

MID-STATE BANCSHARES
Form 10-Q
November 09, 2004

United States
Securities and Exchange Commission

Washington, D.C. 20429

FORM 10-Q

- Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934.**
For the quarterly period ended September 30, 2004
- Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to .**

Commission File Number 000-23925

MID-STATE BANCSHARES

(Exact name of registrant as specified in its charter)

California
(State or Other Jurisdiction of
Incorporation or Organization)

77-0442667
(I.R.S. Employer Identification No.)

1026 Grand Ave. Arroyo Grande, CA
(Address of Principal Executive Offices)

93420-0580
(Zip Code)

Issuer's Telephone Number: **(805) 473-7700**

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

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

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Number of shares of common stock of the Company outstanding as of October 29, 2004: 23,247,339 shares.

Mid-State Bancshares

September 30, 2004

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PART I - FINANCIAL INFORMATION

Item 1 - Financial Statements

Mid-State Bancshares

Consolidated Statements of Financial Position

(Unaudited - figures in 000 s)

| ASSETS | Sept. 30, 2004 | Dec. 31, 2003 | Sept. 30, 2003 |
|--|---------------------|---------------------|---------------------|
| Cash and Due From Banks | \$ 119,104 | \$ 123,763 | \$ 109,469 |
| Fed Funds Sold | | 47,500 | 85,300 |
| Securities Available For Sale | 688,923 | 774,679 | 682,441 |
| Loans Held for Sale | 10,001 | 13,410 | 42,075 |
| Loans, Net of Unearned Income | 1,394,478 | 1,154,932 | 1,091,113 |
| Allowance for Loan Losses | (13,912) | (16,063) | (16,871) |
| Net Loans | 1,380,566 | 1,138,869 | 1,074,242 |
| Premises and Equipment, Net | 25,213 | 26,325 | 25,709 |
| Accrued Interest Receivable | 13,099 | 12,174 | 12,254 |
| Other Real Estate Owned | | 3,428 | 3,279 |
| Goodwill | 47,840 | 47,840 | 33,448 |
| Core Deposit Intangibles, net | 8,076 | 9,107 | 6,698 |
| Other Assets | 16,721 | 11,737 | 11,234 |
| Total Assets | \$ 2,309,543 | \$ 2,208,832 | \$ 2,086,149 |
| LIABILITIES AND EQUITY | | | |
| Non Interest Bearing Demand | \$ 524,785 | \$ 487,624 | \$ 436,565 |
| NOW Accounts, Money Market and Savings Deposits | 1,075,583 | 1,024,207 | 965,821 |
| Time Deposits Under \$100 | 231,147 | 245,052 | 236,275 |
| Time Deposits \$100 or more | 168,052 | 155,548 | 156,131 |
| Total Deposits | 1,999,567 | 1,912,431 | 1,794,792 |
| Other Borrowings | 5,843 | 7,627 | 7,907 |
| Allowance for Losses - Unfunded Commitments | 1,682 | 1,941 | 1,862 |
| Accrued Interest Payable and Other Liabilities | 23,989 | 14,279 | 20,767 |
| Total Liabilities | 2,031,081 | 1,936,278 | 1,825,328 |
| Commitments and Contingencies | | | |
| Shareholders' Equity: Common Stock and Surplus (Shares Outstanding of 23,323, 23,567 and 23,191, respectively) | 68,348 | 75,506 | 67,424 |
| Retained Earnings | 200,626 | 184,771 | 179,448 |
| Accumulated Other Comprehensive Income net of taxes of \$6,326, \$8,200 and \$9,299 | 9,488 | 12,277 | 13,949 |
| Total Equity | 278,462 | 272,554 | 260,821 |
| Total Liabilities and Equity | \$ 2,309,543 | \$ 2,208,832 | \$ 2,086,149 |

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

Mid-State Bancshares

Consolidated Statements of Income

(Unaudited - figures in 000 \$ except earnings per share data)

| | Three Month Period Ended Sept. 30, | | Nine Month Period Ended Sept. 30, | |
|--|---------------------------------------|-----------------|--------------------------------------|------------------|
| | 2004 | 2003 | 2004 | 2003 |
| Interest Income: | | | | |
| Interest and fees on loans | \$ 22,106 | \$ 20,574 | \$ 62,343 | \$ 60,461 |
| Interest on investment securities - | | | | |
| U.S. Treasury securities | 178 | 253 | 820 | 612 |
| U.S. Government agencies and corporations | 2,095 | 2,062 | 6,595 | 6,453 |
| Obligations of states and political sub-divisions and other securities | 3,708 | 3,491 | 11,029 | 10,585 |
| Interest on fed funds sold and other | 149 | 263 | 306 | 604 |
| Total Interest Income | 28,236 | 26,643 | 81,093 | 78,715 |
| Interest Expense: | | | | |
| Interest on NOW, money market and savings | 654 | 497 | 1,855 | 1,997 |
| Interest on time deposits less than \$100 | 849 | 1,034 | 2,595 | 3,540 |
| Interest on time deposits of \$100 or more | 546 | 585 | 1,548 | 1,908 |
| Interest other | 34 | 41 | 151 | 114 |
| Total Interest Expense | 2,083 | 2,157 | 6,149 | 7,559 |
| Net Interest Income before provision | 26,153 | 24,486 | 74,944 | 71,156 |
| (Benefit) Provision for loan losses | | | (2,700) | 260 |
| Net Interest Income after provision | 26,153 | 24,486 | 77,644 | 70,896 |
| Other Operating Income: | | | | |
| Service charges and fees | 2,574 | 2,271 | 7,646 | 6,835 |
| Commissions, fees and other service charges | 3,545 | 3,511 | 10,146 | 9,996 |
| Gains on sale of securities | 93 | 14 | 475 | 43 |
| Gain on sale of loans held for sale | 40 | 1,032 | 414 | 2,992 |
| Other non-interest income | 998 | 1,010 | 3,479 | 2,370 |
| Total Other Operating Income | 7,250 | 7,838 | 22,160 | 22,236 |
| Other Operating Expense: | | | | |
| Salaries and employee benefits | 10,579 | 9,606 | 32,478 | 28,465 |
| Occupancy and furniture | 3,153 | 3,017 | 9,361 | 8,649 |
| Other operating expenses | 6,533 | 5,966 | 18,997 | 17,876 |
| Total Other Operating Expense | 20,265 | 18,589 | 60,836 | 54,990 |
| Income Before Taxes | 13,138 | 13,735 | 38,968 | 38,142 |
| Provision for income taxes | 4,465 | 4,760 | 13,257 | 13,364 |
| Net Income | \$ 8,673 | \$ 8,975 | \$ 25,711 | \$ 24,778 |
| Earnings per share: | | | | |
| basic | \$ 0.37 | \$ 0.39 | \$ 1.09 | \$ 1.06 |
| diluted | \$ 0.36 | \$ 0.37 | \$ 1.07 | \$ 1.01 |
| Dividends per share | \$ 0.14 | \$ 0.13 | \$ 0.42 | \$ 0.37 |
| Average shares used in earnings per share calculations: | | | | |
| basic | 23,369 | 23,287 | 23,496 | 23,411 |
| diluted | 23,842 | 24,350 | 23,949 | 24,487 |

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

Mid-State Bancshares

Consolidated Statements of Comprehensive Income

(Unaudited - figures in 000 s)

| | Three Month Period Ended Sept. 30, | | Nine Month Period Ended Sept. 30, | |
|--|---------------------------------------|----------|--------------------------------------|-----------|
| | 2004 | 2003 | 2004 | 2003 |
| Net Income | \$ 8,673 | \$ 8,975 | \$ 25,711 | \$ 24,778 |
| Other Comprehensive Income Before Taxes: | | | | |
| Unrealized gains (losses) on securities available for sale: | | | | |
| Unrealized holding gains (losses) arising during period | 8,788 | (5,579) | (4,188) | 1,228 |
| Reclassification adjustment for (gains) included in net income | (93) | (14) | (475) | (43) |
| Other comprehensive income (loss), before taxes | 8,695 | (5,593) | (4,663) | 1,185 |
| Income tax expense (credit) related to items in comprehensive income | 3,478 | (2,237) | (1,874) | 474 |
| Other Comprehensive Income (Loss), Net of Taxes | 5,217 | (3,356) | (2,789) | 711 |
| Comprehensive Income | \$ 13,890 | \$ 5,619 | \$ 22,922 | \$ 25,489 |

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

Mid-State Bancshares

Consolidated Statements of Cash Flows

(Unaudited - figures in 000 s)

| | Nine Month Period Ended Sept. 30, | |
|--|--------------------------------------|------------|
| | 2004 | 2003 |
| OPERATING ACTIVITIES | | |
| Net Income | \$ 25,711 | \$ 24,778 |
| Adjustments to reconcile net income to net cash(used in) provided by operating activities: | | |
| (Benefit) provision for credit losses | (2,700) | 260 |
| Depreciation and amortization | 4,669 | 3,376 |
| Net amortization of prem./discounts-investments | 3,987 | 2,934 |
| Impairment of Investment in real estate | | 91 |
| Gain on sale of loans held for sale | (447) | (2,992) |
| Gain on sale of other real estate owned | (1,084) | |
| Gain on sale of securities, net | (470) | (43) |
| Net decrease (increase) in loans held for sale | 3,856 | (16,523) |
| Change in deferred loan fees | (146) | 197 |
| Changes in assets and liabilities: | | |
| Accrued interest receivable | (925) | (565) |
| Other assets, net | (3,110) | (644) |
| Other liabilities | 9,451 | 5,944 |
| Net cash provided by operating activities | 38,792 | 16,813 |
| INVESTING ACTIVITIES | | |
| Proceeds from sales and maturities of investments | 117,536 | 128,074 |
| Purchases of investments | (39,960) | (203,238) |
| Increase in loans, net | (238,851) | (7,797) |
| Proceeds from investments in real estate | | 148 |
| Proceeds from sale of other real estate owned | 4,512 | |
| Purchases of premises and equipment, net | (2,526) | (3,743) |
| Net cash used in investing activities | (159,289) | (86,556) |
| FINANCING ACTIVITIES | | |
| Increase in deposits | 87,136 | 141,845 |
| Decrease in short-term borrowings | (1,784) | (3,066) |
| Exercise of stock options | 1,659 | 1,686 |
| Cash dividends paid | (9,856) | (8,639) |
| Repurchase of company stock | (8,817) | (11,850) |
| Net cash provided by financing activities | 68,338 | 119,976 |
| (Decrease) increase in cash and cash equivalents | (52,159) | 50,233 |
| Cash and cash equivalents, beginning of period | 171,263 | 144,536 |
| Cash and cash equivalents, end of period | \$ 119,104 | \$ 194,769 |
| The accompanying notes are an integral part of these consolidated statements. | | |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the period for interest | \$ 6,138 | \$ 7,671 |
| Cash paid during the period for taxes | 9,306 | 13,636 |
| Transfer of Loans to Other Real Estate Owned | | 3,279 |

Mid-State Bancshares

Notes to Consolidated Financial Statements

(Information with respect to interim periods is unaudited)

NOTE A - BASIS OF PRESENTATION AND MANAGEMENT REPRESENTATION

The accompanying consolidated financial statements include the accounts of Mid-State Bancshares and its wholly owned subsidiary Mid-State Bank & Trust and the Bank's subsidiaries, MSB Properties and Mid-Coast Land Company (collectively the Company, Bank or Mid-State). All significant inter-company transactions have been eliminated in consolidation. These consolidated financial statements should be read in conjunction with the Form 10-K Annual Report for the year ended December 31, 2003 of Mid-State Bancshares. A summary of the Company's significant accounting policies is set forth in the Notes to Consolidated Financial Statements contained therein.

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States on a basis consistent with the accounting policies reflected in the audited consolidated financial statements included in the Annual Report on Form 10-K for the year ended December 31, 2003. They do not, however, include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments including normal recurring accruals considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for any other interim period or for the year as a whole.

NOTE B - EARNINGS PER SHARE

The following is a reconciliation of net income and shares outstanding to the income and number of shares used to compute Earnings Per Share (EPS). Figures are in thousands, except earnings per share data.

| | Three Month Period Ended Sept. 30, 2004 | | | Three Month Period Ended Sept. 30, 2003 | | |
|---|--|--------|---------|--|--------|---------|
| | Net Income | Shares | EPS | Net Income | Shares | EPS |
| Net Income as reported | \$ 8,673 | | | \$ 8,975 | | |
| Basic Earnings Per Share: | | | | | | |
| Income available to Common Shareholders | \$ 8,673 | 23,369 | \$ 0.37 | \$ 8,975 | 23,287 | \$ 0.39 |
| Effect of dilutive securities: | | | | | | |
| Stock Options | | 473 | | | 1,063 | |
| Diluted Earnings Per Share: | | | | | | |
| Income available to Common Shareholders | \$ 8,673 | 23,842 | \$ 0.36 | \$ 8,975 | 24,350 | \$ 0.37 |

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| | Nine Month Period Ended Sept. 30, 2004 | | | Nine Month Period Ended Sept. 30, 2003 | | |
|---|---|--------|---------|---|--------|---------|
| | Net Income | Shares | EPS | Net Income | Shares | EPS |
| Net Income as reported | \$ 25,711 | | | \$24,778 | | |
| Basic Earnings Per Share: | | | | | | |
| Income available to Common Shareholders | \$ 25,711 | 23,496 | \$ 1.09 | \$ 24,778 | 23,441 | \$ 1.06 |
| Effect of dilutive securities: | | | | | | |
| Stock Options | | 453 | | | 1,046 | |
| Diluted Earnings Per Share: | | | | | | |
| Income available to Common Shareholders | \$ 25,711 | 23,949 | \$ 1.07 | \$ 24,778 | 24,487 | \$ 1.01 |

NOTE C RECENT ACCOUNTING PRONOUNCEMENTS

In January of 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 46, Consolidation of Variable Interest Entities. FIN No. 46 addresses consolidation by business enterprises of variable interest entities, which have one or both of the following characteristics: i) the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties, which is provided through other interests that will absorb some or all of the expected losses of the entity; and ii) the equity investors lack an essential characteristic of a controlling financial interest. FIN No. 46 was initially effective for all financial statements issued on or after February 1, 2003, but subsequently the adoption date was deferred to January 1, 2004. The adoption of FIN No. 46 did not have a material impact on the Company's results of operations and financial position.

The FASB issued Statement of Financial Accounting Standards (SFAS) No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity in May of 2003. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. SFAS No. 150 was effective for financial instruments entered into or modified after May 31, 2003, and otherwise was effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's results of operations and financial position.

The FASB issued SFAS No. 132 (revised 2003), Employers' Disclosures about Pensions and Postretirement Benefits in December of 2003. SFAS No. 132 requires additional disclosures about the assets, obligations and cash flows of defined benefit pension and postretirement plans, as well as the expense recorded for such plans. As of December 31, 2003, the Company has disclosed the required elements related to its defined benefit pension plan in Note 16 to those consolidated financial statements.

In December 2003, the Accounting Standards Executive Committee (AcSEC) of the American Institute of Certified Public Accountants (AICPA) issued Statement of Position (SOP) 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer. The SOP is effective for loans acquired in fiscal years beginning after December 15, 2004, with early adoption encouraged. The SOP addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an Investor's initial investment in loans or

debt securities acquired in a transfer if those differences are attributable, at least in part, to credit quality. The adoption of SOP 03-3 is not expected to have a material impact on the Company's results of operations and financial position.

On March 31, 2004, the FASB issued an Exposure Draft, *Share-Based Payment* (an amendment of SFAS No. 123 and 95) that addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise or (b) liabilities that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. The proposed Statement would eliminate the ability to account for share-based compensation transactions using APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and generally would require instead that such transactions be accounted for using a fair-value-based method. The proposed Statement would be applied to public entities prospectively for fiscal years beginning after December 15, 2004, as if all share-based compensation awards granted, modified, or settled after December 15, 1994, had been accounted for using the fair-value-based method of accounting. A final Statement is expected to be issued in the fourth quarter of 2004. The adoption of the new accounting for share-based payment transactions is not expected to have a material impact on the Company's results of operations and financial position.

In June 2004, the Emerging Issues Task Force of the FASB issued guidance on its Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. The guidance made recommendations regarding disclosures about unrealized losses on available-for-sale debt and equity securities accounted for under FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. The guidance for evaluating whether an investment is other-than-temporarily impaired was to be applied in other-than-temporary impairment evaluations made in reporting periods beginning after June 15, 2004. The disclosures were effective in annual financial statements for fiscal years ending after December 15, 2003. On September 30, 2004, the FASB Board directed the issuance of FASB Staff Position (FSP) EITF Issue 03-1-a, *Implementation Guidance for the Application of Paragraph 16 of EITF Issue No. 03-1*. The proposed FSP would provide implementation guidance with respect to debt securities that are impaired solely due to interest rates and/or sector spreads and analyzed for other-than-temporary impairment under paragraph 16 of Issue 03-1. The FASB also asked constituents to comment on whether the application guidance with respect to minor impairments should also be applied to securities analyzed for impairment under paragraphs 10-15 of Issue 03-1. Based on comment letters received, the FASB decided to delay the effective date for the measurement and recognition guidance contained in Issue 03-1 as it further considers whether application guidance is necessary for all securities analyzed for impairment. The delay of the effective date for paragraphs 10-20 of Issue 03-1 will be superseded concurrent with the final issuance of FSP EITF Issue 03-1-a. The adoption of EITF Issue No. 03-1 is not expected to have a material impact on the Company's results of operations and financial position.

NOTE D CORE DEPOSIT INTANGIBLES, NET

The following is a summary of the Company's core deposit intangibles. Figures are in thousands (unaudited).

| | Gross Amount | Sept. 30, 2004 Accumulated Amortization | Net Carrying Amount | Gross Amount | Sept. 30, 2003 Accumulated Amortization | Net Carrying Amount |
|----------------------------|-----------------|---|------------------------|-----------------|---|------------------------|
| Core Deposit Intangible | \$ 11,596 | \$ (3,520) | \$ 8,076 | \$ 8,870 | \$ (2,172) | \$ 6,698 |

| | Dec. 31, 2003 | | | | | |
|-------------------------|---------------|--------|--------------|---------|--------------|-------|
| | Gross | | Accumulated | | Net Carrying | |
| | Amount | | Amortization | | Amount | |
| Core Deposit Intangible | \$ | 11,596 | \$ | (2,489) | \$ | 9,107 |

Aggregate Amortization Expense of Core Deposit Intangibles (\$ in 000 s):

| | Nine Month Period Ended Sept. 30, | |
|---|-----------------------------------|--------|
| | 2004 | 2003 |
| Amortization of Core Deposit Intangible | \$ 1,031 | \$ 804 |

The amortization expense for core deposit intangibles is included within other operating expenses on the consolidated statements of income. The projected amortization expense for core deposit intangibles, assuming no further acquisitions or dispositions, is approximately \$1.4 million per year over the next five years.

NOTE E STOCK OPTIONS

At September 30, 2004, the Company had one stock option plan which is described more fully in Note 15 in the Company's 2003 Annual Report on Form 10-K. The Company accounts for stock options using the intrinsic value method under the provisions of Accounting Principles Board (APB) Opinion No. 25 and provides proforma net income and proforma earnings per share disclosures for employee stock option grants as if the fair-value-based method, defined in SFAS No. 123, Accounting for Stock-Based Compensation, had been applied. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's net income would have been reduced to the pro forma amounts indicated below for the three and nine month periods ended September 30:

| (dollars in 000 s except per share amounts) | Three Month Period Ended Sept. 30, | | Nine Month Period Ended Sept. 30, | |
|--|------------------------------------|----------|-----------------------------------|-----------|
| | 2004 | 2003 | 2004 | 2003 |
| Net income, as reported | \$ 8,673 | \$ 8,975 | \$ 25,711 | \$ 24,778 |
| Deduct: Total stock-based compensation expense determined under the fair value based method for all awards, net of related taxes | (484) | (395) | (1,408) | (1,186) |
| Pro-forma net income | \$ 8,189 | \$ 8,580 | \$ 24,303 | \$ 23,592 |
| Basic income per share, as reported | \$ 0.37 | \$ 0.39 | \$ 1.09 | \$ 1.06 |
| Pro-forma basic income per share | \$ 0.35 | \$ 0.37 | \$ 1.03 | \$ 1.01 |
| Diluted income per share, as reported | \$ 0.36 | \$ 0.37 | \$ 1.07 | \$ 1.01 |
| Pro-forma diluted income per share | \$ 0.34 | \$ 0.35 | \$ 1.01 | \$ 0.96 |

Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is management's discussion and analysis of the major factors that influenced our financial performance for the three months and nine months ended September 30, 2004. This analysis should be read in conjunction with our 2003 Annual Report as filed on Form 10-K and with the unaudited financial statements and notes as set forth in this report. *Unless the context requires otherwise, the terms "Company," "us," "we," and "our" refers to Mid-State Bancshares on a consolidated basis.*

Certain statements contained in this Quarterly Report of Form 10-Q ("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. Such forward looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements 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 we operate, demographic changes, competition, fluctuations in interest rates, changes in business strategy or development plans, changes in governmental regulation, credit quality, the availability of capital to fund the expansion of our business, economic, political and global changes arising from the war on terrorism, the conflict with Iraq and its aftermath, and other factors referenced in our 2003 Annual Report as filed on form 10-K, including in Item 1. Business Factors That May Affect Future Results of Operations. When relying on forward-looking statements to make decisions with respect to our Company, investors and others are cautioned to consider these and other risks and uncertainties. We disclaim 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 our financial statements, including the notes thereto, appearing elsewhere in this report.

Critical Accounting Policies and Estimates This Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as, disclosures included elsewhere in this Form 10-Q, are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements require Management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingencies. A summary of the more significant accounting policies of the Company can be found in Footnote One to the financial statements which is included in Item 8 of the Company's Annual Report on Form 10-K and in the Management's Discussion and Analysis included in Item 7 of that same report entitled "Critical Accounting Policies and Estimates."

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Selected Financial Data Summary The following table provides certain selected consolidated financial data as of and for the three months and nine months ending September 30, 2004 and 2003 (unaudited in 000 s, except per share data).

| | Quarter Ended | | Year-to-Date | |
|---|----------------|----------------|----------------|----------------|
| | Sept. 30, 2004 | Sept. 30, 2003 | Sept. 30, 2004 | Sept. 30, 2003 |
| Interest Income | \$ 28,236 | \$ 26,643 | \$ 81,093 | \$ 78,715 |
| Interest Expense | 2,083 | 2,157 | 6,149 | 7,559 |
| Net Interest Income | 26,153 | 24,486 | 74,944 | 71,156 |
| (Benefit)/Provision for Loan Losses | | | (2,700) | 260 |
| Net Interest Income after provision for loan losses | 26,153 | 24,486 | 77,644 | 70,896 |
| Non-interest income | 7,250 | 7,838 | 22,160 | 22,236 |
| Non-interest expense | 20,265 | 18,589 | 60,836 | 54,990 |
| Income before income taxes | 13,138 | 13,735 | 38,968 | 38,142 |
| Provision for income taxes | 4,465 | 4,760 | 13,257 | 13,364 |
| Net Income | \$ 8,673 | \$ 8,975 | \$ 25,711 | \$ 24,778 |
| Per share: | | | | |
| Net Income basic | \$ 0.37 | \$ 0.39 | \$ 1.09 | \$ 1.06 |
| Net Income diluted | \$ 0.36 | \$ 0.37 | \$ 1.07 | \$ 1.01 |
| Weighted avg. shares used in Basic E.P.S. calc. | 23,369 | 23,287 | 23,496 | 23,441 |
| Weighted avg. shares used in Diluted E.P.S. calc. | 23,842 | 24,350 | 23,949 | 24,487 |
| Cash dividends | \$ 0.14 | \$ 0.13 | \$ 0.42 | \$ 0.37 |
| Book value at period-end | | | \$ 11.94 | \$ 11.25 |
| Tangible book value at period end | | | \$ 9.54 | \$ 9.43 |
| Ending Shares | | | 23,323 | 23,191 |
| Financial Ratios | | | | |
| Return on assets | 1.50% | 1.72% | 1.53% | 1.65% |
| Return on tangible assets | 1.53% | 1.76% | 1.57% | 1.69% |
| Return on equity | 12.47% | 13.61% | 12.42% | 12.77% |
| Return on tangible equity | 15.64% | 16.22% | 15.61% | 15.25% |
| Net interest margin (not taxable equiv.) | 5.01% | 5.14% | 4.93% | 5.23% |
| Net interest margin (taxable equivalent yield) | 5.41% | 5.53% | 5.34% | 5.63% |
| Net loan (recoveries) losses to avg. loans | (0.01)% | 0.38% | (0.06)% | 0.09% |
| Efficiency ratio | 60.7% | 57.5% | 62.7% | 58.9% |
| Period Averages | | | | |
| Total Assets | \$ 2,306,318 | \$ 2,069,078 | \$ 2,249,562 | \$ 2,002,806 |
| Total Tangible Assets | 2,250,254 | 2,026,932 | 2,193,155 | 1,960,666 |
| Total Loans (incl. loans held for sale) | 1,358,768 | 1,140,493 | 1,279,738 | 1,129,684 |
| Total Earning Assets | 2,077,356 | 1,889,499 | 2,031,150 | 1,818,879 |
| Total Deposits | 2,005,694 | 1,787,933 | 1,951,211 | 1,724,251 |
| Common Equity | 276,652 | 261,692 | 276,426 | 259,408 |
| Common Tangible Equity | 220,587 | 219,546 | 220,019 | 217,268 |

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| | Sept. 30, 2004 | | Sept. 30, 2003 | |
|---|----------------|------------------|----------------|------------------|
| Balance Sheet At Period-End | | | | |
| Cash and due from banks | \$ | 119,104 | \$ | 109,469 |
| Investments and Fed Funds Sold | | 688,923 | | 767,741 |
| Loans held for sale | | 10,001 | | 42,075 |
| Loans, net of deferred fees, before allowance for loan losses | | 1,394,478 | | 1,091,113 |
| Allowance for Loan Losses | | (13,912) | | (16,871) |
| Goodwill and core deposit intangibles | | 55,916 | | 42,217 |
| Other assets | | 55,033 | | 50,405 |
| Total Assets | \$ | 2,309,543 | \$ | 2,086,149 |
| | | | | |
| Non-interest bearing deposits | \$ | 524,785 | \$ | 436,565 |
| Interest bearing deposits | | 1,474,782 | | 1,358,227 |
| Other borrowings | | 5,843 | | 7,907 |
| Allowance for losses - unfunded commitments | | 1,682 | | 1,862 |
| Other liabilities | | 23,989 | | 20,767 |
| Shareholders' equity | | 278,462 | | 260,821 |
| Total Liabilities and Shareholders' equity | \$ | 2,309,543 | \$ | 2,086,149 |
| | | | | |
| Asset Quality & Capital At Period-End | | | | |
| Non-accrual loans | \$ | 10,954 | \$ | 12,562 |
| Loans past due 90 days | | | | |
| Other real estate owned | | | | 3,279 |
| Total non performing assets | \$ | 10,954 | \$ | 15,841 |
| | | | | |
| Allowance for losses to loans, gross (1) | | 1.1% | | 1.7% |
| Non-accrual loans to total loans, gross | | 0.8% | | 1.2% |
| Non performing assets to total assets | | 0.5% | | 0.8% |
| Allowance for losses to non performing loans (1) | | 142.4% | | 149.1% |
| | | | | |
| Equity to average assets (leverage ratio) | | 9.5% | | 10.2% |
| Tier One capital to risk-adjusted assets | | 12.4% | | 14.7% |
| Total capital to risk-adjusted assets | | 13.3% | | 16.0% |

(1) Includes allowance for loan losses and allowance for losses - unfunded commitments

Performance Summary. The Company posted net income of \$8.7 million for the three months ended September 30, 2004 compared to \$9.0 million in the like 2003 period. On a per share basis, diluted earnings per share were \$0.36 in the 2004 period compared to \$0.37 in the same quarter of 2003. These earnings represent an annualized return on assets of 1.50% and 1.72%, respectively. The annualized return on equity was 12.47% for the third quarter of 2004 compared to 13.61% in the third quarter of 2003. The decline in the Company's return on assets and return on equity in the comparable periods is primarily attributable to a decline in its net interest margin (the ratio of its net interest income to average earning assets), increases in other operating expenses and a decline in its gain on sale of mortgage loans held for sale. The Company's leverage ratio was 9.5% at September 30, 2004 compared to 10.2% one year earlier reflecting both the Company's on-going stock repurchase program and the premium paid on October 31, 2003 for the acquisition of Ojai Valley Bank.

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Comparing results across the two time periods is affected by the Company's acquisition of the aforementioned Ojai Valley Bank. Ojai Valley Bank, which was not part of the Company's third quarter 2003 results, earned \$205 thousand in the three months ended September 30, 2003 and \$695 thousand in the nine months ended September 30, 2003. The former Ojai Valley Bank's assets, deposits and certain of its staff members were integrated throughout 2004.

For the nine months year-to-date, the Company posted net income of \$25.7 million compared to \$24.8 million earned in the like 2003 period. Diluted earnings per share were \$1.07 in the first nine months of 2004 compared to \$1.01 in the like period one year earlier. These earnings represent an annualized return on assets of 1.53% and 1.65%, respectively, for the comparable 2004 and 2003 periods. The annualized return on equity was 12.42% for the first nine months of 2004 compared to 12.77% in the first nine months of 2003. The decline in the return on assets and return on equity is again primarily attributable to a decline in its net interest margin (the ratio of its net interest income to average earning assets), increases in other operating expenses and a decline in its gain on sale of mortgage loans held for sale. Notwithstanding the decline in return on equity and return on assets across the two periods, Net Income actually increased especially because of a benefit to the provision for loan losses of \$2.7 million which occurred in the second quarter of the year.

Net Interest Income. The following table delineates the impacts of changes in the volume of earning assets, changes in the volume of interest bearing liabilities, and changes in interest rates on net interest income for the three month periods ended September 30, 2004 and 2003.

| Dollars in 000 \$ | 3 Months Ended Sept. 30, 2004 | | | 3 Months Ended Sept. 30, 2003 | | | 2004 Compared to 2003 Composition of Change | | |
|---|----------------------------------|---------------------------------|----------------------------|----------------------------------|---------------------------------|----------------------------|--|--------------------|-----------------|
| | Average Balance | Interest Income / Expense | Average Yield / Rate | Average Balance | Interest Income / Expense | Average Yield / Rate | Change Due To: Volume | Rate | Total Change |
| EARNING ASSETS: | | | | | | | | | |
| Loans | \$ 1,358,768 | \$ 22,106 | 6.47% | \$ 1,140,493 | \$ 20,574 | 7.16% | \$ 3,739 | \$ (2,207) | \$ 1,532 |
| Investment Securities | 675,237 | 5,981 | 3.52% | 626,614 | 5,806 | 3.68% | 440 | (265) | 175 |
| Fed Funds, Other | 43,351 | 149 | 1.37% | 122,392 | 263 | 0.85% | (221) | 107 | (114) |
| TOTAL BEARING ASSETS | 2,077,356 | 28,236 | 5.41 % | 1,889,499 | 26,643 | 5.59 % | 3,958 | (2,365) | 1,593 |
| INTEREST BEARING LIABILITIES: | | | | | | | | | |
| NOW, Savings, and Money Market Accounts | 1,085,220 | 654 | 0.24% | 951,724 | 497 | 0.21% | 75 | 82 | 157 |
| Time Deposits | 400,035 | 1,395 | 1.39% | 396,014 | 1,619 | 1.62% | 15 | (239) | (224) |
| Interest Bearing Deposits | 1,485,255 | 2,049 | 0.55% | 1,347,738 | 2,116 | 0.62% | 90 | (157) | (67) |
| Other Borrowings | 3,258 | 34 | 4.15% | 5,596 | 41 | 2.91% | (21) | 14 | (7) |
| TOTAL INTEREST BEARING LIABILITIES | 1,488,513 | 2,083 | 0.56 % | 1,353,334 | 2,157 | 0.63 % | 69 | (143) | (74) |
| NET INTEREST INCOME | \$ 2,077,356 | \$ 26,153 | 5.01 % | \$ 1,889,499 | \$ 24,486 | 5.14 % | \$ 3,889 | \$ (2,222) | \$ 1,667 |

Mid-State's annualized yield on interest earning assets was 5.41% for the third quarter of 2004 (5.81% on a taxable equivalent basis) compared to 5.59% in the like 2003 period (5.99% on a taxable equivalent basis). While the Prime Rate, to which many of the Bank's loans are tied, averaged 4.41% in the third quarter of 2004 compared to 4.00% in the like 2003 period, the extended period of low interest rates has dropped the yields being earned on fixed rate loans and fixed rate investment securities more dramatically (higher yields have been replaced with lower yielding instruments) than the higher prime based loans. Annualized interest expense as a percent of interest bearing liabilities also decreased from 0.63% in the three months ended September 2003 to 0.56% in the comparable 2004 period. The lower overall cost of the time deposit portfolio was the primary reason for this drop. Overall, Mid-State's annualized Net Interest Income, expressed as a percent of earning assets, decreased from 5.14% for the three month period of 2003 (5.53% on a taxable equivalent basis) to 5.01% in the comparable 2004 period (5.41% on a taxable equivalent basis). Annualized Net Interest Income as a percent of average total assets declined from 4.70% in the third quarter of 2003

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(5.05% taxable equivalent) to 4.51% in the comparable 2004 period (4.87% taxable equivalent). The impact of the decline in net interest margin by itself would have caused net interest income to decline, however, as noted in the table above, the increase in volume of loans and investment securities increased net interest income. The combination of the volume and rate considerations resulted in net interest income increasing across the comparable periods (\$26.2 million in the third quarter of 2004 compared to \$24.5 million in the like 2003 period). The Company is attempting to improve its net interest margin (and consequently its return on assets and return on equity) by altering the mix of its earning asset base in favor of more loans resulting in fewer investment securities and lower fed funds sold. Steps taken in this direction have included the restructuring of the commercial banking division, focused promotions of certain consumer loan products, retention of certain jumbo residential adjustable rate mortgages and the purchase of residential adjustable mortgages. The mix did improve modestly across the two quarters with loans averaging 65.4% of earning assets in the 2004 quarter compared to 60.4% in the 2003 quarter.

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Average earnings assets for the three months ended September 30, 2004 increased \$187.9 million from the like 2003 period (\$2,077.4 million compared to \$1,889.5 million). Approximately \$82.0 million of this increase relates to the acquisition completed October 31, 2003 of Ojai Valley Bank. Average interest bearing deposits in this same time-frame were up \$137.5 million, (\$1,485.3 million compared to \$1,347.7 million) of which approximately \$79.0 million can be traced to that merger.

The following table presents a similar analysis of changes in interest income and expense for the nine month period ended September 30, 2004 and 2003.

| Dollars in 000 s | 9 months ended | | | 9 months ended | | | 2004 Compared to 2003 Composition of Change | | |
|---|---------------------|---|----------------------------|---------------------|---|----------------------------|--|-------------------|-----------------|
| | Average Balance | Sept. 30, 2004 Interest Income / Expense | Average Yield / Rate | Average Balance | Sept. 30, 2003 Interest Income / Expense | Average Yield / Rate | Change Due To: Volume | Rate | Total Change |
| <i>EARNING ASSETS:</i> | | | | | | | | | |
| Loans | \$ 1,279,738 | \$ 62,343 | 6.51% | \$ 1,129,684 | \$ 60,461 | 7.16% | \$ 7,674 | \$ (5,792) | \$ 1,882 |
| Investment Securities | 713,774 | 18,444 | 3.45% | 608,510 | 17,650 | 3.88% | 2,888 | (2,094) | 794 |
| Fed Funds, Other | 37,638 | 306 | 1.09% | 80,684 | 604 | 1.00% | (336) | 38 | (298) |
| TOTAL EARNING ASSETS | 2,031,150 | 81,093 | 5.33% | 1,818,878 | 78,715 | 5.79% | 10,226 | (7,848) | 2,378 |
| <i>INTEREST BEARING LIABILITIES:</i> | | | | | | | | | |
| NOW, Savings, and Money Market Accounts | 1,054,537 | 1,855 | 0.23% | 915,261 | 1,997 | 0.29% | 275 | (417) | (142) |
| Time Deposits | 400,182 | 4,143 | 1.38% | 398,312 | 5,448 | 1.83% | 22 | (1,327) | (1,305) |
| Interest Bearing Deposits | 1,454,719 | 5,998 | 0.55% | 1,313,573 | 7,445 | 0.76% | 297 | (1,744) | (1,447) |
| Other Borrowings | 4,386 | 151 | 4.60% | 4,422 | 114 | 3.45% | (1) | 38 | 37 |
| TOTAL INTEREST BEARING LIABILITIES | 1,459,105 | 6,149 | 0.56% | 1,317,995 | 7,559 | 0.77% | 296 | (1,706) | (1,410) |
| NET INTEREST INCOME | \$ 2,031,150 | \$ 74,944 | 4.93% | \$ 1,818,878 | \$ 71,156 | 5.23% | \$ 9,930 | \$ (6,142) | \$ 3,788 |

Mid-State's year-to-date annualized yield on interest earning assets was 5.33% for the first nine months of 2004 (5.74% on a taxable equivalent basis) compared to 5.79% in the like 2003 period (6.18% on a taxable equivalent basis). The Prime Rate, to which many of the Bank's loans are tied, averaged 4.14% in the first nine months of 2004 compared to 4.16% in the like period of 2003. Additionally, the extended period of low interest rates has dropped the yields being earned on fixed rate loans and fixed rate investment securities significantly (higher yields have been replaced with lower yielding instruments). Annualized interest expense as a percent of interest bearing liabilities also decreased from 0.77% in the first nine months of 2003 to 0.56% in the comparable 2004 period.

Overall, Mid-State's annualized Net Interest Income, expressed as a percent of earning assets, decreased from 5.23% for the first nine month period of 2003 (5.63% on a taxable equivalent basis) to 4.93% in the comparable 2004 period (5.34% on a taxable equivalent basis). Annualized Net Interest Income as a percent of average total assets (not shown in the table above) declined from 4.75% in the first nine months of 2003 (5.11% taxable equivalent) to 4.45% in the comparable 2004 period (4.82% taxable equivalent). As with the quarterly comparison, the impact of the decline in net interest margin by itself would have caused net interest income to decline, however, as noted in the table above, the increase in volume of loans and investment securities completely offset this decrease. The combination of the volume and rate considerations resulted in net interest income increasing across the comparable periods (\$74.9 million in the first nine months of 2004 compared to \$71.2 million in the like 2003 period). Average earnings assets for the nine months ended September 30, 2004 increased from the like 2003 period (\$2,031.2 million compared to \$1,818.8 million).

Provision and Allowance for Loan Losses. Mid-State did not make a provision for loan losses in either the third quarter of 2004 or 2003. For the nine months ended September 30, 2003 the Company had made a provision for loan losses of \$260 thousand and for the comparable 2004 period it took a benefit to the provision for loan losses of \$2.7 million.

Management believes that the allowance for loan losses and allowance for losses - unfunded commitments, which collectively stand at 1.1% of total loans at September 30, 2004, are adequate to cover inherent losses in the portfolio. Management has determined that the allocated and unallocated components of the reserve as calculated and required for its non performing loans and the general loan loss reserve, are sufficient to offset potential losses arising from less than full recovery of the loans from the supporting collateral. Non performing loans consist of loans on non-accrual and accruing loans 90 days or more past due. The \$15.6 million of collective allowances for credit losses is approximately 142% of the level of non performing loans compared to 149% one year earlier. Non performing loans were \$11.0 million at September 30, 2004 compared to \$12.6 million one year earlier. Additionally, the Bank carried Other Real Estate Owned in the amount of \$3.3 million one year earlier compared to none at September 30, 2004. The Other Real Estate Owned was liquidated in the second quarter of 2004. A combination of loan payoffs and improvements in the underlying credit quality of certain borrowers led to a dramatic drop in internally classified assets.

The improving trend in non performing loans, continued improvements in the level of internally classified assets, net recoveries from the Company's on-going collection efforts and continuing improvement in local economic conditions have significantly improved the Company's asset quality. These factors led to Management's decision to take the aforementioned \$2.7 million benefit to the provision for loan losses.

The unallocated portion of the allowance for loan losses was reduced from the level of approximately \$6.7 million at the end of May 2004 to approximately \$4.0 million by virtue of the benefit to the provision for loan losses recorded in the second quarter. During the first quarter review of the allowance, it was decided not to reduce the allowance as there was continuing uncertainty surrounding the loss potential in two of the Company's problem credits and there was still some uncertainty surrounding general economic conditions. During Management's review of the allowance in June, circumstances had changed dramatically with respect to two significant problem credits with much of the uncertainty of loss lifted. Moreover, further evidence suggested improving trends in the overall economy. Less significantly, but a factor nonetheless, there has also been a very modest change in portfolio mix over the last twelve months with real estate secured loans (excluding Construction and Land Development) now accounting for 63.5% of the portfolio compared to 55.4% one year earlier. These loans carry general reserves in the allowance for loan loss calculation at a lower rate (due to historically lower loss rates) than other categories of loans. This had a minor effect on the size of the unallocated portion of the allowance. Terms offered on most categories of loans have remained substantially similar over this period of time and did not have a bearing on the change in the allowance for loan losses.

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Changes in the allowance for loan losses (in thousands) for the periods ended September 30, 2004 and 2003 are as follows:

| | Three Months Ended Sept. 30, | | Nine Months Ended Sept. 30, | |
|---|------------------------------|-----------|-----------------------------|-----------|
| | 2004 | 2003 | 2004 | 2003 |
| Balance at beginning of period: | | | | |
| Allowance for loan losses | \$ 13,895 | \$ 17,963 | \$ 16,063 | \$ 17,370 |
| Allowance for losses-unfunded commitments | 1,570 | 1,812 | 1,941 | 1,771 |
| Total allowances for losses at beginning of period | 15,465 | 19,775 | 18,004 | 19,141 |
| Additions (reductions) to the allowance for losses unfunded commitments charged (credited) to expense | 112 | 50 | (259) | 91 |
| Additions (reductions) to the allowance for loan losses charged (credited) to provision | | | (2,700) | 260 |
| Loans charged off | (118) | (1,404) | (665) | (1,645) |
| Recoveries of loans previously charged-off | 135 | 312 | 1,214 | 886 |
| Total allowances for losses-end of quarter | \$ 15,594 | \$ 18,733 | \$ 15,594 | \$ 18,733 |
| Allowance for loan losses | \$ 13,912 | \$ 16,871 | \$ 13,912 | \$ 16,871 |
| Allowance for losses-unfunded commitments | 1,682 | 1,862 | 1,682 | 1,862 |
| Total allowances for losses-end of quarter | \$ 15,594 | \$ 18,733 | \$ 15,594 | \$ 18,733 |

At September 30, 2004, the recorded investments in loans, which have been identified as impaired, totaled \$11,035,000. Of this amount, \$1,478,000 related to loans with no valuation allowance and \$9,557,000 related to loans with a corresponding valuation allowance of \$4,413,000. Impaired loans totaled \$23,219,000 at September 30, 2003. Of this amount, \$12,893,000 related to loans with no valuation allowance and \$10,326,000 related to loans with a corresponding valuation allowance of \$2,217,000. For the quarter ended September 30, 2004, the average recorded investment in impaired loans was \$11,257,000 compared to \$19,131,000 in the 2003 period. The reduction is primarily the result of the payoff and principal reductions of certain impaired loans. A loan is identified as impaired when it is probable that interest and principal will not be collected according to the contractual terms of the loan agreement. Because this definition is very similar to that used by bank regulators to determine on which loans interest should not be accrued, the Bank expects that most impaired loans will be on non-accrual status.

Non-interest Income. Non-interest income for the third quarter of 2004 was \$7.3 million, down from the \$7.8 million earned in the 2003 period. There was an increase in service charges and fees of approximately \$303 thousand over the comparable periods, primarily as a result of the implementation of a new decision plan module for handling non-sufficient fund and overdraft accounts. The slowdown in refinance activity caused the net gain on sale of mortgage loans held for sale to decline to \$40 thousand in the third quarter of 2004 compared to \$1.0 million in the comparable quarter of 2003 due to a lower portfolio of loans available for sale. Gain on sale of securities rose from \$14 thousand in the third quarter of 2003 to \$93 thousand in the comparable 2004 period. Other non-interest income decreased slightly from \$1.0 million in the third quarter of 2003 to \$998 thousand in the comparable 2004 period.

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For the nine months ended September 30, 2004, non-interest income was virtually identical to the same 2003 period at \$22.2 million. There was an increase in service charges and fees of approximately \$811 thousand over the comparable periods, primarily as a result of the implementation of a new decision plan module for handling non-sufficient fund and overdraft accounts. Pre-tax securities gains increased by \$432 thousand across the comparable periods. The majority of this was due to accepting a tender offer for a \$1.0 million block of corporate bonds held by the Bank resulting in a \$352 thousand gain in the first quarter of 2004. Other non-interest income rose from \$2.4 million in the first nine months of 2003 to \$3.5 million in the comparable 2004 period. The increase was primarily due to a gain on the sale of other real estate of approximately \$1.1 million. Offsetting these increases in non interest income across the comparable nine month periods was a decline in the net gain on sale of mortgage loans held for sale of \$2.6 million. This was because of the dramatic slowdown in refinance activity currently being experienced widely by the mortgage industry. Management expects this source of income to be lower for the full year 2004 compared to 2003 levels. However, it should be noted that the fourth quarter of 2004 should be comparable to the fourth quarter of 2003 as the refinance boom experienced in 2003 was generally in the first three quarters of the year and not a factor over the final three months.

Non-interest Expense. Non-interest expense for the third quarter of 2004 was \$20.3 million. This compares to \$18.6 million in the like 2003 period. This increase was the result of increases in salaries and benefits of approximately \$1.0 million, an increase in occupancy and furniture expense of \$136 thousand and an increase in other operating expenses of \$567 thousand.

The increase in salaries and benefits in the comparable quarters was comprised of \$0.7 million in salary increases and \$0.3 million in benefit cost increases. The amount of increase was influenced by several factors, including: 1) the addition of employees from the acquisition of Ojai Valley Bank resulting in approximately \$284 thousand more salaries and benefits expense, 2) increases in the Company cost of health care coverage for employees of approximately \$217 thousand, 3) increases in workers compensation premiums of approximately \$117 thousand, and 4) regular salary increases.

The increases in Occupancy expense across the comparable quarters noted above was primarily attributable to increased rental expenses for the new Ojai facilities and partly to increases in maintenance, utility and depreciation expenses.

The increases in Other expense across the comparable quarters noted above was primarily attributable to increased advertising and promotional expenses of approximately \$383 thousand and the increased cost of professional services of \$343 thousand (primarily fees paid to consultants and auditors to comply with the new Sarbanes Oxley corporate governance requirements). Other expenses actually declined in this category resulting in the net increase of \$567 thousand noted above.

Non-interest expense for the first nine months of 2004 was \$60.8 million. This compares to \$55.0 million in the comparable 2003 period. This increase was the result of increases in salaries and benefits of approximately \$4.0 million, an increase in occupancy and furniture expense of \$0.7 million and an increase in other operating expenses of \$1.1 million.

The increase in salaries and benefits in the comparable nine month periods was comprised of \$2.1 million in salary increases and \$1.9 million in benefit cost increases. The amount of increase was influenced by several factors, including: 1) the addition of employees from the acquisition of Ojai Valley Bank resulting in approximately \$817 thousand more salaries and benefits expense, 2) increases in accrual rates for incentive compensation of \$350 thousand, 3) increases in the Company cost of health care coverage for employees of approximately \$545 thousand, 4) increases in workers compensation premiums of \$222 thousand, and 5) regular salary increases representing the majority of the balance of the increase.

The increases in Occupancy expense across the comparable nine month periods noted above was primarily attributable to increased rental expenses for the new Ojai facilities and partly to increases in maintenance, and utility expenses.

The increase in other operating expenses is due primarily to increases in advertising and promotion expense of \$844 thousand and the increased cost of professional services of \$341 thousand (primarily fees paid to consultants and auditors to comply with the new Sarbanes Oxley corporate governance requirements). Other expenses actually declined in this category resulting in the net increase of \$1.1 million noted above.

Provision for Income Taxes. The year-to-date provision for income taxes declined modestly from \$13.4 million in the 2003 period to \$13.3 million in the current year. For the third quarter of 2004 the provision for income taxes declined by \$295 thousand, down from the \$4.8 million in the 2003 period to \$4.5 million. The year-to-date effective tax rate in 2004 is 34.0% compared to 35.0% in 2003. While the normal combined federal and state statutory tax rate is 42% for Mid-State Bancshares, the tax-exempt income generated by its municipal bond portfolio is the primary reason that the effective rate is lower.

Balance Sheet. Total assets at September 30, 2004 totaled \$2.310 billion, up 10.7% from the level one year earlier of \$2.086 billion. This growth was fueled primarily by an increase in deposits of 11.4% to \$2.000 billion, up from \$1.795 billion one year earlier. Part of the growth in deposits (approximately \$79.0 million) was due to the merger with Ojai Valley Bank on October 31, 2003. While Time Deposits under \$100 thousand decreased from \$236.3 million one year earlier to \$231.1 million at period end, the Time Deposits over \$100 thousand increased by \$11.9 million. All other core deposit categories of Demand, NOW, Money Market and Savings increased to \$1.600 billion from \$1.402 billion one year earlier. In an ongoing effort to improve earnings, the Company continues to focus its attention on attracting lower cost core deposits and has consciously chosen not to pay the higher rates on certain more expensive Time Deposits. Loan activity over the last year has increased, with net loans increasing by \$307 million from \$1.074 billion to \$1.381 billion at period-end. Approximately \$30 million of this growth was due to the merger with Ojai Valley Bank. Loans held for sale (single family, mortgage originations) decreased by \$32.1 million to \$10.0 million from one year earlier, reflecting the slow-down in refinance activity. Stockholders' equity increased by \$17.6 million when comparing September, 2004 over September, 2003 (see below under Capital Resources for a recap of the components of this change).

Mid-State Bancshares' loan to deposit ratio of 69.7% at September 30, 2004 is up from the 60.8% ratio one year earlier. There is ample internal liquidity to fund increases in this ratio through liquidation of Mid-State's \$688.9 million investment portfolio which is categorized entirely as available for sale.

Investment Securities and Fed Funds Sold. Of the \$688.9 million portfolio at September 30, 2004, 5% is invested in U.S. treasury securities, 36% is invested in U.S. government agency obligations, 58% is invested in municipal and corporate securities and 1% is invested in mortgage-backed securities. Sixty-two percent of all investment securities and fed funds sold combined mature within five years. Approximately 21% of the total portfolio matures in less than one year. The Bank's investment in mortgage-backed securities consist of investments in FNMA and FHLMC pools which have contractual maturities of up to 15 years. The actual time of repayment may be shorter due to prepayments made on the underlying collateral.

A summary of investment securities owned is as follows:

September 30, 2004

| (amounts in 000 s) | Cost Basis | Gross Unrealized Gains | Gross Unrealized Losses | Market Value |
|---|------------|------------------------|-------------------------|--------------|
| Securities Available For Sale | | | | |
| U.S. Treasury securities | \$ 31,694 | \$ 23 | \$ (72) | \$ 31,645 |
| Securities of U.S. government agencies and corporations | 247,731 | 1,514 | (584) | 248,661 |
| Mortgage backed securities | 8,861 | 619 | (37) | 9,443 |
| Obligations of states and political subdivisions | 368,807 | 14,395 | (273) | 382,929 |
| Other investments | 16,016 | 229 | | 16,245 |
| TOTAL | \$ 673,109 | \$ 16,780 | \$ (966) | \$ 688,923 |

September 30, 2003

| (amounts in 000 s) | Cost Basis | Gross Unrealized Gains | Gross Unrealized Losses | Market Value |
|---|------------|------------------------|-------------------------|--------------|
| Securities Available For Sale | | | | |
| U.S. Treasury securities | \$ 65,517 | \$ 519 | \$ | \$ 66,036 |
| Securities of U.S. government agencies and corporations | 244,232 | 5,725 | (108) | 249,849 |
| Mortgage backed securities | 5,762 | 623 | | 6,385 |
| Obligations of states and political subdivisions | 329,566 | 16,082 | (374) | 345,274 |
| Other investments | 14,115 | 782 | | 14,897 |
| TOTAL | \$ 659,192 | \$ 23,731 | \$ (482) | \$ 682,441 |

The following table shows those investments with gross unrealized losses and their market value aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2004.

| (amounts in 000 s) | Less than 12 months | | 12 months or more | | Total | |
|---|---------------------|-------------------|-------------------|-------------------|--------------|-------------------|
| | Market Value | Unrealized Losses | Market Value | Unrealized Losses | Market Value | Unrealized Losses |
| U.S. Treasury securities | \$ 26,103 | \$ (72) | \$ | \$ | \$ 26,103 | \$ (72) |
| Securities of U.S. government agencies and corporations | 116,102 | (451) | 9,964 | (133) | 126,066 | (584) |
| Mortgage backed securities | 1,789 | (37) | | | 1,789 | (37) |
| Obligations of states and political subdivisions | 9,967 | (52) | 3,821 | (221) | 13,788 | (273) |
| Other investments | | | | | | |
| TOTAL | \$ 153,961 | \$ (612) | \$ 13,785 | \$ (354) | \$ 167,746 | \$ (966) |

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All of the unrealized losses identified in the table above are primarily attributable to changes in general interest rate levels and are not considered to be other than temporary impairment. The unrealized losses are not the result of any deteriorating financial conditions or near term prospects of the underlying issuers and Management believes that it has the intent and ability to retain these investment securities to allow for the eventual recovery in market value.

Capital Resources. At the start of 2004, there were 872 shares of the Company's common stock remaining for repurchase under the Board of Directors May 2002 stock repurchase program authorization. At its regular Board meeting of January 21, 2004, the Board authorized the repurchase of up to 1,178,352 additional shares of the Company's common stock. The new authorization does not have an expiration date. There were 215,607 shares repurchased in the third quarter of 2004 at an average price of \$24.38 per share compared to 207,541 shares repurchased in the third quarter of 2003 at an average price of \$20.95 per share. Year-to-date, the Company has repurchased 373,819 shares at an average price of \$23.59 per share compared to 625,830 repurchased in the like 2003 period at an average price of \$18.93 per share. As of September 30, 2004, the Company is continuing the program and can repurchase up to 805,405 additional shares under the January authorization.

In other matters concerning capital, the Board of Directors declared three quarterly 2004 dividends of \$0.14 per share, or \$0.42 for the nine months, representing a 13.5% increase over the \$0.37 declared in the first nine months of 2003. The Company paid a dividend of \$0.13 in the third quarter of 2003.

Total stockholders' equity increased from \$260.8 million at September 30, 2003 to \$278.5 million at September 30, 2004. Changes in stockholders' equity over this 12 month period includes activity outlined in the following table (in 000's):

| | Common Stock & Surplus | Retained Earnings | Accumulated Comp. Income | Total |
|---|---|------------------------------|---|-------------------|
| Ending Equity at Sept. 30, 2003 | \$ 67,424 | \$ 179,448 | \$ 13,949 | \$ 260,821 |
| Net Income 3 Months 2003 (Oct. - Dec.) | | 8,386 | | 8,386 |
| Common Stock Repurchased 3 Months 2003 (Oct. - Dec.) | (4,362) | | | (4,362) |
| Stock Options Exercised - 3 Months 2003 (Oct. - Dec.) | 598 | | | 598 |
| Regular Dividends 3 Months 2003 (Oct. - Dec.) | | (3,063) | | (3,063) |
| Change in Accumulated Other Comprehensive Income | | | (1,672) | (1,672) |
| Shares issued in connection with merger | 11,846 | | | 11,846 |
| Ending Equity at December 31, 2003 | 75,506 | 184,771 | 12,277 | 272,554 |
| Net Income 9 Months Y-T-D 2004 | | 25,711 | | 25,711 |
| Common Stock Repurchased 9 Months Y-T-D 2004 | (8,817) | | | (8,817) |
| Stock Options Exercised 9 Months Y-T-D | 1,659 | | | 1,659 |
| Regular Dividends - 9 Months Y-T-D 2004 | | (9,856) | | (9,856) |
| Change in Accumulated Other Comprehensive Income | | | (2,789) | (2,789) |
| Ending Equity at Sept. 30, 2004 | \$ 68,348 | \$ 200,626 | \$ 9,488 | \$ 278,462 |

Liquidity. The focus of the Company's liquidity management is to ensure its ability to meet cash requirements. Sources of liquidity include cash, due from bank balances (net of Federal Reserve requirements to maintain reserves against deposit liabilities), fed funds sold, investment securities (net of pledging requirements), loan repayments, deposits and fed funds borrowing lines. Typical demands on liquidity are deposit run-off from demand deposits and savings accounts, maturing time deposits, which are not renewed, and anticipated funding under credit commitments to customers.

The Bank has adequate liquidity at the present time. Its loan to deposit ratio at September 30, 2004 was 69.7% versus 60.8% one year earlier. The Bank normally strives for a loan to deposit ratio in the 65% to 75% range. The Bank's internally calculated liquidity ratio stands at 36.4% at September 30, 2004, which is above its minimum policy of 15% and below the 44.3% level of September 30, 2003. Management is not aware of any future capital expenditures or other significant demands or commitments which would severely impair liquidity.

Off Balance Sheet Transactions and Other Related Transactions. Off-balance sheet arrangements are any contractual arrangement to which an unconsolidated entity is a party, under which the Company has: 1) any obligation under a guarantee contract; 2) a retained or contingent interest in assets transferred to an unconsolidated entity or similar arrangement that serves as credit, liquidity or market risk support to that entity for such assets; 3) any obligation under certain derivative instruments; or 4) any obligation under a material variable interest held by the Company in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to the Company, or engages in leasing, hedging or research and development services with the Company. 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.

The Company is contingently liable for letter of credit accommodations made to its customers in the ordinary course of business totaling \$29.1 million at September 30, 2004, down from \$30.7 million one year earlier. Additionally, the Company has undisbursed loan commitments, also made in the ordinary course of business, totaling \$633.6 million, which was up from the \$478.1 million outstanding one year earlier. The Company has an allowance for losses-unfunded commitments totaling \$1,682,000 and \$1,862,000 at September 30, 2004 and 2003, respectively, to cover losses inherent in its letter of credit accommodations and undisbursed loan commitments.

There are no Special Purpose Entity (SPE) trusts, corporations, or other legal entities established by Mid-State which reside off-balance sheet. There are no other off-balance sheet items other than the aforementioned items related to letter of credit accommodations and un-disbursed loan commitments.

The Company does make loans and leases to related parties (directors and officers) in the ordinary course of business at prevailing rates and terms. These loans and leases totaled \$9.0 million and \$1.5 million at September 30, 2004 and 2003, respectively.

In the ordinary course of business, the Bank is a party to various operating leases. For a fuller discussion of these financial instruments, refer to Note 6 of the Company's consolidated financial statements contained in Item 8 of Part II of the Company's December 31, 2003 Form 10K.

Item 3 - Quantitative and Qualitative Disclosure About Market Risk

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The Bank expects its risk exposure to changes in interest rates to remain manageable and well within acceptable policy ranges. A recent review as of September 30, 2004 of the potential changes in the Bank's net interest income over a 12 month time horizon showed that it could fluctuate under extreme alternative rate scenarios from between +4.4% and -8.1% of the base case (rates unchanged) of \$105.3 million. The Bank's policy is to maintain a structure of assets and liabilities which are such that net interest income will not vary more than plus or minus 15% of the base forecast over the next 12 months. Management expects that its exposure to interest rate risk is manageable and it will continue to strive for an optimal trade-off between risk and earnings.

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The following table presents a summary of the Bank's net interest income forecasted for the coming 12 months under alternative interest rate scenarios.

| | Change From Base |
|---|-------------------------|
| Rates Down Very Significant (Prime down to 2.75% over 6 months) | -8.1% |
| Rates Down Significant (Prime down to 3.50% over 7 months) | -4.1% |
| Rates Down Modestly (Prime down to 4.00% over 7 months) | -1.6% |
| Base Case - Rates Unchanged (Prime unchanged at 4.75% over 12 months) | |
| Rates Up Modestly (Prime up to 5.75% over 10 months) | +1.2% |
| Rates Up Aggressive (Prime up to 6.75% over 10 months) | +2.8% |
| Rates Up Very Aggressive (Prime up to 7.75% over 10 months) | +4.4% |

Net interest income under the above scenarios is influenced by the characteristics of the Bank's assets and liabilities. In the case of N.O.W., savings and money market deposits (total \$1.076 billion) interest is based on rates set at the discretion of management ranging from 0.05% to 0.80%. In a downward rate environment, there is a limit to how far these deposit instruments can be re-priced and this behavior is similar to that of fixed rate instruments. In an upward rate environment, the magnitude and timing of changes in rates on these deposits is assumed to be more reflective of variable rate instruments.

It is important to note that the above table is a summary of several forecasts and actual results may vary. The forecasts are based on estimates and assumptions of management that may turn out to be different and may change over time. Factors affecting these estimates and assumptions include, but are not limited to - competitors' behavior, economic conditions both locally and nationally, actions taken by the Federal Reserve Board, customer behavior, and management's responses. Changes that vary significantly from the assumptions and estimates may have significant effects on the Bank's net interest income. Therefore the results of this analysis should not be relied upon as indicative of actual future results. Historically, the Bank has been able to manage its Net Interest Income in a fairly narrow range reflecting the Bank's relative insensitivity to interest rate changes. The impact of prepayment behavior on mortgages, real estate loans, mortgage backed securities, securities with call features, etc. is not considered material to the sensitivity analysis. Over the last 5 calendar years (1999 - 2003), the Bank's net interest margin (which is net interest income divided by average earning assets of the Bank) had ranged from a low of 5.14% to a high of 6.44% (not taxable equivalent). The Bank's net interest margin in 2003 of 5.14% is at the low end of this range by historical standards, coming off the higher levels experienced in 2000 of 6.44%. In the first six months of 2004, the net interest margin fell further to 4.89%, but recent increases in interest rates (e.g. three 25 basis point increases in the Federal Funds Rate and Prime Rate) which began at the end of June have led to an improving net interest margin for the Bank to 5.01% in the third quarter of this year. The net interest margin under the forecasted alternative scenarios ranges from 4.44% to 5.04%. Management believes this range of scenarios, while lower than historical standards, is conservative given current interest rate levels, but no assurances can be given that actual future experience will fall within this range.

The Bank's exposure with respect to interest rate derivatives, exchange rate fluctuations, and/or commodity price movements is nil. The Bank does not own any instruments within these markets.

Item 4 Controls and Procedures

As of the end of the period covered by this report, Management, including the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures with respect to the information generated for use in this Quarterly Report. The evaluation was based in part upon reports and affidavits provided by a number of executives. Based upon, and as of the date of that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective to provide reasonable assurances that information required to be disclosed in the reports the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within time periods specified in the SEC's rules and forms.

There was no change in the Company's internal controls over financial reporting during the quarter ended September 30, 2004 that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

In designing and evaluating disclosure controls and procedures, the Company's Management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable, not absolute, assurances of achieving the desired control objectives and Management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

Mid-State is not a party to any material legal proceeding.

Item 2 - Changes in Securities and Use of Proceeds

On January 21, 2004, the Company's board of directors authorized the repurchase of up to 1,178,352 shares of the Company's common stock. During the three months ended September 30, 2004, the Company repurchased 215,607 shares of common stock at an average price of \$24.38. All of these shares were purchased in open market transactions. As of September 30, 2004, 805,405 shares are available to be repurchased in the future under this repurchase plan.

The following table provides the information with respect to the purchases made under the publicly announced stock repurchase program during the third quarter ended September 30, 2004:

| Period | Total Number of Shares Purchased | Average Price Paid Per Share | Remaining Shares That May be Purchased Under the Authorization | Dollar Value of Shares That May be Purchased Under the Authorization (3) |
|---------------|--|------------------------------------|--|--|
| July 2004 | 81,824 | \$ 23.97 | 939,188 | \$ 22,888,012 |
| August 2004 | 69,052 | \$ 23.94 | 870,136 | \$ 21,231,318 |
| Sept. 2004 | 64,731 | \$ 25.36 | 805,405 | \$ 20,723,071 |
| Totals | 373,819 | \$ 23.59 | 805,405 | \$ 20,723,071 |

(1) The May 2002 authorization provided for the repurchase of up to 1,203,580 shares of stock. There was no expiration date associated with the authorization.

(2) On January 21, 2004, the Board of Directors authorized the repurchase of an additional 1,178,352 shares of stock. There was no expiration date associated with the authorization.

(3) Value is based on the closing price of the Company's stock multiplied by the number of shares that may be purchased under the authorization.

Item 3 - Defaults Upon Senior Securities**Item 4 - Controls and Procedures**

Not applicable.

Item 4 - Submission of Matters to a Vote of Security Holders

There were no items presented to the security holders during the third quarter of 2004.

Item 5 - Other Information

Not applicable.

Item 6 - Exhibits and Reports on Form 8-K

A) Exhibits

| Exhibit No. | Exhibit |
|--------------------|--|
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32 | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

B) Reports on Form 8-K

The Company filed its first report on Form 8-K during the third quarter of 2004 on July 23, 2004, it announced the Company's financial results for the second quarter of 2004. The Press Release dated July 22, 2004 was attached.

The Company filed its second report on Form 8-K on September 22, 2004 to report that on September 15, 2004 at its regular meeting of the Board of Directors of Mid-State Bancshares, the Board declared a fourteen cents per-share quarterly cash dividend for all shareholders of record on September 30, 2004, payable on October 15, 2004. The Press Release dated September 21, 2004 was attached.

SIGNATURES

Pursuant to the requirement of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Mid-State Bancshares

Date: November 5, 2004

By:

/s/ JAMES W. LOKEY
JAMES W. LOKEY
President and
Chief Executive Officer
(Principal Executive Officer)

Date: November 5, 2004

By:

/s/ JAMES G. STATHOS
JAMES G. STATHOS
Executive Vice President and
Chief Financial Officer
(Principal Accounting Officer)

EXHIBIT INDEX

| Exhibit No. | Description | | |
|-------------|--|--|--|
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