PELICAN FINANCIAL INC
Form 10-Q
August 13, 2003

U.S. Securities and Exchange Commission

Washington, D.C. 20549

Form 10-Q

ý	**Quarterly Report Pursuant To Section 13 or 15 (d) of the Securities Exchange Act of 1934**

For the Quarter Ended June 30, 2003

Or

o	**Transition Report Pursuant To Section 13 or 15 (d) of the Securities Exchange Act of 1934**

Commission file number 000-26601

Pelican Financial, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**58-2298215**
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

3767 Ranchero Drive
Ann Arbor, Michigan 48108
(Address of Principal Executive Offices)

734-662-9733
(Registrant s Telephone Number, Including Area Code)

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

Indicate the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date:

Common Stock Outstanding as of July 31, 2003

Common stock, $0.01 Par value	4,441,221 Shares

Index

PELICAN FINANCIAL, INC.

Consolidated Balance Sheets

	June 30, 2003 (Unaudited)	December 31, 2002
ASSETS		
Cash and cash equivalents		
Cash and due from banks	$ 5,027,284	$ 10,410,554
Interest-bearing deposits	107,944,204	33,005,000
Federal funds sold	6,530,701	13,946,381
Total cash and cash equivalents	119,502,189	57,361,935
Accounts receivable, net	6,826,540	7,962,115
Securities available for sale	4,984,310	2,560,305
Federal Reserve & Federal Home Loan Bank Stock	1,230,000	1,330,000
Loans held for sale	248,234,005	192,488,348
Loans receivable, net	104,291,350	104,533,053
Mortgage servicing rights, net	14,041,059	13,799,691
Other real estate owned	1,855,102	1,293,148
Premises and equipment, net	2,712,114	2,410,902
Other assets	2,068,723	1,958,466
	$ 505,745,392	$ 385,697,963
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities		
Deposits		
Noninterest-bearing	$ 123,817,309	$ 87,304,821
Interest-bearing	73,168,975	66,428,958
Total deposits	196,986,284	153,733,779
Due to bank	58,302,118	34,849,016
Notes payable	74,605,436	43,866,403
Repurchase agreements	94,569,913	82,987,994
Federal Home Loan Bank borrowings	18,000,000	18,000,000
Other liabilities	26,153,250	20,430,113
Total liabilities	468,617,001	353,867,305
Commitments and contingencies		
Shareholders equity		
Preferred stock, 200,000 shares authorized; none outstanding		
Common stock, $.01 par value 10,000,000 shares authorized; 4,441,221 and 4,440,241 outstanding at June 30, 2003 and December 31, 2002 respectively	44,412	44,402
Additional paid in capital	15,351,796	15,345,573
Retained earnings	21,726,859	16,426,842

Accumulated other comprehensive income, net of tax		5,324		13,841
Total shareholders equity		37,128,391		31,830,658
	$	505,745,392	$	385,697,963

See accompanying notes to the financial statements

PELICAN FINANCIAL, INC.

Consolidated Statements of Income and Comprehensive Income (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Interest income				
Loans, including fees	$ 6,237,562	$ 4,373,744	$ 11,580,229	$ 10,376,294
Investment securities, taxable	125,779	180,401	204,261	292,240
Federal funds sold and overnight accounts	145,002	78,691	245,017	119,503
Total interest income	6,508,343	4,632,836	12,029,507	10,788,037
Interest expense				
Deposits	548,019	850,761	1,132,734	1,742,569
Other borrowings	1,989,911	1,273,732	3,653,143	2,935,773
Total interest expense	2,537,930	2,124,493	4,785,877	4,678,342
Net interest income	3,970,413	2,508,343	7,243,630	6,109,695
Provision for loan losses	290,000	80,000	370,000	230,000
Net interest income after provision for loan losses	3,680,413	2,428,343	6,873,630	5,879,695
Noninterest income				
Gain on sales of securities	57,708	50,070	129,360	50,070
Service charges on deposit accounts	47,615	31,302	100,209	72,122
Servicing income	1,718,934	1,649,970	3,444,115	2,919,617
Gain on sales of mortgage servicing rights and loans, net	15,089,407	2,956,481	26,550,985	11,793,457
Other income	369,160	165,623	542,182	227,506
Total noninterest income	17,282,824	4,853,446	30,766,851	15,062,772
Noninterest expense				
Compensation and employee benefits	7,627,988	2,782,718	13,675,940	8,012,540
Occupancy and equipment	697,299	452,175	1,315,631	824,986
Telephone	180,823	141,926	333,868	289,180
Postage	213,581	134,869	404,867	279,761
Amortization of loan servicing rights	1,461,817	1,197,376	2,649,485	2,126,862
Loan servicing rights valuation adjustment	2,830,175	2,718,506	4,635,179	2,881,523
Other noninterest expense	2,983,335	1,482,877	5,210,075	3,165,019
Total noninterest expense	15,995,018	8,910,447	28,225,045	17,579,871
Income (loss) before income taxes	4,968,219	(1,628,658)	9,415,436	3,362,596
Provision for income taxes	1,711,098	(549,306)	3,227,287	1,151,624

Net income (loss)	$	3,257,121	$	(1,079,352)	$	6,188,149	$	2,210,972
Basic earnings (loss) per share	$	0.73	$	(0.24)	$	1.39	$	0.50
Diluted earnings (loss) per share	$	0.73	$	(0.24)	$	1.39	$	0.49
Comprehensive income (loss)	$	3,394,568	$	(1,028,246)	$	6,179,632	$	2,232,839

See accompanying notes to the financial statements

PELICAN FINANCIAL, INC.

Consolidated Statements of Cash Flows (Unaudited)

Six Months Ended June 30,

	2003	2002
Cash flows from operating activities		
Net cash provided (used) by operating activities	$ (59,217,700)	$ 127,989,757
Cash flows from investing activities		
Loans receivable originations, net	(128,297)	(6,377,778)
Proceeds from sales of mortgage servicing rights	16,746,523	6,176,072
Other real estate owned, net	(561,954)	(702,296)
Property and equipment expenditures, net	(635,694)	(887,440)
Purchase of securities available for sale	(44,775,000)	(12,000,000)
Proceeds from sales of securities available for sale	42,457,589	9,610,070
Proceeds from maturities and principal repayments of securities available for sale	10,127	1,370,279
Purchase (retirement) of Federal Reserve Stock	100,000	(260,000)
Net cash provided (used) by investing activities	13,213,294	(3,071,093)
Cash flows from financing activities		
Increase in deposits	43,252,505	28,244,064
Increase (decrease) in due to bank	23,453,102	(15,309,672)
Increase (decrease) in notes payable due on demand	30,739,032	(39,790,864)
Advances on Federal Home Loan Bank borrowings		4,000,000
Proceeds from exercise of stock options	6,233	154,603
Cash dividends	(888,131)	
Increase (decrease) in repurchase agreements	11,581,919	(76,585,624)
Net cash provided (used) by financing activities	108,144,660	(99,287,493)
Net change in cash and cash equivalents	62,140,254	25,631,171
Cash and cash equivalents at beginning of period	57,361,935	16,884,630
Cash and cash equivalents at end of period	$ 119,502,189	$ 42,515,801

See accompanying notes to the financial statements

PELICAN FINANCIAL, INC.

Notes to the Consolidated Financial Statements (Unaudited)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation:

The unaudited consolidated financial statements as of and for the three and six months periods ended June 30, 2003 and 2002, include the accounts of Pelican Financial Inc. (Pelican Financial) and its wholly owned subsidiaries Pelican National Bank (Pelican National) and Washtenaw Mortgage Company (Washtenaw) for all periods. All references herein to Pelican Financial include the consolidated results of its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Stock Compensation:

Compensation expense under stock options is reported using the intrinsic value method. No stock-based compensation cost is reflected in net income, as all options granted had an exercise price equal to or greater than the market price of the underlying common stock at date of grant. The following table illustrates the effect on net income and earnings per share if expense was measured using the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*.

	Three Months Ended June 30,			
		2003		2002
Net income as reported	$	3,257,121	$	(1,079,352)
Stock-based compensation expense, net of forfeitures, using fair value method		9,778		(14,528)
Pro forma net income	$	3,266,899	$	(1,093,880)
Basic earnings per share as reported	$	0.73	$	(0.24)
Pro forma basic earnings per share		0.74		(0.24)
Diluted earnings per share	$	0.73	$	(0.24)
Pro forma diluted earnings per share		0.73		(0.24)

	Six Months Ended June 30,			
		2003		2002
Net income as reported	$	6,188,149	$	2,210,972
Stock-based compensation expense, net of forfeitures, using fair value method		724		(29,056)
Pro forma net income	$	6,188,873	$	2,181,916
Basic earnings per share as reported	$	1.39	$	0.50
Pro forma basic earnings per share		1.39		0.50

Diluted earnings per share	$	1.39	$	0.49
Pro forma diluted earnings per share		1.39		0.49

<u>Cumulative Effect of Change in Accounting Principle:</u>

The Derivative Implementation Group (DIG) of the Financial Accounting Standards Board (FASB) issued guidance on mortgage loan rate lock commitments to borrowers. The guidance categorizes as derivatives rate lock commitments on loans intended for sale, and was effective July 1, 2002. Upon adopting this guidance on July 1, 2002, the Company began recording the fair value of rate lock commitments as derivatives, and accordingly the fair value of rate lock commitments is included in the June 30, 2003 financial statements but is not included in the June 30, 2002 financial statements. The effect of following this guidance on the June 30, 2003 financial statements was a reduction of pre-tax income of $1,661,028.

NOTE 2 BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include information or footnotes necessary for a complete presentation of consolidated financial condition, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. However, all adjustments, consisting of normal recurring accruals, which, in the opinion of management, are necessary for fair presentation of the consolidated financial statements have been included. The results of operations for the period ended June 30, 2003, are not necessarily indicative of the results which may be expected for the entire fiscal year or for any other period. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2002 included in Pelican Financial s Form 10-K.

Certain prior year amounts have been reclassified to conform to the 2003 presentation.

NOTE 3 LOANS RECEIVABLE

Loans receivable consist of the following:

		June 30, 2003		December 31, 2002
Commercial, financial and agricultural	$	636,154	$	962,713
Commercial real estate		50,358,666		59,542,563
Residential real estate		39,668,267		43,377,309
Installment loans		14,756,400		1,712,577
		105,419,487		105,595,162
Deduct allowance for loan losses		(1,128,137)		(1,062,109)
Loans receivable, net	$	104,291,350	$	104,533,053

Activity in the allowance for loan losses for the quarter ended June 30, are as follows:

		2003		2002
Balance at beginning of period	$	1,046,243	$	976,964
Provision for loan losses		290,000		80,000
Loans charged-off		(208,106)		(356)
Recoveries				285
Balance at end of period	$	1,128,137	$	1,056,893

7

Activity in the allowance for loan losses for the six months ended June 30, are as follows:

		2003		2002
Balance at beginning of period	$	1,062,109	$	856,216
Provision for loan losses		370,000		230,000
Loans charged-off		(314,110)		(31,206)
Recoveries		10,138		1,883
Balance at end of period	$	1,128,137	$	1,056,893

NOTE 4 - EARNINGS PER SHARE

The following summarizes the computation of basic and diluted earnings (loss) per share.

		Three Months ended June 30, 2003		Three Months ended June 30, 2002
Basic earnings (loss) per share				
Net income (loss)	$	3,257,121	$	(1,079,352)
Weighted average shares outstanding		4,440,930		4,410,673
Basic earnings (loss) per share	$	0.73	$	(0.24)
Diluted earnings (loss) per share				
Net income (loss)	$	3,257,121	$	(1,079,352)
Weighted average shares outstanding		4,440,930		4,410,673
Dilutive effect of assumed exercise of stock options		37,560		
Diluted average shares outstanding		4,478,490		4,410,673
Diluted earnings (loss) per share	$	0.73	$	(0.24)

		Six Months ended June 30, 2003		Six Months ended June 30, 2002
Basic earnings per share				
Net income	$	6,188,149	$	2,210,972
Weighted average shares outstanding		4,440,560		4,401,982
Basic earnings per share	$	1.39	$	0.50
Diluted earnings per share				
Net income	$	6,188,149	$	2,210,972
Weighted average shares outstanding		4,440,560		4,401,982
Dilutive effect of assumed exercise of stock options		22,968		65,566
Diluted average shares outstanding		4,463,528		4,467,548
Diluted earnings per share	$	1.39	$	0.49

NOTE 5 - SEGMENT INFORMATION

Pelican Financial s operations include two primary segments: mortgage banking and retail banking. The mortgage banking segment involves the origination and purchase of single-family residential mortgage loans in approximately 40 states; the sale of such loans in the secondary market, generally on a pooled and securitized basis; and the servicing of mortgage loans for investors. The retail-banking segment involves attracting deposits from the general public and using such funds to originate and purchase existing consumer, commercial, commercial real estate, residential construction, and single-family residential mortgage loans, from its offices in Naples, San Carlos and Fort Myers, Florida.

Of the two segments, Pelican National comprises the retail-banking segment, with net interest income from loans, investments and deposits accounting for its primary revenues. Washtenaw comprises the mortgage-banking segment, with gains on sales of mortgage servicing rights (MSR) and loans, as well as loan servicing income accounting for its primary revenues.

The following segment financial information has been derived from the internal financial statements of Pelican National and Washtenaw, which are used by management to monitor and manage the financial performance of Pelican Financial. The accounting policies of the two segments are the same as those of Pelican Financial.

The evaluation process for segments does not include holding company income and expense. Holding company amounts are the primary difference between segment amounts and consolidated totals, and are reflected in the Other column below, along with minor amounts to eliminate transactions between segments.

Dollars in thousands

	Retail Banking	Mortgage Banking	Other	Consolidated Totals
Three Months Ended June 30, 2003				
Net interest income	$ 1,930	$ 2,040	$	$ 3,970
Gain on sales of MSR and loans, net	46	15,043		15,089
Servicing income	5	1,714		1,719
Noncash items:				
Provision for loan losses	290			290
MSR amortization & valuation	4	4,288		4,292
Provision for income taxes	108	1,786	(183)	1,711
Segment profit/(loss)	207	3,406	(356)	3,257
Segment assets	232,740	273,007	(2)	505,745
Three Months Ended June 30, 2002				
Net interest income	$ 1,577	$ 937	$ (6)	$ 2,508
Gain on sales of MSR and loans, net	110	2,846		2,956
Servicing income	3	1,647		1,650
Noncash items:				
Provision for loan losses	80			80
MSR amortization & valuation	3	3,913		3,916
Provision for income taxes	256	(765)	(40)	(549)
Segment profit/(loss)	496	(1,496)	(79)	(1,079)
Segment assets	166,317	109,020	(52)	275,285

Dollars in thousands

	Retail Banking	Mortgage Banking	Other	Consolidated Totals
Six Months Ended June 30, 2003				
Net interest income	$ 3,682	$ 3,562	$	$ 7,244
Gain on sales of MSR and loans, net	71	26,480		26,551
Servicing income	10	3,434		3,444
Noncash items:				
Provision for loan losses	370			370
MSR amortization & valuation	8	7,276		7,284
Provision for income taxes	288	3,162	(223)	3,227
Segment profit/(loss)	557	6,065	(434)	6,188
Segment assets	232,740	273,007	(2)	505,745
Six Months Ended June 30, 2002				
Net interest income	$ 3,096	$ 3,027	$ (13)	$ 6,110
Gain on sales of MSR and loans, net	222	11,571		11,793
Servicing income	5	2,915		2,920
Noncash items:				
Provision for loan losses	230			230

MSR amortization & valuation	5	5,003		5,008
Provision for income taxes	463	801	(112)	1,152
Segment profit/(loss)	897	1,532	(218)	2,211
Segment assets	166,317	109,020	(52)	275,285

NOTE 7 SUBSEQUENT EVENTS

On July 24, 2003, Pelican Financial, issued a press release announcing the intent to spin-off Washtenaw Mortgage Company into a newly formed separate company called The Washtenaw Group, Inc. It is anticipated that Pelican Financial, Inc. shareholders will receive identical holdings in the newly formed company.

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

Forward Looking Statements

Certain information in this Form 10-Q may constitute forward-looking information that involves risks and uncertainties that could cause actual results to differ materially from those estimated. Persons are cautioned that such forward-looking statements are not guarantees of future performance and are subject to various factors that could cause actual results to differ materially from those estimated. These factors include, but are not limited to, changes in general economic and market conditions, legislative and regulatory changes, monetary and fiscal policies of the federal government, demand for loan and deposit products and the development of an interest rate environment that adversely affects the interest rate spread or other income from Pelican Financial s investments and operations.

EARNINGS PERFORMANCE

Pelican Financial reported net income of $3.3 million for the quarter ended June 30, 2003, an increase of $4.4 million when compared to net the net loss of $1.1 million for the same period in 2002. Earnings per share, basic and diluted, were $0.73 per share compared to a net loss of $0.24 per share for the three months ended June 30, 2003 and 2002 respectively. The primary cause for the improvement is the increase in mortgage loan production. This is due to the low mortgage interest rates during the quarter.

For the six months ended June 30, 2003 Pelican Financial reported net income of $6.2 million compared to $2.2 million for the same period in 2002. Basic and diluted earnings per share were $1.39 for the six months ended June 30, 2003 compared to $0.50 basic and $0.49 diluted, for the six months ended June 30, 2002.

For further explanation of the earnings performance, please see the discussion on the retail and mortgage banking segments to follow.

RESULTS OF OPERATIONS

Retail Banking

The following discussion provides information that relates specifically to Pelican Financial s retail banking line of business.

For the three months ended June 30, 2003, Pelican Financial s net income from retail banking activities primarily conducted by Pelican National totaled $207,000. For the three months ended June 30, 2002 Pelican National s comparable net income was $496,000. For the six months ended June 30, 2003, Pelican Financial s net income from retail banking activities primarily conducted by Pelican National totaled $557,000. For the six months ended June 30, 2002 Pelican National s comparable net income was $897,000.

The decrease in net income for both the three and six month periods was primarily attributable to an increase in the provision for loan losses and noninterest expense partially offset by an increase in net interest income.

Net Interest Income

Net Interest Income was $1.9 million and $1.6 million for the three months ended June 30, 2003 and 2002, respectively. For the six months ended June 30, 2003 and 2002 net interest income was $3.7 million and $3.1 million respectively. The increase in net interest income was due primarily to an increase in the average interest bearing assets outstanding as well as a decrease in the cost of funds. This was partially offset by a decrease in yield on interest earning assets.

Average Balance Sheet

The following tables summarizes the average yields earned on interest-earning assets and the average rates paid on interest-bearing liabilities for Pelican Financial. With the exception of loans held for sale and other borrowings, the interest earning-assets and interest-bearing liabilities are attributable to Pelican National.

	Three months ended June 30,					
	2003			2002		
	Average Volume	Interest	Yield/Cost	Average Volume	Interest	Yield/Cost
ASSETS						
Interest-earning assets:						
Federal funds sold	$ 46,382	$ 145	1.25%	$ 18,626	$ 79	1.70%
Securities	9,630	126	5.23	11,172	180	6.44
Loans held for sale	241,817	4,062	6.72	131,869	2,308	7.00
Loans receivable, net	110,018	2,175	7.91	104,543	2,066	7.90
Total interest-earning assets	407,847	6,508	6.38	266,210	4,633	6.96
Non-earning assets	20,367			38,471		
Total assets	$ 428,214			$ 304,681		
LIABILITIES AND STOCKHOLDERS EQUITY						
Interest-bearing liabilities:						
NOW accounts	$ 744	1	0.53	$ 859	2	0.93
Money market accounts	14,119	49	1.39	5,720	34	2.38
Savings deposits	12,840	44	1.37	10,778	64	2.38
Time deposits	47,809	454	3.80	61,552	751	4.88
Other borrowings	199,476	1,990	3.99	122,030	1,274	4.18
Total interest-bearing liabilities	274,988	2,538	3.69	200,939	2,125	4.23
Noninterest-bearing liabilities	120,100			72,001		
Stockholders equity	33,126			31,741		
Total liabilities and stockholders equity	$ 428,214			$ 304,681		
Interest rate spread			2.69%			2.73%
Net interest income and net interest margin		$ 3,970	3.89%		$ 2,508	3.77%

	Six months ended June 30,					
	2003			2002		
	Average Volume	Interest	Yield/Cost	Average Volume	Interest	Yield/Cost
ASSETS						
Interest-earning assets:						
Federal funds sold	$ 38,981	$ 246	1.26%	$ 14,292	$ 120	1.68%
Securities	7,903	204	5.16	9,359	292	6.24
Loans held for sale	222,557	7,284	6.55	174,809	6,071	6.95
Loans receivable, net	106,908	4,296	8.04	105,170	4,305	8.19
Total interest-earning assets	376,349	12,030	6.39	303,630	10,788	7.11
Non-earning assets	49,815			34,747		
Total assets	$ 426,164			$ 338,377		
LIABILITIES AND STOCKHOLDERS EQUITY						
Interest-bearing liabilities:						
NOW accounts	$ 736	3	0.82	$ 865	4	0.92
Money market accounts	11,306	85	1.50	6,043	74	2.45
Savings deposits	12,854	102	1.59	10,857	152	2.80
Time deposits	48,176	943	3.91	60,660	1,512	4.99
Other borrowings	193,496	3,653	3.78	157,873	2,936	3.72
Total interest-bearing liabilities	266,568	4,786	3.59	236,298	4,678	3.96
Noninterest-bearing liabilities	124,570			70,789		
Stockholders equity	35,026			31,290		
Total liabilities and stockholders equity	$ 426,164			$ 338,377		
Interest rate spread			2.80			3.15
Net interest income and net interest Margin		$ 7,244	3.85%		$ 6,110	4.02%

Net interest income represents the excess of income on interest-earning assets over interest expense on interest bearing liabilities. The principal interest-earning assets are federal funds sold, investment securities and loans receivable. Interest-bearing liabilities primarily consist of notes payable, repurchase agreements, time deposits, interest-bearing checking accounts (NOW accounts), savings, deposits and money market accounts. Funds attracted by these interest-bearing liabilities are invested in interest-earning assets. Accordingly, net interest income depends upon the volume of average interest-earning assets and average interest bearing liabilities and the interest rates earned or paid on them.

Noninterest Income

Noninterest income for the three months ended June 30, 2003 was $175,000, compared to $211,000 for the same period in 2002, a decrease of $36,000 or 21%. The decrease was primarily due to the decrease in net gains on sales of mortgage servicing rights and loans. The gain on sales of mortgage servicing rights and loans decreased from $110,000 for the three months ended June 30, 2002, to $46,000 for the same period of 2003, a decrease of $64,000, or 58%. The decrease was due to a sale of boat loans during the three months ended June 30, 2002. No similar transaction occurred during 2003.

For the six months ended June 30 2002, noninterest income was $361,000 compared to $387,000 for the same period in 2001. The decrease of $26,000, or 7%, was primarily the result of a decrease in gain on sale of mortgage servicing rights and loans of $151,000. The decrease in the gain on sale of mortgage servicing right and loans is due to the sale of several small marine loan packages that occurred during 2002. The decrease in gain on sales of loans was offset by increases in securities gains and service charges on deposit accounts.

Noninterest Expense

Total noninterest expense for the three months ended June 30, 2003 was $1.5 million, compared to $957,000 for the same period in 2002, an increase of approximately $550,000 or 57%. This increase was primarily due to the increase in compensation and employee benefits of $374,000 or 80%. The increase was the result of expenses related to additional support staff hired due to the growth of the bank and the opening of an additional branch location. The additional branch contributed to increases in both occupancy and equipment expense of $71,000 and other noninterest expense of $86,000.

For the six months ended June 30 2003, noninterest expense was $2.8 million compared to $1.9 million for the same period in 2002. The increase of $900,000 or 47% was also attributable to the aforementioned expenses.

Mortgage Banking

The following discussion provides information that relates specifically to Pelican Financial s mortgage banking line of business.

For the three months ended June 30, 2003, Pelican Financial s net income from mortgage banking activities primarily conducted by Washtenaw totaled $3.4 million. For the three months ended June 30, 2002 Washtenaw s comparable net loss was $1.5 million. For the six months ended June 30, 2003, the net income from mortgage banking activities totaled $6.1 million compared to net income of $1.5 million for the same period in 2002. The increase in the net income for both periods was primarily attributable to the increased mortgage loan production.

The volume of loans produced for the three months ended June 30, 2003 totaled $1.3 billion as compared to $492 million for the three months ended June 30, 2002, an increase of approximately $800 million or 163%. For the six months ended June 30, loan production totaled $2.2 billion and $1.2 billion for 2003 and 2002 respectively. This represents an increase of $1.0 billion or 83%. Mortgage interest rates reached the lowest levels in recent history which allowed for large quantities of refinancing.

Noninterest Income

Total noninterest income for the three months ended June 30, 2003 was $17.1 million, compared to $4.6 million for the three months ended June 30, 2002, an increase of $12.5 million or 272%. This increase was primarily due to a 429% increase in the gain on sales of mortgage servicing rights and loans of $12.2 million. For the six months ended June 30, 2003, noninterest income was $30.5 million, compared to $14.7 million for the six months ended June 30, 2002, an increase of $15.8 million or 107%. This increase was primarily due to the increase in the gain on sales of mortgage servicing rights and loans and servicing income.

The increase in gain on sales of mortgage servicing rights and loans for the three and six month periods was primarily due to the increase in new loan originations during the periods ended June 30, 2003. During the three month period ended June 30, 2003 Washtenaw sold $1.2 billion in mortgage loans to the secondary market compared to $516.0 million for the three months ended June 30, 2002. For the six months ended June 30, 2003, Washtenaw sold $2.1 billion in mortgage loans to the secondary market compared $1.3 billion during the preceding year.

Loan Servicing

At June 30, 2003 and 2002, Washtenaw serviced $2.3 billion and $2.4 billion of loans. Washtenaw has retained the servicing on a portion of its new production to offset the normal portfolio runoff that occurs when mortgage interest rates decline. This includes both fixed and variable rate conventional loans as well loans insured by the Government National Mortgage Association. At June 30, 2003 and 2002, with the exception of servicing related to loans held for sale in Washtenaw s loan portfolio and servicing sold but not yet delivered, all loan servicing was serviced for others.

Service fee income, net of amortization, was $257,000 and $452,000 for the three months ended June 30, 2003 and 2002 respectively. For the six months ended June 30, 2003 and 2002, service fee income net of amortization was $795,000 and $793,000, respectively.

Noninterest Expense

Total noninterest expense for the three months ended June 30, 2003 was $14.0 million, compared to $7.8 million for the same period in 2002, an increase of $6.2 million or 79%. This increase was primarily due to an increase in compensation and employee benefits of $4.2 million, the increase in loan servicing right valuation adjustment of $1.0 million and the increase in other noninterest expense of $1.5 million. The increase in employee compensation and benefits was primarily the result of an increase in personnel and overtime as well as a increase in total commissions paid to the existing sales force as a result of the increase in new loan originations. Washtenaw s sales force is comprised primarily of commission based business consultants who are paid a percentage of the loan production from their customers. In addition, the management at Washtenaw receives bonus compensation based on the profitability of the company. During the second quarter of 2002 Washtenaw recorded a loss and as a result their was no bonus compensation expense. The mortgage servicing rights valuation adjustment increased due to the decrease in mortgage interest rates. As mortgage interest rates drop, the value of the mortgage servicing rights asset decreases because of the higher likelihood the loans will be refinanced. The increase in other noninterest expense is primarily the result of additional accruals recorded to increase the liability for potential and actual loan repurchases.

For the six months ended June 30, 2003 and 2002, noninterest expense was $24.8 million and $15.4 million, a difference of $9.4 million between the comparable periods. As previously discussed, compensation and employee benefits increased $4.7 million and the mortgage servicing rights valuation adjustment increased $1.8 million due to the decrease in mortgage interest rates. In addition, other noninterest expense increased by $1.9 million due to the increase expenses related to potential and actual loan repurchases.

During the quarter ended June 30, 2003, Pelican Financial incurred a $300,000 charge related to a severance agreement with the former president of Pelican National. Their was no similar charge in the prior year.

BALANCE SHEET ANALYSIS

The following is a discussion of the consolidated balance sheet of Pelican Financial.

ASSETS

At June 30, 2003, total assets of Pelican Financial equaled $505.8 million as compared to $385.7 million at December 31, 2002, an increase of $120.1 million or 31%. This increase is primarily due to the increase cash and cash equivalents and loans held for sale.

Cash and Cash Equivalents

Cash and cash equivalents were $119.5 million at June 30, 2003 compared to $57.4 million at December 31, 2002. The increase of $62.1 million or 108% was primarily the result of an increase in interest-bearing deposits of $74.9 million. The increase is the result of the increase in the balance of custodial accounts related to the mortgage loan servicing portfolio at Washtenaw. The ending balance in these accounts are at their highest at the end of the month due to loan payoffs that have been received but not yet remitted to the investor. These custodial accounts are maintained at Pelican National.

Investment Securities

Pelican National utilizes investments in securities for liquidity management and as a method of deploying excess funding not utilized for investment in loans. Pelican National has invested primarily in U. S. government and agency securities and U. S. government sponsored agency issued mortgage-backed securities. Pelican National classifies securities as held-to-maturity, available-for-sale, or trading. At June 30, 2003 and at December 31, 2002, all of the investment securities held in Pelican National s investment portfolio were classified as available for sale.

The following table contains information on the carrying value of Pelican National s investment portfolio at the dates indicated. At June 30, 2003, the market value of Pelican National s investment portfolio totaled $6.2 million. During the periods indicated and except as otherwise noted, Pelican National had no securities of a single issuer that exceeded 10% of stockholders equity.

	At June 30, 2003	At December 31, 2002
	(Dollars in thousands)	
U. S. Government agency	$ 4,952	$ 2,517
Mortgage-backed securities	32	43
Federal Reserve Bank and Federal Home Loan Bank Stock	1,230	1,330
Total investment securities	$ 6,214	$ 3,890

Loans Held for Sale

Loans held for sale were $248.2 million at June 30, 2003 compared to $192.5 million at December 31, 2002. This increase of $55.7 million or 29% was caused by the increased refinance activity at Washtenaw resulting from the decrease in mortgage interest rates. Throughout the second quarter, mortgage interest rates were at very low levels relative to recent history.

Loans Receivable

Total loans receivable were $104.3 million at June 30, 2003 compared to $104.5 million at December 31, 2002. The portfolio was relatively the same due to new loan originations being offset by loan prepayments and loan sales.

The following table contains selected data relating to the composition of Pelican Financial s loan portfolio by type of loan at the dates indicated. This table includes mortgage loans held for sale and mortgage loans held for investment. Pelican Financial had no concentration of loans exceeding 10% of total loans that are not otherwise disclosed below.

	June 30, 2002		December 31, 2002	
	Amount	**Percent**	**Amount**	**Percent**
Real estate loans:				
Residential, one to four units	$ 287,848	81.44%	$ 220,882	74.12%
Commercial and industrial real estate				