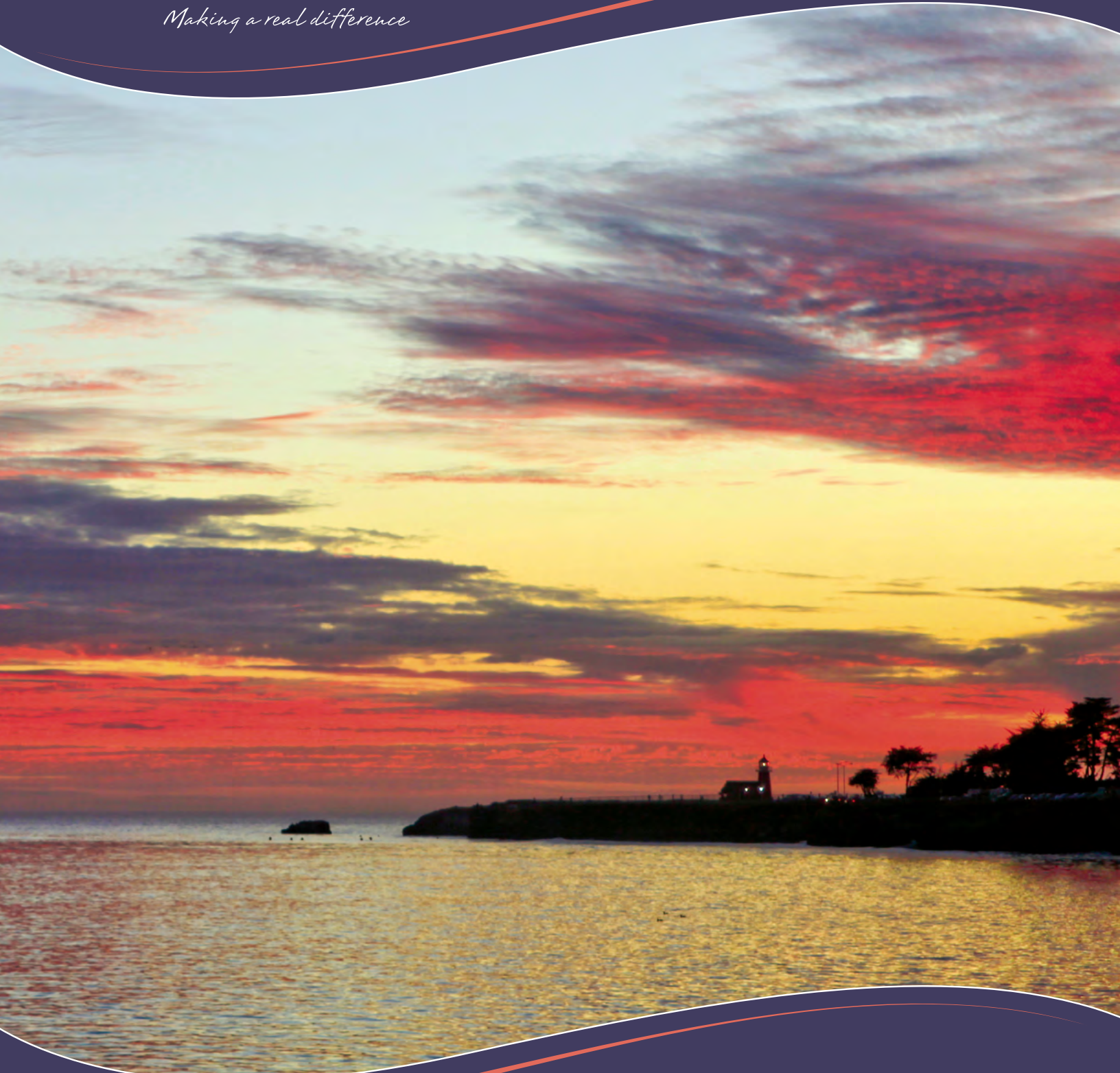




Bay Federal

CREDIT UNION

Making a real difference



2011 Annual Report

A Letter from the Chairperson and the President and CEO



While the national economy continues to show signs of slow improvement, Santa Cruz County also gained a sense of strength. We began to see evidence of increasing consumer confidence towards the second half of 2011 in member and loan growth. While the world grappled with the Eurozone debt crisis, oil price spikes, the Japanese earthquake and nuclear fallout and the financial market turmoil, including the downgrading of the US government debt ratings, we focused on how to better serve the financial needs of the people in Santa Cruz County. Highlights include:

- We welcomed over 2,000 new members as a result of dissatisfaction with the mega national banks and Bank Transfer Day.
- Our CFS* Investment Services program, rated among the top 10% of CFS clients in the nation, assisted our members with investing over \$12.5 million in 2011.
- Bay Federal financed \$61 million in single-family and mobile home loans, and was ranked among the top 300 of all credit unions nationwide for mortgage loan fundings.
- We reintroduced our indirect lending program for Bay Federal financing at local auto dealerships, resulting in \$13 million in auto loans.
- 88% of members surveyed rated the overall service experience at Bay Federal excellent or very good.
- 100% of Bay Federal Credit Union employees donated their time and money to assist local non-profit organizations for the 9th consecutive year.
- Bay Federal raised over \$11,000 to help provide local storm and tsunami relief.

Yet, we recognize the demand for aid in our community continues, even as we have seen these improvements. In 2011, we continued to provide members experiencing financial hardship with loan modifications to help them keep their homes and vehicles. Over 400 students and adults benefited from our financial literacy efforts, including free classroom presentations and evening seminars. We also continue to offer free financial counseling and educational resources for our entire membership through our relationship with BALANCE Financial Fitness.

Behind the scenes, we worked to improve efficiencies and reduce operating expenses throughout our organization. Due to the hard work and dedication of our employees and volunteer Board of Directors, we ended 2011 with a net income of \$1.6 million and an increase in deposits of 7.20%. Our capital ratio is considered adequately capitalized at 6.09%.

Our member and community support efforts continue to be recognized by local and trade organizations. In 2011, Bay Federal was recognized with the following awards:

- Voted the "Best Financial Institution" by readers of the regional newspapers, including the Good Times, Press Banner and Santa Cruz Weekly.
- Named the "Organization of the Year" by the United Way of Santa Cruz County.
- Won the Marketing Association of Credit Union's Gold Award for outstanding product/service brochures, for implementing ecologically and economically-intelligent designs utilizing local photography.

As we look ahead to 2012, we are excited about investments in our infrastructure to offer a more convenient and integrated banking experience. This includes the installation of new image-enabled ATMs across our network, the introduction of mobile banking and online applications, and enhancement of our internal technology to improve the branch experience.

We are also prepared to face the challenges that may arise with an unstable national economy and dynamic regulatory environment. We will continue to fine tune the business model to improve the bottom line and strength of our locally owned financial cooperative.

We wish to express our sincere appreciation to the entire membership, our employees and our dedicated volunteers that serve on our Board of Directors and Supervisory Committee. Your generous support of our financial cooperative truly allows us to make a real difference in the lives of those who we serve.

Sincerely,

Dennis Osmer,
Chairperson

Carrie L. Birkhofer,
President and CEO

* Non-deposit investment products and services are offered through CUSO Financial Services, L.P. ("CFS"), a registered broker-dealer (Member FINRA/SIPC) and SEC Registered Investment Advisor. Products offered through CFS: **are not NCUA/NCUSIF or otherwise federally insured, are not guarantees or obligations of the credit union, and may involve investment risk including possible loss of principal.** Investment Representatives are registered through CFS. Bay Federal Credit Union has contracted with CFS to make non-deposit investment products and services available to credit union members.



Supervisory Committee and Treasurer's Report

In 2011, Bay Federal Credit Union's assets grew by 6.80% and ended the year at \$651 million, driven by a growth in core savings, checking and money market deposits. The Credit Union posted earnings of \$1.6 million and remained adequately capitalized with a net worth ratio of 6.09%. These results were achieved due to robust non-interest income growth and lower than expected operating expenses, despite \$7 million of loan charge-offs. Both the dollar amount and the number of delinquent loans declined in 2011, although mortgage loan losses have continued due to the decrease in home values.

The Supervisory Committee secured the services of Orth, Chakler, Murnan and Company to perform a certified financial audit of the Credit Union in 2011. The CPAs stated that the financial statements presented fairly the financial position of the Credit Union as of June 30, 2011.

The Credit Union continued its focus on improving internal controls and enhancing risk management procedures this year, utilizing industry experts for best practices.

While the Credit Union had strong financial results in 2011, the reality of the continued economic challenges faced by our members and our community at large does impact the Credit Union. We continue to monitor significant exposure to losses from "underwater" home loans, but we have mitigated actual losses by modifying home loans to give the borrowers more affordable payments.

Bay Federal Credit Union strives to offer exceptional and affordable services to all of our members, in times of prosperity and in times of need. We have served our community since 1957 and will remain dedicated to this purpose for years to come.

We are grateful to the Board, the Management Team and the employees of Bay Federal Credit Union for their commitment to a strong set of core values and a commendable work ethic which is demonstrated every day. We would like to extend our warm appreciation to our membership, on behalf of our entire organization, for making Bay Federal Credit Union your financial institutions of choice.

“We are excited about the opportunities that abound with investments in our infrastructure to offer a more convenient and integrated banking experience.”

Statement of Income

for the year ending December 31, 2011 (unaudited)

INTEREST INCOME

Interest on Loans	\$ 23,931,034
Interest on Investments	\$ 1,845,311
Total Interest Income	\$ 25,776,345

INTEREST EXPENSE

Dividends and Interest	\$ 4,456,761
Interest on Borrowed Money	\$ 2,829,196
Total Interest Expense	\$ 7,285,957

Net Interest Income	\$ 18,490,388
Provision for Loan Losses	\$ 4,407,300

Interest Income Net of Provision	\$ 14,083,088
Non-Interest Income	\$ 9,139,076

OPERATING EXPENSES

Compensation and Benefits	\$ 12,256,237
Operations	\$ 3,043,518
Occupancy	\$ 1,590,718
Other Expenses	\$ 4,711,743
Total Operating Expenses	\$ 21,602,216
Net Income	\$ 1,619,948

Statement of Financial Condition

as of December 31, 2011 (unaudited)

ASSETS

Member Loans (net)	\$ 420,662,596
Cash	\$ 12,030,432
Investments	\$ 191,850,488
Land, Building and Equipment	\$ 13,969,271
Other	\$ 12,426,264
Total Assets	\$ 650,939,051

LIABILITIES, DEPOSITS AND EQUITY

Notes Payable	\$ 71,000,000
Other Liabilities	\$ 10,322,073
Member Deposits	\$ 529,702,921
Equity	\$ 39,914,057
Total Liabilities, Deposits and Equity	\$ 650,939,051



Board of Directors

Dennis Osmer
Chairperson

H. Duane Smith
Vice Chairperson

Michael Leung
Treasurer

Ivonne J. Guzman
Secretary

Bob Bugalski
Director

Sheila Joyce Kellerman
Director

Kathleen Lawler Bodmer
Director

Larry Hebert
Associate Director

Danny Keith
Associate Director

Jessica Dixon
Associate Director

Jim Phillips
Associate Director

Supervisory Committee

Patricia J. Pfremmer
Chairperson

Phil Kidder
Committee Member

Richard Mills
Committee Member

Bob Bugalski
Board Liaison

President and CEO

Carrie L. Birkhofer



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