

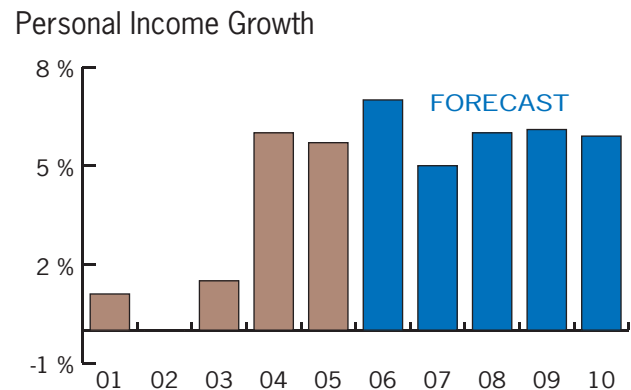
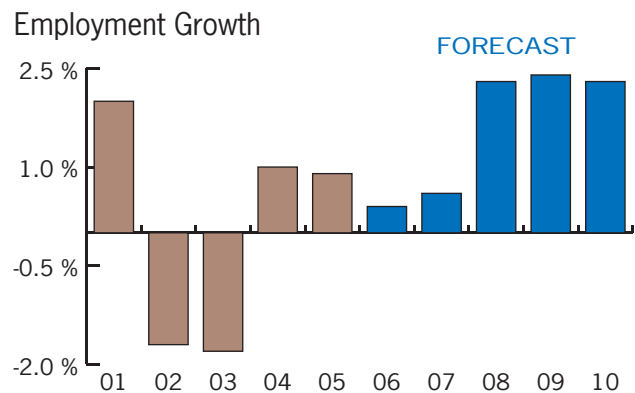
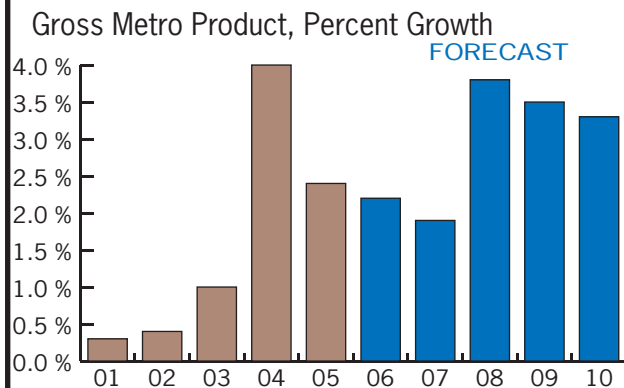


In This Report:

- Sonoma County's outlook for the near term is very modest.** Conditions look better for 2008 and beyond.
- Robust U.S. domestic business investment spending and an acceleration of Bay Area venture capital placements offer some support for a **new cycle of expansion among Sonoma's various technology-producing industries.**
- Given that office and industrial vacancy rates are falling and rents are rising in Marin County, San Francisco, and the East Bay, **businesses seeking space will increasingly turn their attention to Sonoma County.**
- With the total supply of housing increasing and a focus on more affordable multifamily units, **a dent finally may be made in the problem of housing affordability in Sonoma County.**
- Brad Zigler reports on the performance of local stocks.** Brad Zigler is a Santa Rosa-based financial writer and editor, and is the creator of the North Bay Stock Index.

Five-Year Forecast

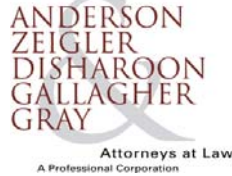
Moody's Economy.com projects that Sonoma County's job creation rate will be in the second quintile of U.S. regions over the next five years.





With Acknowledgment and Appreciation to the Underwriters of the Economic Development Board Foundation Research Initiatives Program:

- Sonoma County Permit & Resources Management ■ Community Development Commission ■
- Sonoma County Health Services ■ Sonoma County Transportation & Public Works ■



SONOMA COUNTY

EMPLOYMENT GROWTH RANK

Best=1 Worst=387

2005-07

306
4th quintile

2005-10

140
2nd quintile

LIFE CYCLE PHASE

Mature/Decline

Best=1 Worst=379

VITALITY

328
5th quintile

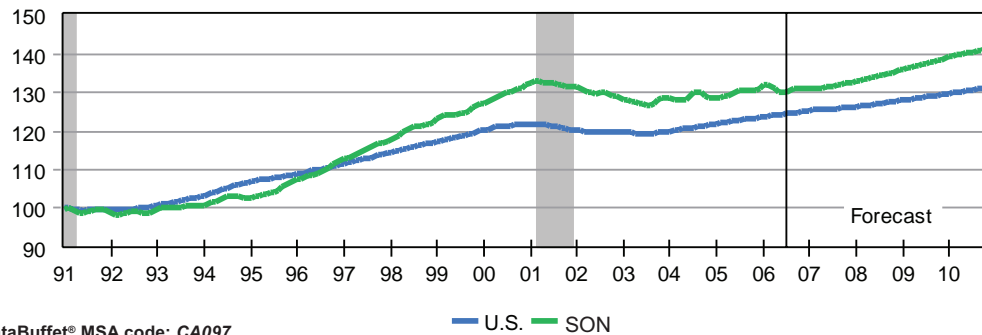
COST OF DOING BUSINESS

U.S.=100% **110%**

COST OF LIVING

U.S.=100% **135%**

Relative Employment Performance (1991=100)



DataBuffet® MSA code: CA097

— U.S. — SON

1999	2000	2001	2002	2003	2004	2005	Indicators	2006	2007	2008	2009	2010
14.4	15.9	16.0	16.0	16.2	16.8	17.2	Gross Metro Product, C\$B	17.6	18.0	18.6	19.3	19.9
9.7	10.5	0.3	0.4	1.0	4.0	2.4	% Change	2.2	1.9	3.8	3.5	3.3
179.3	186.1	189.8	186.6	183.2	185.0	186.6	Total Employment (000)	187.2	188.3	192.7	197.3	201.9
3.6	3.8	2.0	-1.7	-1.8	1.0	0.9	% Change	0.4	0.6	2.3	2.4	2.3
2.7	3.3	3.6	5.1	5.5	4.9	4.4	Unemployment Rate	4.0	4.2	4.0	3.8	3.6
5.8	14.8	1.1	-0.0	1.5	6.0	5.7	Personal Income Growth	7.0	5.0	6.0	6.1	5.9
453.4	460.5	465.6	465.8	467.2	467.9	466.5	Population (000)	467.7	470.2	477.1	485.4	494.0
2,348	2,013	1,717	1,350	1,503	1,342	1,598	Single-Family Permits	1,503	1,701	2,181	2,167	2,140
688	492	866	578	749	587	1,221	Multifamily Permits	998	672	782	783	833
284.3	360.6	408.1	436.2	490.3	574.0	697.0	Existing Home Price (\$Ths)	693.9	647.3	633.5	644.8	666.9
4,420	3,948	9,310	11,399	16,551	11,077	12,100	Mortgage Originations (\$Mil)	11,868	10,087	8,535	8,603	8,982
6.1	5.6	3.7	-1.4	-0.4	-1.0	-3.3	Net Migration (000)	-0.7	0.6	4.8	6.1	6.1
1,627	1,158	1,183	1,223	1,300	1,267	1,997	Personal Bankruptcies	927	1,212	1,191	1,161	1,222

STRENGTHS & WEAKNESSES

STRENGTHS

- Demand is improved for technology-based products made in SON.
- Leisure and business travel is holding steady.
- Household balance sheets are in good shape.

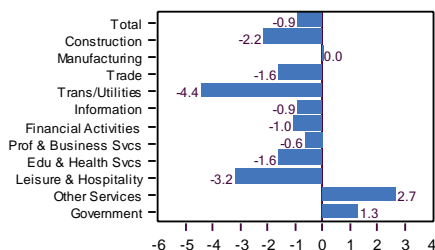
WEAKNESSES

- House prices are still correcting. Affordability remains poor.
- Weak population and labor force growth.
- Stiff international competition for many SON-produced goods.

CURRENT EMPLOYMENT TRENDS

November 2006 Employment Growth

% change year ago, 3 mo. MA



FORECAST RISKS

SHORT TERM ↑ LONG TERM ↓ RISK-ADJUSTED RETURN, '05-10 **0.00%**

UPSIDE

- Business investment spending accelerates sharply as global growth creates renewed business confidence.
- Stronger wage and capital gains in West support leisure travel.

DOWNSIDE

- Labor force constraints cause firms to seek locations closer to clusters of skilled labor.
- Water resources constrain long-term growth potential.

ANALYSIS

Recent Performance. The Sonoma County (SON) economy has stalled. Employment peaked around one year ago and has been flat, at best, ever since. House prices also peaked a year ago and fell moderately through year's end. Demographic trends are weak, with lackluster population growth continuing since 2002. The unemployment rate is stable at well below the U.S. average, but this is due as much to a declining labor force as to any significant vitality in the labor market. The metro area is struggling to find support for growth as industries restructure and its open economy faces significant headwinds from international competition.

Technology. Robust U.S. domestic business investment spending and an acceleration of Bay Area venture capital placements offer some support for a new cycle of expansion among SON's various technology-producing industries. Telecom services, in particular, finally are expanding capacity and are in need of new technology for last-mile network connections. Biomedical technology and industrial instrumentation also see improved investment and demand, creating a shift from layoffs and restructuring to hiring and expansion. Payroll expansions in 2007, modest as they may be, are expected at Agilent Technologies and Medtronic Vascular.

Real estate. The increasing stability of tech-producing industries is beginning to be felt in commercial real estate. Transactions are occurring for long-vacant properties and reinvestment may make them more appealing. Given that office and industrial vacancy rates are falling and rents are rising in Marin County, San Francisco and the East Bay, businesses seeking space will increasingly turn their attention to SON. The startup of commercial air service in March—now that security screening services seem assured—will further enhance the area's prospects.

Despite the weak housing market, residential construction permit issuance remained steady this past year, with multifamily growth offsetting

weakness in single-family construction. With the total supply of housing increasing and a focus on more affordable multifamily units, a dent finally may be made in the problem of housing affordability in SON. Improved housing affordability is key to the economy's long-term growth.

Services. Limited population growth hinders service industries, as evidenced by the imminent closure of Sutter Hospital. Some operations will be taken over by Memorial Hospital, which will expand, but this indicates a shift in market expectations since the economy slowed earlier this decade.

Resources. Increasingly, water resources are seen as a long-term constraint to growth. Supply may not meet demand in coming years, particularly as environmental protection claims a steady or increasing amount of current supply. The ability to build sufficient new housing stock, as well as to support SON's broad base of manufacturing and agricultural industries, will hinge, in part, on water management and development of new sources.

Labor resources are another issue. Some aggressive recruiting of highly skilled and educated talent is planned by firms such as Agilent, although affordable housing remains a problem. At least the widening of Highway 101 may make the commute from outside the county seem less daunting in the near term. SON's labor force has been shrinking for over one year.

Sonoma County's outlook for the near term is very modest, with new investment expected to give the labor market only a slight boost. Conditions look better for 2008 and beyond as the broader U.S. economy accelerates, a weaker dollar creates advantage for SON's export products, and investment and consumer spending accelerate once again. Over the long term, SON is still seen as a slightly above average performer.

Steven G. Cochrane
December 2006

EMPLOYMENT & INDUSTRY

TOP EMPLOYERS

County of Sonoma	4,143
Santa Rosa Junior College	3,231
Kaiser Permanente	2,200
St. Joseph Health System	1,918
Agilent Technologies	1,900
Santa Rosa City School	1,605
Sonoma State University	1,500
City of Santa Rosa	1,366
Medtronic Vascular	1,290
Sutter Medical Center of Santa Rosa	1,024
Safeway, Inc.	960
Kendall-Jackson Wine Estates	920
Home Depot	900
Amy's Kitchen	832
JDS Uniphase Corporation	800
Albertsons, Inc.	780
River Rock Casino	701
Hansel Auto Group	652
Wal-Mart Stores, Inc.	610
AT&T California	600
State Farm Insurance Company	566
Washington Mutual	560
Longs Drug Stores, Inc.	550
Beam Wine Estates	500
Pacific Gas and Electric Company	500

Source: North Bay Business Journal - Sonoma County, Feb 2006

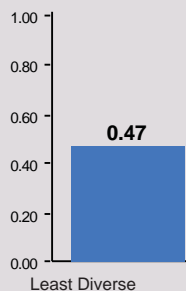
Public

Federal	1,700
State	5,392
Local	23,370

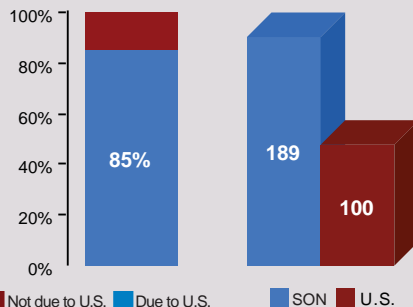
2005

INDUSTRIAL DIVERSITY

Most Diverse (U.S.)



EMPLOYMENT VOLATILITY DUE TO U.S. FLUCTUATIONS RELATIVE TO U.S.



MIGRATION FLOWS

Into Sonoma County	Number of Migrants	Median Income
San Francisco, CA	3,156	37,285
Oakland, CA	1,083	31,654
Sacramento, CA	658	25,697
Los Angeles, CA	552	24,921
Vallejo, CA	454	33,094
San Jose, CA	432	40,624
Napa, CA	405	32,499
San Diego, CA	319	21,704
Santa Ana, CA	226	35,832
Riverside, CA	223	22,482
Total Immigration	15,323	27,265

Into Sonoma County	Number of Migrants	Median Income
San Francisco, CA	2,199	31,234
Sacramento, CA	1,370	30,628
Oakland, CA	829	28,855
Vallejo, CA	570	41,022
Napa, CA	465	31,666
Phoenix, AZ	415	33,057
San Jose, CA	414	39,106
Los Angeles, CA	406	18,789
San Diego, CA	384	20,624
Portland, OR	345	32,551
Total Outmigration	20,241	28,292

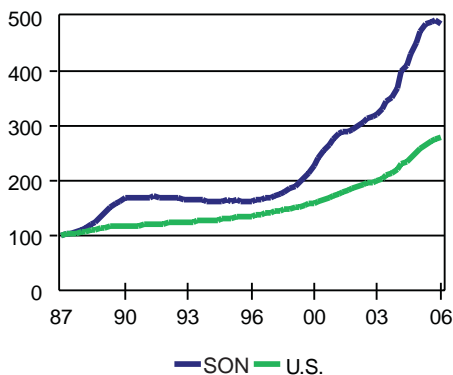
Net Migration	-4,918	-1,027
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COMPARATIVE EMPLOYMENT AND INCOME

Sector	% of Total Employment			Average Annual Earnings		
	SON	CA	US	SON	CA	US
Construction	7.7%	6.1%	5.5%	\$56,988	\$56,402	\$45,244
Manufacturing	12.7%	10.2%	10.7%	\$63,724	\$74,458	\$65,673
Durable	51.7%	64.0%	62.9%	nd	\$82,554	\$67,102
Nondurable	48.3%	36.0%	37.1%	nd	\$60,752	\$63,325
Transportation/Utilities	2.0%	3.3%	3.7%	\$51,115	\$61,459	\$54,428
Wholesale Trade	3.9%	4.6%	4.3%	\$57,560	\$64,240	\$62,643
Retail Trade	12.7%	11.2%	11.4%	\$30,759	\$32,692	\$26,652
Information	2.0%	3.2%	2.3%	\$65,377	\$95,664	\$79,678
Financial Activities	5.2%	6.3%	6.1%	\$42,155	\$53,163	\$51,729
Prof. and Bus. Services	10.9%	14.5%	12.6%	\$39,800	\$53,381	\$49,211
Educ. and Health Services	12.1%	10.7%	13.0%	\$42,315	\$44,032	\$39,829
Leisure and Hosp. Services	11.0%	10.0%	9.6%	\$17,410	\$23,750	\$19,370
Other Services	3.3%	3.5%	4.0%	\$25,215	\$24,070	\$22,940
Government	16.3%	16.3%	16.3%	\$51,929	\$61,048	\$53,033

Sources: Percent of total employment - Moody's Economy.com & BLS, 2005; Average annual earnings - BEA, 2004

HOUSE PRICES



Source: OFHEO, 1987Q1= 100, NSA

CREDIT QUALITY

MOODY'S RATING

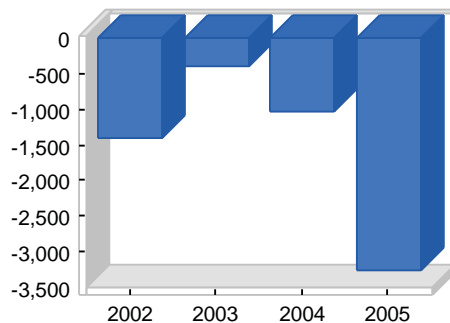
County **Aa2**

LEADING INDUSTRIES

NAICS Industry	Employees (000)
GVSL State & Local Government	28.8
FR Farms	8.7
7221 Full-Service Restaurants	7.5
3121 Beverage Manufacturing	6.3
6221 General Medical and Surgical Hospitals	5.8
7222 Limited-Service Eating Places	5.4
4451 Grocery Stores	5.2
2360 Construction of Buildings	4.0
7211 Traveler Accommodation	3.3
5617 Services to Buildings and Dwellings	3.3
5613 Employment Services	3.0
2383 Building Finishing Contractors	2.9
2382 Building Equipment Contractors	2.7
4521 Department Stores	2.6
6211 Offices of Physicians	2.5
High-tech employment	10.1
As % of total employment	5.0

Sources: BLS, Moody's Economy.com, 2005

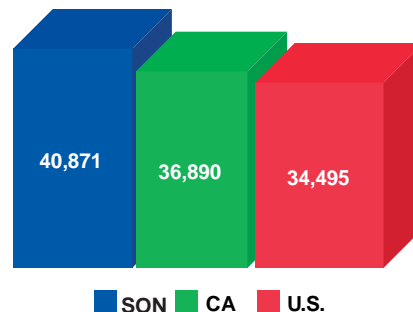
Net Migration, SON



	2002	2003	2004	2005
Domestic	-4,088	-2,927	-3,351	-5,380
Foreign	2,680	2,540	2,323	2,120
Total	-1,408	-387	-1,028	-3,260

Sources: IRS (top), 2005; Census Bureau 2005

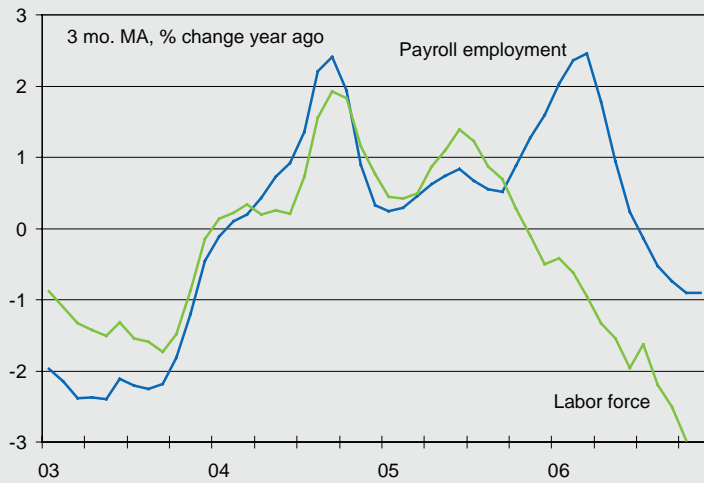
PER CAPITA INCOME



Source: Bureau of Economic Analysis, 2004

Sonoma County

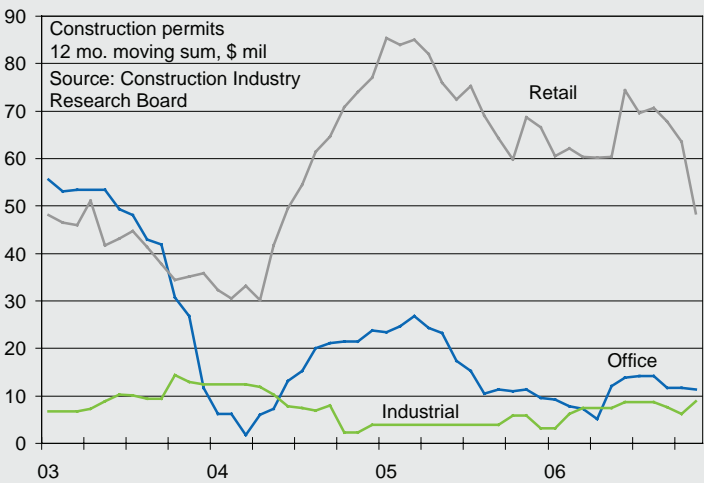
Employment Is Down and Labor Force Is Shrinking



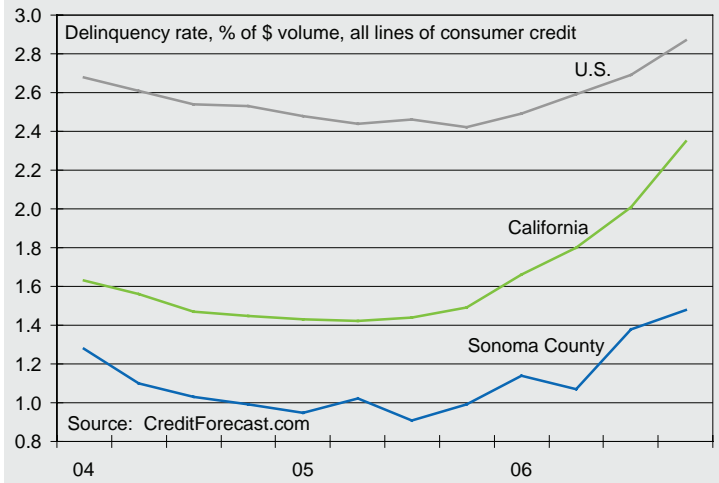
Shrinking Labor Force Keeps Jobless Rate Low



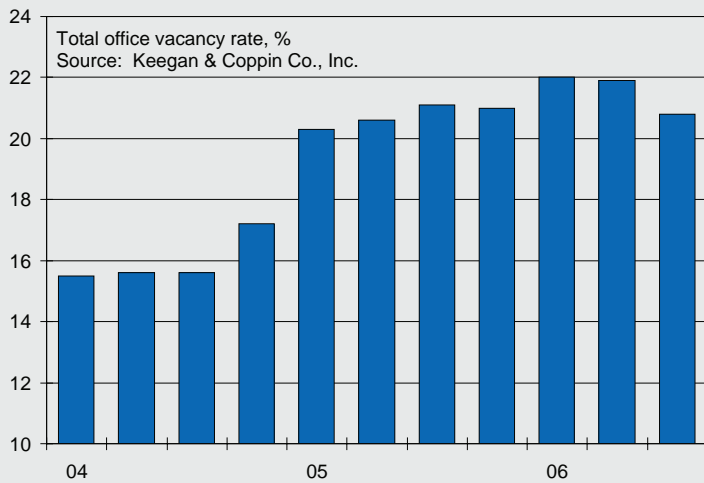
Lackluster Office/Industrial Construction; Retail Is Well Supplied



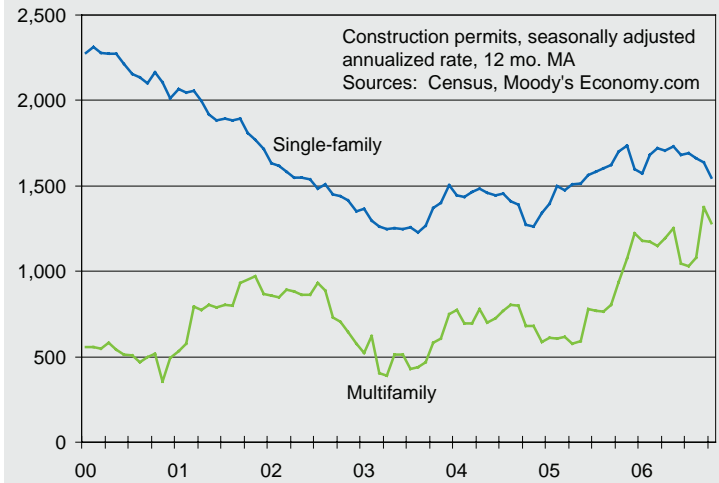
Modest Deterioration of Household Credit Quality



Some Improvement in Office Market



Multifamily Bolsters Residential Construction



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SONOMA COUNTY STOCKS: BLUE CHIP BLUES

*This report was prepared by **Brad Zigler**, a Santa Rosa-based financial writer and editor. Mr. Zigler's work has appeared in the Journal of Indexes, Institutional Investor, Financial Planning, Financial Advisor, Mutual Funds, Futures, Registered Rep. and the North Bay Business Journal, among other publications. Previously the head of marketing, research and education at the Pacific Exchange and Barclays Global Investors, Mr. Zigler is the creator of the North Bay Stock Index and a commentator on National Public Radio affiliate KRCB. He holds investments in some or all of the Sonoma County-based securities mentioned in this report.*

RED VS. BLUE

The Dow Jones Industrial Average's 16.3 percent gain in 2006 heralded a banner year for blue chip stocks. Smaller local stocks, as measured by the North Bay Stock Index (NBSI), pulled ahead only 10.6 percent for the year.

Volatility in the local stock set is still a shade lower than that of larger stocks, but not by a wide enough margin to tip the reward-to-risk advantage to the North Bay. The Sharpe ratio -- a measure of risk-adjusted returns favored by financial professionals -- for North Bay stocks was .58 in 2006. Contemporaneously, the Dow's Sharpe ratio was 1.08 (a Sharpe ratio of 1.00 is indicative of an investment offering a respectable return for the amount of risk undertaken).

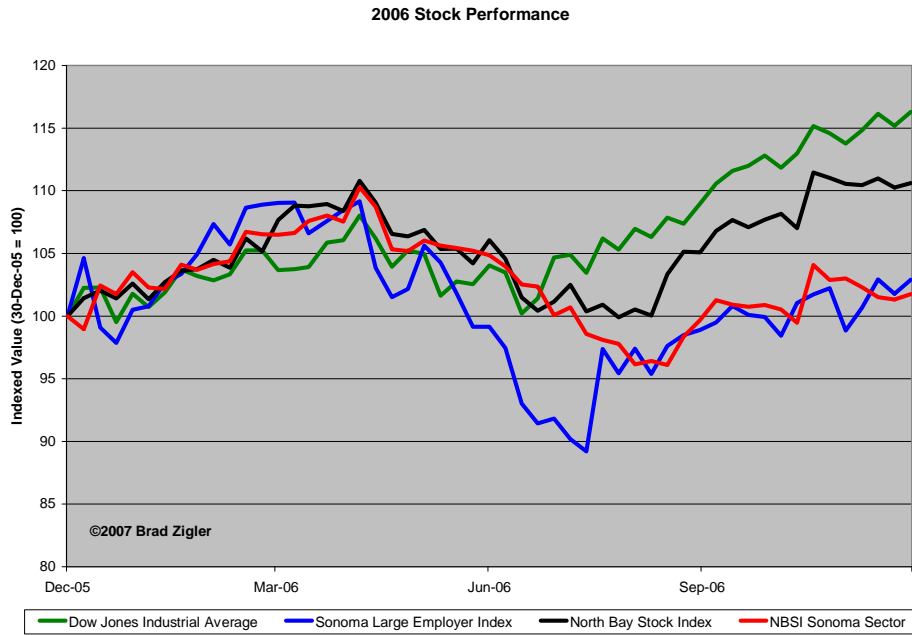
Blue chips' outsized performance shows in even greater relief when compared to the track record of Sonoma County-headquartered issues. NBSI's nine-stock Sonoma Sector gained a paltry 1.8 percent in 2006. The sector's -.33 Sharpe ratio belies the fact that some local issues posted substantial gains for the year (see below).

Figure 1 illustrates the year-to-date performance of local stocks compared to the Dow ("Dow Jones Industrial Average" in **green**). The composite performance of nine Sonoma County-headquartered companies ("NBSI Sonoma Sector" in **red**) are put up against that of Sonoma County's 15 largest publicly traded employers¹ ("Sonoma Large-Employer Index" in **blue**) with headquarters outside of Sonoma County. The Sonoma Large Employer Index is employment-weighted: Each stock's heft in the benchmark is determined as the ratio of Sonoma County jobs to the company's total employment base. This weighting can be thought of as an approximation of Sonoma County employees' contribution to each stock's performance. The North Bay Stock Index ("North Bay Stock Index" in **black**) is a price-weighted index of 29 public companies headquartered in the counties of Marin, Napa or Sonoma.

Stock performance across all sectors was fairly congruent in the first half of 2006. By June, however, Sonoma County stock performance began to flag. Employees of companies based outside of Sonoma County represented a return of **2.9 percent** by year's end. The returns of Sonoma County-based stocks, at **1.8 percent**, were well-correlated (69 percent). The Dow's **16.3 percent** return was equally well-correlated (71 percent) with the price action producing the North Bay Stock Index's **10.8 percent** gain.

¹ These include: Agilent Technologies, Supervalu, AT&T, Cisco Systems, Federated Department Stores, Home Depot, JDS Uniphase, Longs Drug Stores, Medtronic, New York Times Co., PG&E, Safeway, Tellabs, Washington Mutual and Wal-Mart Stores.

Figure 1



The median Sonoma County-based stock gained nearly 25 percent in 2006 as winners outpaced losers by a 2-to-1 margin. Negative Sharpe ratios for three issues: Sonoma College (SNMA), Summit State Bank (SSBI) and Exchange Bank-Santa Rosa (EXSR) indicate that, for 2006 at least, a risk-free security such as a Treasury bill would have been a better parking place for investors' money. Figure 2 provides details on each locally headquartered stock.

Figure 2

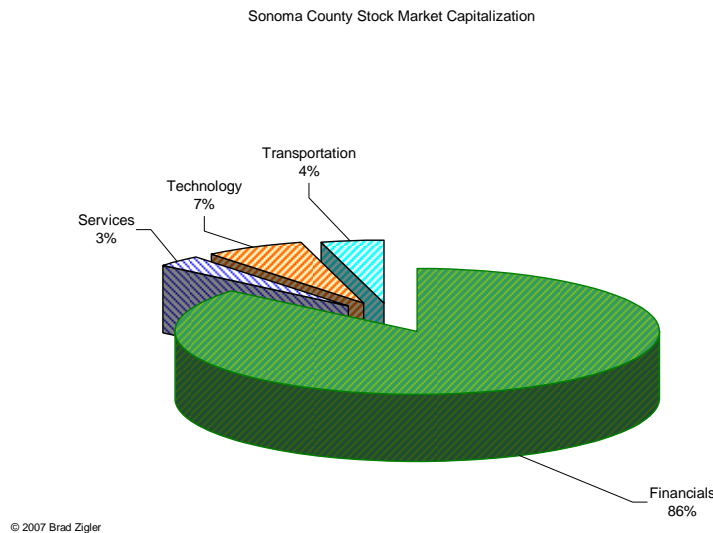
**NBSI Sonoma Sector Stocks
2006 Performance**

Company	Industry	Stock Price 29-Dec-06	2006 Gain/Loss	Sharpe Ratio	Market Cap (\$mm)
ZAP (ZAAP)	Recreational & Other Vehicles	\$0.79	205.4%	1.21	34.8
Sonoma Valley Bancorp (SBNK)	Regional Bank	\$28.00	30.8%	1.11	65.6
Northern Empire Bancshares (NREB)	Regional Bank	\$29.54	24.9%	0.77	312.6
Sonoma West Holdings, Inc. (SWHI)	Rental/Leasing	\$14.25	41.8%	0.73	29.2
Atlantic Pacific Bank (APFB)	Regional Bank	\$13.83	34.9%	0.73	18.5
Burst.com (BRST)	Software/Programming	\$1.15	7.5%	0.04	53.9
Sonoma College (SNMA)	Education/Training	\$0.23	-77.9%	-0.42	6.8
Summit State Bank (SSBI)	Regional Bank	\$12.76	-14.9%	-1.30	61.2
Exchange Bank-Santa Rosa (EXSR)	Regional Bank	\$132.25	-0.5%	-1.32	224.5
Median		\$14.04	24.9%	0.73	53.9

BREAKDOWN BY INDUSTRY

The Sonoma County market mix remains heavily skewed in favor of financial issues, owing largely to the hefty price of Exchange Bank's stock. Nearly 93 percent of the Sonoma Sector's price weight represents regional bank stocks. Regional banks contribute 86 percent of the local stock set's total market capitalization.

Figure 3



Transportation

This one-stock sector earned a 1.21 Sharpe in 2006 for its outsized gain. Despite the smallness of its representative stock, the transportation industry represents 6.9 percent of the employment among Sonoma County public companies.

- ZAP (ZAAP) - ZAP added a letter to its ticker as its stock listing dropped back to the Over-the-Counter Bulletin Board from the NYSE Arca Exchange (the former Pacific Exchange). Still, ZAP provides the best reward-to-risk ratio of any Sonoma County stock. The stock's price is very volatile.

Services

Accounting for 5.6 percent of employment among Sonoma County's tradeable companies, the services industry's 24.5 percent gain earned a Sharpe ratio of 0.51 in 2006.

- SonomaWest Holdings, Inc. (SWHI) - The engine of the Sonoma services industry, SonomaWest's prospects seemed buoyant after a management-led buyout was shelved earlier in the year.

- Sonoma College, Inc (SNMA) - Still without a dedicated market maker, Sonoma College's stock slid at one point to only 12 cents per share. Dilution pressure was kept on the share price late in the year in the wake of a half-million dollar private financing deal.

Financials

Financial institutions account for 85.6 percent of the jobs among Sonoma County's listed companies. As a group, the five financial institutions earned a 20.7 percent return for the year. The local bank industry's Sharpe ratio stands at 1.27.

- Sonoma Valley Bancorp (SBNK) - The county's smallest bank earned its 30.8 percent return before dividends. Loan growth, higher operating efficiencies, and increases in non-interest income contributed to record profits. Further bounce in the share price came when a stock buyback program was announced.
- Northern Empire Bancshares (NREB) - The parent of Sonoma National Bank is set to be acquired by Washington's Sterling Financial later in 2007 in a cash-and-stock deal valued at \$335 million. News of the acquisition in September set the then-plodding share price on an upward trajectory.
- Atlantic Pacific Bank (APFB) - Shares of Sonoma County's newest business bank found good demand in the open market after the mid-year initial public offer at \$10. The share price barely paused long enough to look back.
- Summit State Bank (SSBI) - The public offering price of \$15 has been the stock's high-water mark since July. A pinch on fee income contributed to a 10.8 percent decline in third quarter earnings.
- Exchange Bank-Santa Rosa (EXSR) - The share price of Sonoma County's largest bank was rarely above water in 2006. Mounting interest expense continues to squeeze the bank's margins.

Technology

The ranks of Sonoma County tech companies dwindled as Tegal Corporation (TGAL) moved its headquarters to Silicon Valley in the summer of 2006. Only Burst.com, with its 0.3 percent employment share, remains to represent the industry.

- Burst.com (BRST) - Aside from initiating a patent infringement suit against Apple, Inc., the Santa Rosa software maker's biggest financial development of 2006 was its petition for a nearly \$1 million tax refund.

DIVIDENDS

The median annual dividend yield on Sonoma Sector stocks stands at 2.82 percent as of December 29, 2006. Dividends were contributed by three regional bank stocks – Exchange Bank, Sonoma Valley Bancorp and Summit State Bank. By comparison, the annual yield on three-month Treasury bills averaged 4.71 percent in 2006.

LIQUIDITY

Sonoma County stocks, with a median \$53.9 market value, are micro-cap issues. Still, some are quite liquid. The median liquidity index, representing the size of a transaction necessary to move an issue's price by one percentage point, tops \$69,000 largely because of Northern Empire Bancshares (NREB) being in play late in the year. With an index over \$2 million, or 69,804 shares, Northern Empire is Sonoma County's most liquid issue. The least liquid, with a \$5,624 (479 share) reading, is SonomaWest Holdings, Inc. (SWHI).

Figure 4

NBSI Sonoma Sector Stocks 2006 Fundamentals

Company	Average Daily Volume	Shares Out (mm)	Price/ Earnings	Price/ Book	Dividend Yield	Liquidity Index	
						\$	Shares
ZAP (ZAAP)	170,479	36.99		7.0		\$69,640	79,136
Sonoma Valley Bancorp (SBNK)	463	2.28	17.4	2.6	2.14%	\$32,582	1,164
Northern Empire Bancshares (NREB)	28,705	10.96	17.7	2.6		\$2,060,004	69,804
Sonoma West Holdings, Inc. (SWHI)	2,866	1.16	18.6	3.0		\$5,624	479
Atlantic Pacific Bank (APFB)	1,387	2.75					
Burst.com (BRST)	23,460	39.95					
Sonoma College (SNMA)	4,473	68.14					
Summit State Bank (SSBI)	9,900	4.76	6.9	8.1	2.82%		
Exchange Bank-Santa Rosa (EXSR)	400	1.71	11.5	1.9	3.02%	\$70,695	535
Median	4,473	4.76	17.4	2.8	2.82%	\$69,640	1,164

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INSIDER TRANSACTIONS

Three companies reported significant insider trading activity in 2006: ZAP (ZAAP), Northern Empire Bancshares (NREB) and Sonoma Valley Bancorp (SBNK). Officers and directors of ZAP were most active with respect to their company's stock. More than \$5.7 million ZAAP shares were sold, 27 times the value of ZAAP shares bought during 2006. ZAAP's sell ratio, however, was bested by NREB. Net sales of nearly \$845,000 put NREB's sellers in command by a multiple of 35.

SBNK insider dealings favored buyers in 2006. Nearly \$1.7 million SBNK shares were bought by officers and directors, putting the holding company's sell ratio at only .73.

NEW ENTRIES

Oculus Innovative Science (OCLS), a Petaluma healthcare company, had intended to float an initial public offering of some \$40 million by the end of 2006. Shares were originally targeted for the \$12 to \$14 range, but softness in indications of interest likely forced the company to rejigger its offer \$10 million downward. Now 3.5 million shares of OCLS are expected to be priced between \$8 and \$10.

***Note:** The foregoing information and discussion on Sonoma County stock performance was obtained by the County of Sonoma from Mr. Zigler and is presented for the convenience of the reader. Any opinions expressed are solely those of Mr. Zigler and not of the County of Sonoma. The information provided here is not intended to replace other stock performance reports, investment publications, and the like and should not be used as the sole source for investment decisions. You should perform your own research and evaluation before making any investment decisions. Although the information presented here is believed to be accurate, the County of Sonoma does not guarantee its accuracy and assumes no liability for investment results that may occur following your use of the information provided herein.*