

BAKER BOYER BANCORP

THIRD QUARTER

REPORT

2005



Baker Boyer Bancorp

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Letter To Our Shareholders

October 28, 2005

Dear Baker Boyer Shareholders:

I am pleased to bring you more good financial news, along with a look back at just some of the successes we achieved during our 135th year. Net Income for the first three quarters of 2005 grew to \$3.16 million, or \$2.44 per share, compared to \$2.89 million, or \$2.23 per share in 2004. Earnings per share grew 9.4% despite the sale of our Connell branch last November.

Healthy growth in non-interest income, primarily in investment services, as well as continued cost control accounted for the increase. Non-interest income was up 7% and non-interest expenses were down 4%. The bottom line is we are producing more net income from every dollar of assets in our banking and investment management businesses. That's an important demonstration of increased efficiency.

Last fall the entire bank was involved in planning and launching our 135th year anniversary event, "Celebrating Baker Boyer." The program included a major bank-wide business development and client retention effort. Measurable results included a forty percent increase in client referrals and significant new business throughout the celebration. The momentum continues today.

We had even more reason to celebrate when we received three prestigious awards during the anniversary celebration quarter. First, we were voted **Best Bank** in Walla Walla Valley in the *Union-Bulletin* Reader Poll. With the number of competitors out there, we are very proud of that. In addition, *Washington CEO Magazine* voted us one of the **Best Companies to Work For** in the state. We particularly enjoyed being the only Eastern Washington company on the list. Finally, *Independent Banker Magazine* named us **Most Community Reflective in Architectural Excellence**. These honors confirmed that our clients have a high level of confidence in the oldest independent bank in the region. They also speak to the strong satisfaction our employees feel in working for their company and our innovative capability in an ever-changing, increasingly competitive business environment.

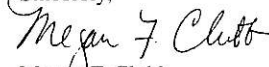
Like all banks, we continue to be challenged in growing our net interest income. The Federal Reserve has increased short-term rates by 275 basis points since June 2004. Despite this, most banks are struggling to grow assets in a competitive market while increasing net interest margin.

We continually make strategic choices in pricing loan and deposit services to increase net interest income, even though it causes us to lose deals in some cases. We are carefully managing interest expense and have allowed our highest interest cost deposits to run off. The good news is many of these deposits have been moved to our Investor Services broker dealer business, thereby retaining the full client relationship at Baker Boyer.

The amount and percentage of non-interest bearing accounts continued to rise, which favorably impacts net interest margin. Overall non-interest bearing deposits grew from \$66 million a year ago to \$71 million—an 8% annual rate of growth.

It is a real privilege to serve as your President and CEO. As always, I welcome your questions, comments, and ideas. My team of hard-working, talented and loyal employees is actively partnering with your Board of Directors to continuously make improvements that position us for a very successful future.

Sincerely,


Megan F. Clubb
Chair, President and CEO

Board of Directors

Megan F. Clubb, Chair	Stephen G. Kimball
D.F. Baker	Edward N. Lange
Jon S. Bren	Susan C. Pratt
David B. Campbell	Robert R. Richards
Thomas W. Campbell	

Consolidated Balance Sheets

(Unaudited)

	September 30,		% Chg.
	2005	2004	
(Dollars in Thousands)			
ASSETS			
Cash and due from banks	\$ 10,274	\$ 16,385	(37.30)
Federal funds sold and security resell agreements	—	13,765	—
Investment securities			
Held-to-maturity	32,048	33,307	(3.78)
Available-for-sale	66,341	62,296	6.49
	<u>98,389</u>	<u>95,603</u>	2.91
Other securities	1,690	1,733	(2.48)
Loans	257,405	253,522	1.53
Less: Allowance for loan losses	(3,088)	(3,958)	(21.98)
	<u>254,317</u>	<u>249,564</u>	1.90
NET LOANS			
Bank premises and equipment, net of accumulated depreciation	8,548	8,023	6.54
Accrued interest receivable	3,667	3,435	6.75
Other assets	925	997	(7.22)
	<u>\$377,810</u>	<u>\$389,505</u>	(3.00)
TOTAL ASSETS			
LIABILITIES AND SHAREHOLDERS' EQUITY			
Deposits			
Noninterest bearing	\$ 71,575	\$ 66,177	8.16
Interest bearing	258,827	283,349	(8.65)
	<u>330,402</u>	<u>349,526</u>	(5.47)
TOTAL DEPOSITS			
Federal funds purchased and security repurchase agreements	8,170	6,044	35.18
Other borrowed funds	5,000	—	—
Accrued interest payable	379	343	10.50
Other liabilities	1,247	1,597	(21.92)
	<u>345,198</u>	<u>357,510</u>	(3.44)
TOTAL LIABILITIES			
SHAREHOLDERS' EQUITY			
Common stock (no par value, \$3.125 stated value)			
	9/30/05	9/30/04	
Shares authorized	4,000,000	4,000,000	
Shares issued and outstanding	1,299,809	1,300,130	
	4,062	4,063	(0.02)
Capital surplus	1,112	1,129	(1.51)
Retained earnings	27,753	26,437	4.98
Unearned shares - Long-Term Performance & Retention Plan	(245)	—	—
Accumulated other comprehensive income (loss)	(70)	366	(119.13)
	<u>32,612</u>	<u>31,995</u>	1.93
TOTAL SHAREHOLDERS' EQUITY			
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY			
	<u>\$377,810</u>	<u>\$389,505</u>	(3.00)

Consolidated Statements of Income

(Unaudited)

	Nine Months Ending September 30,		
	2005	2004	% Chg.
(Dollars in Thousands)			
Interest Income:			
Loans, including fees	\$ 12,670	\$12,381	2.33
Investment securities			
Taxable	1,390	1,084	28.23
Tax-exempt	1,141	1,294	(11.82)
	<u>2,531</u>	<u>2,378</u>	6.43
Other securities	23	59	(61.02)
Federal funds sold	25	107	(76.64)
	<u>15,249</u>	<u>14,925</u>	2.17
TOTAL INTEREST INCOME			
Interest Expense:			
Interest bearing deposits	3,272	3,154	3.74
Federal funds purchased and security repurchase agreements	154	68	126.47
Other borrowed funds	68	—	—
	<u>3,494</u>	<u>3,222</u>	8.44
TOTAL INTEREST EXPENSE			
NET INTEREST INCOME			
	<u>11,755</u>	<u>11,703</u>	0.44
Provision for Loan Losses	1,080	632	70.89
	<u>10,675</u>	<u>11,071</u>	(3.58)
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES			
Other Income:			
Investment Management and Trust fees	3,004	2,827	6.26
Service charges on deposits	857	917	(6.54)
Other service charges and fees	781	675	15.70
Investment securities losses	(16)	(38)	(57.89)
Other operating income	210	139	51.08
	<u>4,836</u>	<u>4,520</u>	6.99
Other Expense:			
Salaries and wages	5,597	5,708	(1.94)
Retirement and employee benefits	1,829	1,840	(0.60)
Net occupancy expense	585	604	(3.15)
Furniture and equipment expense	527	503	4.77
Other operating expense	2,815	3,208	(12.25)
	<u>11,353</u>	<u>11,863</u>	(4.30)
INCOME BEFORE INCOME TAXES			
	<u>4,158</u>	<u>3,728</u>	11.53
Provision For Income Taxes	999	836	19.50
	<u>\$ 3,159</u>	<u>\$ 2,892</u>	9.23
NET INCOME			
Basic Earnings Per Common Share	<u>\$ 2.44</u>	<u>\$ 2.23</u>	9.42
Average number of shares outstanding	<u>1,294,087</u>	<u>1,299,663</u>	