,237,325 | 1,603,836 |
| | 168,968,762 | 172,075,222 |
| Deferred loan fees | (675,858) | (741,054) |
| Allowance for loan losses | (1,673,410) | (1,653,695) |
| | $ 166,619,494 | $ 169,680,473 |

The allowance for loan losses is increased by the provision to income and decreased by net charge-offs. Management's periodic evaluation of the adequacy of the allowance is based on the Company's past loan experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and current economic conditions.

Transactions in the allowance for credit losses are summarized as follows:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Balance at beginning of year | $ 1,653,695 | $ 1,470,261 | $ 1,200,036 |
| Provision charged to expense | — | 240,000 | 300,000 |
| Loans charged off | (60,779) | (84,002) | (46,355) |
| Recoveries on loans previously charged off | 80,494 | 27,436 | 16,580 |
| Balance at end of year | $ 1,673,410 | $ 1,653,695 | $ 1,470,261 |

The following is a summary of the investment in impaired loans, the related allowance for loan losses, income recognized and information pertaining to nonaccrual and past due loans as of December 31:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Recorded investment in impaired loans | $ 2,175,694 | $ — | $ 134,872 |
| Related allowance for loan losses | $ 144,000 | $ — | $ — |
| Average recorded investment in impaired loans | $ 591,000 | $ 250,000 | $ 459,000 |
| Interest income recognized for cash payments | $ — | $ 3,045 | $ 28,581 |
| Total nonaccrual loans | $ 2,175,694 | $ — | $ 134,872 |
| Total loans past-due ninety days or more and still accruing | $ — | $ 550,000 | $ — |

**NOTE D – RELATED PARTY TRANSACTIONS –** In the ordinary course of business, the Bank has granted loans to certain executive officers, directors and the businesses with which they are associated. All such loans and commitments to lend were made under terms which are consistent with the Bank's normal lending policies.

The following is an analysis of the activity of all such loans:

| | 2007 | 2006 |
|---|---|---|
| Beginning balance | $ 3,734,153) | $ 2,976,502) |
| Credits granted, including renewals | 5,515,322) | 2,797,483) |
| Repayments | (4,484,643) | (2,039,832) |
| | $ 4,764,832) | $ 3,734,153) |

Undisbursed loans amount to approximately $894,712 and $2,337,163 at December 31, 2007 and 2006, respectively.

Deposits from related parties held by the Bank at December 31, 2007 and 2006 amounted to $2,367,291 and $3,323,903, respectively.

**NOTE E – PREMISES AND EQUIPMENT –** The composition of premises and equipment at December 31 is as follows:

| | 2007 | 2006 |
|---|---|---|
| Premises | $ 7,497,978 | $ 7,411,967 |
| Furniture, fixtures and equipment | 3,990,273 | 4,149,808 |
| | 11,488,251 | 11,561,775 |
| Less accumulated depreciation | 4,650,509 | 4,334,333 |
| | 6,837,742 | 7,227,442 |
| Land | 2,030,765 | 2,030,765 |
| | $ 8,868,507 | $ 9,258,207 |

**NOTE F – DEPOSITS –** At December 31, 2007, the scheduled maturities of time deposits are as follows:

| | |
|---|---|
| Due in one year | $ 64,801,857 |
| Due in one to three years | 6,188,863 |
| Due after three years | 853,474 |
| | $ 71,844,194 |

**NOTE G – SHORT-TERM BORROWINGS –** The Bank has two borrowing arrangements with the Federal Home Loan Bank of San Francisco. The first allows the Bank to borrow up to approximately $41 million against which the Bank has pledged approximately $100 million of its real estate secured loans. The second arrangement allows the Bank to borrow up to approximately $12 million against which the Bank has pledged approximately $12 million of its investment securities.

As of December 31, 2007 the Bank has borrowed $5,900,000 under these arrangements. This amount is due on January 2, 2008 and includes interest at 3.25%. During 2007 the bank had average borrowings outstanding of $1,100,000 at an effective rate of 4.55%.

The Bank may also borrow up to $5,900,000 overnight on an unsecured basis from two correspondent banks.

**NOTE H – LONG-TERM BORROWINGS –** During the third quarter of 2003, the Bank issued Subordinated Debentures to nineteen investors including executive officers and members of the Bank's Board of Directors, in the total sum of $2,000,000 ("Debentures"). The total amount issued to executive officers and directors was $1,100,000. The Debentures include quarterly payment of interest at prime plus 1.5% and quarterly principal installments of $166,666 commencing on September 30, 2008 until paid in full on June 30, 2011. The Debentures, which are subordinated to the right of payment to depositors and other creditors, partially qualify as Tier 2 Capital.

On April 28, 2006, the Company issued $5,155,000 in junior subordinated debt securities (the "debt securities") to the Santa Lucia Bancorp (CA) Capital Trust, a statutory trust created under the laws of the State of Delaware. These debt securities are subordinated to effectively all borrowings of the Company and are due and payable on July 7, 2036. These debt securities may be redeemed for 105% of the principal balance through July 7, 2011 and then at par thereafter. Interest is payable quarterly beginning July 7, 2006 at 1.48% over the quarterly adjustable 3-month LIBOR.

The Company also purchased a 3% minority interest in Santa Lucia Bancorp (CA) Capital Trust. The balance of the equity of Santa Lucia Bancorp (CA) Capital Trust is comprised of mandatorily redeemable preferred securities.

**NOTE I – INCOME TAXES –** The asset and liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax liabilities and assets as of December 31 are as follows:

| | 2007 | 2006 |
|---|---|---|
| Deferred liabilities: | | |
| Tax over book depreciation | $ 425,000 | $ 493,000 |
| Market value adjustment on investment securities | 138,000 | — |
| Other | 111,000 | 107,000 |
| Total deferred tax liabilities | 674,000 | 600,000 |
| Deferred tax assets: | | |
| Allowance for loan losses | 673,000 | 673,000 |
| Deferred compensation plans | 498,000 | 390,000 |
| Market value adjustment on investment securities | — | 190,000 |
| State taxes | 191,000 | 224,000 |
| Net loss carryforward | 41,000 | 55,000 |
| Other | 85,000 | 9,000 |
| Total deferred tax assets | 1,488,000 | 1,541,000 |
| Net deferred tax assets | $ 814,000 | $ 941,000 |

The provision for income taxes consists of the following:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Currently payable | $ 2,135,000) | $ 2,389,000 | $ 1,784,000 |
| Deferred taxes (benefits) | (201,000) | (147,000) | (25,000) |
| | $ 1,934,000 | $ 2,242,000 | $ 1,759,000 |

The principal sources of deferred income taxes and the tax effect of eachare as follows:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Tax over book depreciation | $ (68,000) | $ 6,000) | $ 173,000 |
| Provision for loan losses | — | (75,000) | (118,000) |
| State taxes | 33,000 | (75,000) | (46,000) |
| Net loss carryforward | 14,000 | 14,000 | 14,000 |
| Deferredcompensationplans | (108,000) | (42,000) | (41,000) |
| Other | (72,000) | (25,000) | (7,000) |
| Net deferred taxes | $ (201,000) | $ (147,000) | $ (25,000) |

As of December 31, 2007, the Bank had federal net operating loss carryforwards available to reduce future taxable income of approximately $163,000. These net operating loss carryforwards expire in 2010. The 1995 merger with Central Coast National Bank resulted in an ownership change as defined in the Internal Revenue Code Section 382. Accordingly, the utilization of the net operating loss will be subject to the limitations prescribed in Section 382.

As a result of the following items, the total tax expense was different from the amount computed by applying the statutory income tax rate to earnings before income taxes:

| | 2007 | | 2006 | | 2005 | |
|---|---|---|---|---|---|---|
| Federal "expected" tax | $1,679,000 | 34.0% | $1,914,000 | 34.0% | $1,532,000 | 34.0% |
| State franchise tax, net | 347,000 | 7.0 | 396,000 | 7.0 | 318,000 | 7.0 |
| Tax exempt income | (122,000) | (2.5) | (80,000) | (1.3) | (82,000) | (1.8) |
| Other | 30,000 | 0.6 | 12,000 | 0.2 | (9,000) | (0.2) |
| Total expense | $1,934,000 | 39.1% | $2,242,000 | 39.9% | $1,759,000 | 39.0% |

The Company is subject to Federal income tax and California franchise tax. Federal income tax returns for the years ended December 31, 2006, 2005 and 2004 are open to audit by the Federal authorities and California returns for the years ended December 31, 2006, 2005, 2004 and 2003 are open to audit by state authorities.

**NOTE J – EMPLOYEE PROFIT SHARING AND DEFERRED COMPENSATION –** The Bank sponsors a 401 (k) plan for the benefit of its employees. In 1994 the Bank also approved the creation of an Employee Stock Ownership Plan for the benefit of its employees. Contributions to these plans are determined by the Board of Directors. For income tax purposes, the annual contribution is limited to 15% of the compensation of eligible employees. The Bank contributed $203,000 in 2007, $210,000 in 2006, and $240,000 in 2005, to the Employee Stock Ownership Plan. The Bank contributed $57,000 to the 401 (k) plan in 2007 and $50,000 in 2006. There were no contributions to the 401 (k) plan in 2005.

The Bank has entered into deferred compensation agreements with key officers and board members. Under these agreements, the Bank is obligated to provide, upon retirement, a lifetime benefit for the officers and directors. The annual benefits ranging from $25,000 to $75,000 for key officers and $4,000 to $6,000 for directors. The estimated present value of future benefits to be paid is being accrued over the period from the effective date of the agreements until the expected retirement dates of the participants. The expense incurred and amount accrued for this plan for the years ended December 31, 2007, 2006, and 2005 totaled $292,385, $131,454, and $120,715, respectively. The Bank is a beneficiary of life insurance policies that have been purchased as a method of financing the benefits under the agreements.

**NOTE K – STOCK OPTIONS –** The Company sponsors one compensatory incentive and non-qualified stock option plan which provides certain key employees and the Board of Directors with the option to purchase shares of common stock, and one Equity Based Compensation Plan which provides certain key employees and the Board of Directors with the award of any Option, Stock Appreciation Right, Restricted Stock Award, Restricted Share Unit, Performance Share Award, Dividend Equivalent, or any combination thereof. In 1999, the Bank adopted a stock option plan (the 2000 plan) under which up to 360,000 shares of the Bank's common stock may be issued to directors, officers, and key employees. In 2006, the Company adopted the 2006 Equity Based Compensation Plan (the Plan), which the maximum number of shares of common stock that may be awarded under this Plan shall not exceed 200,000 shares, including 38,200 shares rolled over from the Company's 2000 Stock Option Plan. Option prices may not be less than 100% of the fair market value of the stock at the date of grant. Options became exercisable at the rate of 20% per year beginning at various dates and expire not more than ten years from the date of grant. The Company recognized stock-based compensation costs of $122,645 and $63,558 and related tax benefits of $18,450 and $7,193 for 2007 and 2006, respectively.

The fair value of each option granted was estimated on the date of grant using the Black-Scholes options pricing model with the following assumptions:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Risk-free rates | 4.65% | 4.77% | 3.75% |
| Expected volatility | 20.00% | 20.00% | 17.00% |
| Expected dividened yield | 1.40% | 1.40% | 2.10% |
| Expected term | 6.0 years | 6.0 years | 6.5 years |
| Weighted-average grant date fair value | $ 6.72 | $ 6.43 | $ 4.47 |

A summary of the status of the Company's fixed stock option plan as of December 31, 2007 and changes during the year then ended is presented below:

| | December 31, 2007 | | | |
|---|---|---|---|---|
| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value |
| Outstanding at the beginning of the year | 243,176 | $ 15.55 | | |
| Granted | 34,000 | 26.15 | | |
| Exercised | (36,916) | 10.23 | | |
| Foreited or expired | (16,500) | 23.04 | | |
| Outstanding at the end of the year | 223,760 | 17.48 | 6.5 years | $ 1,730,000 |
| Options Exercisable | 126,260 | $ 13.04 | 4.9 years | $ 1,518,000 |

The total intrinsic value of options exercised during the years ended December 31, 2007, 2006, and 2005 were approximately $638,000, $539,000, and $760,000 respectively. As of December 31, 2007 there was $503,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted average period of 2.4 years.

**NOTE L – EARNINGS PER SHARE (EPS) –** The following is a reconciliation of net income and shares outstanding to the income and number of shares used to compute EPS:

| | December 31, 2007 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 3,002,819 | |
| Average shares outstanding | | 1,933,231 |
| Used in Basic EPS | 3,002,819 | 1,933,231 |
| Dilutive effect of outstanding stock options | | 59,823 |
| Used in Diluted EPS | $ 3,002,819 | 1,993,054 |

| | December 31, 2006 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 3,388,271 | |
| Average shares outstanding | | 1,916,253 |
| Used in Basic EPS | 3,388,271 | 1,916,253 |
| Dilutive effect of outstanding stock options | | 98,413 |
| Used in Diluted EPS | $ 3,388,271 | 2,014,666 |

| | December 31, 2005 | |
|---|---|---|
| | Income (Numerator) | Shares (Denominator) |
| Net income | $ 2,746,820 | |
| Average shares outstanding | | 1,878,949 |
| Used in Basic EPS | 2,746,820 | 1,878,949 |
| Dilutive effect of outstanding stock options | | 105,289 |
| Used in Diluted EPS | $ 2,746,820 | 1,984,238 |

**NOTE M – COMMITMENTS AND CONTINGENCIES –** The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those commitments. Commitments to extend credit (such as the unfunded portion on lines of credit and commitments to fund new loans) as of December 31, 2007 and 2006 amounts to approximately $57,326,000 and $56,557,000, respectively, of which approximately $4,286,000 and

$2,603,000 are related standby letters of credit, respectively. The Company uses the same credit policies in these commitments as is done for all of its lending activities. As such, the credit risk involved in these transactions is essentially the same as that involved in extending loan facilities to customers.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Company evaluates each client's credit worthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Company is based on management's credit evaluation of the customer. The majority of the Company's commitments to extend credit and standby letters of credit are secured by real estate.

In the normal course of business, the Company is involved in various litigation. In the opinion of management, and based on the advise of the Company's legal counsel, the disposition of all pending litigation will not have a material effect on the Company's financial position.

**NOTE N – FAIR VALUES OF FINANCIAL INSTRUMENTS –** The fair value of a financial instrument is the amount at which the asset or obligation could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire holdings of a particular financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The following methods and assumptions were used to estimate the fair value of significant financial instruments:

**Financial Assets –** The carrying amounts of cash, short term investments, due from customers on acceptances, and bank acceptances outstanding are considered to approximate fair value. Short term investments include federal funds sold, securities purchased under agreements to resell, and interest bearing deposits with banks. The fair values of investment securities, including available for sale, are generally based on quoted market prices. The fair value of loans are estimated using a combination of techniques, including discounting estimated future cash flows and quoted market prices of similar instruments where available.

**Financial Liabilities –** The carrying amounts of deposit liabilities payable on demand, commercial paper, and other borrowed funds are considered to approximate fair value. For fixed maturity deposits, fair value is estimated by discounting estimated future cash flows using currently offered rates for deposits of similar remaining maturities. The fair value of long term debt is based on rates currently available for debt with similar terms and remaining maturities.

**Off-Balance Sheet Financial Instruments –** The fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements. The fair values of these financial instruments are not deemed to be material.

The estimated fair value of financial instruments at December 31, 2007 and 2006 are summarized as follows:

| | December 31, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| | Carrying Value | Market Value | Carrying Value | Market Value |
| Financial Assets: | | | | |
| Cash and cash equivalents | $ 7,399,412 | $ 7,399,412 | $10,139,526 | $10,139,526 |
| Investment securities | 56,107,156 | 56,107,156 | 42,778,417 | 42,778,417 |
| Loans receivable, net | 166,619,494 | 167,422,617 | 169,680,473 | 170,091,100 |
| Cash surrender value of life insurance | 5,005,376 | 5,005,376 | 3,336,076 | 3,336,076 |
| Federal Reserve Bank FHLB Stock | 1,453,850 | 1,453,850 | 1,397,700 | 1,397,700 |
| Accrued interest receivable | 1,465,402 | 1,465,402 | 1,559,551 | 1,559,551 |
| Financial Liabilities: | | | | |
| Time deposits | $71,844,194 | $72,612,333 | $65,917,714 | $65,838,613 |
| Other deposits | 140,874,184 | 141,374,184 | 147,070,738 | 147,070,738 |
| Other borrowings | 5,900,000 | 5,900,000 | — | — |
| Long-term debt | 7,155,000 | 7,155,000 | 7,155,000 | 7,155,000 |
| Accrued interest and other liabilities | 1,677,551 | 1,677,551 | 1,457,716 | 1,457,716 |

**NOTE O – REGULATORY MATTERS –** The Company and the Bank are 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 material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain offbalance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2007, the most recent notification from the Federal Reserve Bank (FRB) 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 have changed the Bank's category). To be categorized as well capitalized, the Bank must maintain minimum ratios as set forth in the table below. The following table also sets forth the Company's and Bank's actual capital amounts and ratios (dollar amounts in thousands):

| | Actual | | For capital adequacy purposes | | To be well capitalized under prompt corrective action provisions | |
|---|---|---|---|---|---|---|
| | Amount (thousands) | Ratio | Amount (thousands) | Ratio | Amount (thousands) | Ratio |
| **As of December 31, 2007:** | | | | | | |
| **Company** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 29,075 | 14.6% | $ 15,912 | 8.0% | $ 19,890 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 26,147 | 13.2% | $ 7,956 | 4.0% | $ 11,934 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 26,147 | 10.5% | $ 9,794 | 4.0% | $ 12,243 | 5.0% |

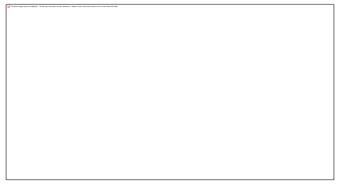
| | | | | | | |
|---|---|---|---|---|---|---|
| **Bank** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 27,410 | 13.8% | $ 15,888 | 8.0% | $ 19,860 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 24,482 | 12.3% | $ 7,944 | 4.0% | $ 11,916 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 24,482 | 9.9% | $ 9,941 | 4.0% | $ 12,427 | 5.0% |
| **As of December 31, 2006:** | | | | | | |
| **Company** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 27,872 | 14.4% | $ 14,026 | 8.0% | $ 17,533 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 24,563 | 12.7% | $ 7,013 | 4.0% | $ 10,520 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 24,563 | 10.0% | $ 9,794 | 4.0% | $ 12,243 | 5.0% |
| **Bank** | | | | | | |
| Total Capital (to Risk-Weighted Assets) | $ 25,575 | 13.1% | $ 15,588 | 8.0% | $ 19,485 | 10.0% |
| Tier 1 Capital (to Risk-Weighted Assets) | $ 22,266 | 11.4% | $ 7,794 | 4.0% | $ 11,691 | 6.0% |
| Tier 1 Capital (to Average Assets) | $ 22,266 | 9.1% | $ 9,777 | 4.0% | $ 12,221 | 5.0% |

The California Financial Code provides that a bank may not make a cash distribution to its shareholders in excess of the lesser of the Bank's undivided profits or the Bank's net income for its last three fiscal years less the amount of any distribution made by the Bank to shareholders during the same period.

With certain exceptions the Company may not pay a dividend to its shareholders unless its retained earnings equal at least the amount of the proposed dividend.

**NOTE P – HOLDING COMPANY –** On April 3, 2006 Santa Lucia Bancorp acquired all the outstanding shares of Santa Lucia Bank by issuing 1,909,837 shares of common stock in exchange for the surrender of all outstanding shares of the Bank's common stock. There was no cash involved in this transaction. The acquisition was accounted for like a pooling of interest and the consolidated financial statements contained herein have been restated to give full effect to this transaction.

Santa Lucia Bancorp has no significant business activities other than its investment in Santa Lucia Bank and its investment and related borrowings from Santa Lucia (CA) Capital Trust as discussed in Note H. Accordingly, no separate financial information on the Company is provided.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## SANTA LUCIA BANCORP

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| **SANTA LUCIA BANCORP BOARD OF DIRECTORS** | |
| **JERRY W. DECOU III** | CHAIRMAN |
| **DOUGLAS C. FILIPPONI** | VICE CHAIRMAN |
| **KHATCHIK H. ACHADJIAN** | |
| **STANLEY R. CHERRY** | |
| **JOHN C. HANSEN** | |
| **JEAN HAWKINS** | |
| **PAUL G. MOERMAN** | |
| **LARRY H. PUTNAM** | |
| **D. JACK STINCHFIELD** | |

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|---|---|
| **SANTA LUCIA BANCORP EXECUTIVE OFFICERS** | |
| **LARRY H. PUTNAM** | PRESIDENT AND CHIEF EXECUTIVE OFFICER |
| **JOHN C. HANSEN** | EXECUTIVE VICE PRESIDENT, CHIEF FINANCIAL OFFICER |

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|---|---|
| **SANTA LUCIA BANK BOARD OF DIRECTORS** | |
| **JERRY W. DECOU III** | CHAIRMAN |
| **DOUGLAS C. FILIPPONI** | VICE CHAIRMAN |
| **KHATCHIK H. ACHADJIAN** | |
| **STANLEY R. CHERRY** | |
| **JOHN C. HANSEN** | |
| **JEAN HAWKINS** | |
| **PAUL G. MOERMAN** | |
| **LARRY H. PUTNAM** | |
| **D. JACK STINCHFIELD** | |

## SANTA LUCIA BANK

| | |
|---|---|
| **EXECUTIVE OFFICERS** | |
| **LARRY H. PUTNAM** | Chief Executive Officer |
| **JOHN C. HANSEN** | President and Chief Operating Officer |
| **JAMES M. COWAN** | Executive Vice President, Chief Credit Officer |

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|---|---|
| **SENIOR VICE PRESIDENTS** | |
| **MELODEE FONTANA** | Senior Vice President, Operations Administrator |
| **ROBERT COVARRUBIAS** | Senior Vice President, Manager |

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|---|---|
| **VICE PRESIDENTS** | |
| **TERI DAVIS** | Vice President, Loan Officer |
| **SHARON SATTERTHWAITE** | Vice President, Controller |
| **LEAH T. WEST** | Vice President, Manager |
| **JIM KELLEY** | Vice President, Loan Officer |
| **MICHAEL W. McKENZIE** | Vice President, Manager |
| **LARRY WOMACK** | Vice President, Loan Officer |
| **JAMES P. BURUBELTZ** | Vice President, Loan Officer |
| **RICHARD ALLEN** | Vice President, Loan Officer |
| **JULIE A. JOSLIN** | Vice President, Cashier |

| | |
|---|---|
| **ASSISTANT VICE PRESIDENTS** | |
| **JENNIFER BASSI GINDER** | Assistant Vice President, Operations Officer |
| **KRISTIE KELLER** | Assistant Vice President, Central Operations |

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|---|---|
| **KIM DONALDSON** | Assistant Vice President, Operations Officer |
| **CHERYL MUMFORD** | Assistant Vice President, Operations Officer |
| **RYUN McCRORY** | Assistant Vice President, Loan Officer |
| **J. DARREN BARNES** | Assistant Vice President, Loan Officer |
| **REGINA M. SHELDON** | Assistant Vice President, Loan Officer |

**OFFICERS**

| | |
|---|---|
| **KAREN SAMPSON** | Assistant Operations Officer |
| **STELLA MARTINEZ** | Operations Officer |
| **ROBERT McCONAGHY** | Loan Officer |

| **ATASCADERO** | **PASO ROBLES** | **ARROYO GRANDE** | **SANTA MARIA** |
|---|---|---|---|
| 7480 EL CAMINO REAL | 1240 SPRING STREET | 1530 E. GRAND AVENUE | 1825 S. BROADWAY |
| ATASCADERO, CA 93422 | PASO ROBLES, CA 93446 | ARROYO GRANDE, CA 93420 | SANTA MARIA, CA 93454 |
| 805-466-7087 | 805-239-1140 | 805-473-1988 | 805-614-9100 |

**MARKET MAKERS**

| | |
|---|---|
| **GEORGE CROSBY, MAGUIRE INVESTMENTS – SANTA MARIA, CA** | 805/922-6901 or 800/244-4183 |
| **LISA GALLO, WEDBUSH MORGAN SECURITIES – LAKE OSWEGO, OR** | 503/675-3100 or 866/491-7828 |
| **MICHAEL S. HEDREI, HOWE BARNES HOEFER & ARNETT, INC. – SAN FRANCISCO, CA** | 415/538-5749 or 800/774-8723 |
| **RANDY KRUMLAND, EDWARD JONES – ATASCADERO, CA** | 805/466-0244 or 800/467-0244 |
| **JIM MOFFATT, MORGAN STANLEY – PASO ROBLES, CA** | 805/239-0920 or 800/733-0920 |
| **TREVOR MORRIS, UBS FINANCIAL SERVICES, INC. – LOS ANGELES, CA** | 213/972-1511 or 800/443-5203 |
| **JOEY J. WARMENHOVEN, McADAMS WRIGHT RAGEN – PORTLAND, OR** | 503/922-4888 or 866/662-0351 |

**Exhibit 31.1**

**CERTIFICATION**

I, Larry H. Putnam, President and Chief Executive Officer of Santa Lucia Bancorp, certify that:

1. I have reviewed this annual report on Form 10-KSB/A of Santa Lucia Bancorp;

2. Based on my knowledge, this annual 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 annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;

4. The registrant's other certifying officers 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 we 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 annual 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 officers 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 function):

   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: July 22, 2008

/s/ Larry H. Putnam
Larry H. Putnam
President and Chief Executive Officer

**Exhibit 31.2**

**CERTIFICATION**

I, John C. Hansen, Executive Vice President and Chief Financial Officer of Santa Lucia Bancorp, certify that:

1. I have reviewed this annual report on Form 10-KSB/A of Santa Lucia Bancorp;

2. Based on my knowledge, this annual 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 annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;

4. The registrant's other certifying officers 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 we 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 annual 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 officers 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 function):

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: July 22, 2008

/s/ John C. Hansen
John C. Hansen
Executive 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

Each of the undersigned hereby certifies in his capacity as an officer of Santa Lucia Bancorp (the “Company”) that the Annual Report of the Company on Form 10-KSB/A for the period ended December 31, 2007 fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition of the Company at the end of such period and the results of operations of the Company for such period.

Date: July 22, 2008

/s/ Larry H. Putnam
Larry H. Putnam
President and Chief Executive Officer

Date: July 22, 2008

/s/ John C. Hansen
John C. Hansen
Executive Vice President and Chief Financial Officer