



July 29, 2010

Dear Friends,

Attached are the financial results for Merchants Bancorp, the financial holding company for MBank, for the second quarter ending June 30, 2010. The results show a continuing trend of improvement in nonperforming assets. The loss for the quarter was \$1.0 million, compared to a \$1.2 million loss in the 1st quarter of 2010 and compared to a \$4.1 million loss in the 2nd quarter of 2009. Nonperforming assets have dropped approximately 20% from \$44.7 million at June 30, 2009 to \$36.0 million at June 30, 2010. Losses related to the workout of troubled assets are the lion's share of the overall losses at MBank. These losses are within expectations and notably dropping in volume with the decrease in the overall level of nonperforming assets.

The drop in real estate prices in 2009 impacted many of our customers and ultimately impacted MBank. Those real estate prices appear to have stabilized and we see the corresponding trends of stabilization within our loan portfolio. However, the negative impact of losses related to troubled loans have significantly depleted MBank's capital. Our capital must be replenished and management and the Board continue to actively explore all options to restore the bank's capital. While the most likely scenarios would be dilutive, the Board is hopeful that current shareholders are willing to participate in the recapitalization process to both provide an investment opportunity as well as protect the value of existing shares. We would welcome any comments, suggestions, or questions you may have. Please contact Jef Baker, MBank Chief Financial Officer, at 503-674-3401.

As noted in previous letters the Board and management have and continue to make tough, but necessary decisions to reduce overhead and expenses. These kinds of decisions are the same many of our community business owners make as they position their companies for success in a challenging economy. Those choices have included deleveraging (shrinking) the size of the bank, reducing staff, and significantly cutting discretionary spending. During this period of planned deleveraging we have taken the opportunity to significantly reduce reliance on expensive brokered deposits and borrowings as a source of funding. We also continue to maintain strong liquidity reserves.

Despite all the distractions in this economy we continue to focus on our customers. We have a knowledgeable and experienced team of employees that is committed to providing the best service possible. We work diligently to protect our customers and ensure all of their deposits are adequately insured. We continue to seek new deposit customers and are aggressively looking to make loans in our communities. As a shareholder, you have a unique opportunity to protect your investment by both building your banking relationship with MBank as well as referring your friends, family and associates.

We understand we have all felt the impact of this rough economic cycle. Many of us have been through these cycles and can take comfort in knowing for every downturn there is an upturn. The downturns teach us how valuable it is to work together to get through. At MBank we are encouraging everyone to bank local and shop local. Money spent locally stays in our local economy twice as long as if spent in out of state banks and big box stores. Local people helping local people. That's MBanking.

We look forward to our return to financial strength as we seek to recapitalize, grow, and provide shareholder value through ongoing profitability. We are proud to be the only Gresham-based community bank and we are blessed with supportive communities, customers and shareholders. Thank you for your continued trust and giving MBank the opportunity to serve you.

Sincerely,

Stanley C. Morris
Chairman of the Board

H. Rex Brittle
President/CEO

Balance Sheet (Unaudited)

	As of June 30, 2010	As of June 30, 2009
Assets		
Cash and due from banks	\$14,713,385	\$32,272,758
Available-for-sale securities, at est. fair value	38,386,809	16,616,125
Federal Home Loan Bank stock	2,041,500	2,041,500
Loans, net of allowance for loan losses and unearned income	143,591,207	212,848,890
Bank premises and equipment, net depreciation and amortization	7,109,933	7,731,380
Other real estate owned	4,813,936	5,245,311
Goodwill	-	1,159,019
Cash surrender value of bank-owned life ins.	6,201,115	5,933,315
Accrued interest and other assets	<u>3,333,936</u>	<u>7,467,860</u>
TOTAL ASSETS	<u>\$220,191,821</u>	<u>\$291,316,158</u>
Liabilities and Stockholders' Equity		
Demand deposit and NOW accounts	\$32,380,850	\$34,598,911
Money market and savings accounts	31,433,994	40,218,702
Time deposits	<u>134,627,532</u>	<u>156,231,030</u>
Total deposits	198,442,376	231,048,643
Repurchase agreements	1,170,519	4,826,256
Federal Home Loan Bank borrowings	8,000,000	30,500,000
Junior subordinated debentures	5,155,000	5,155,000
Accrued interest payable and other liabilities	<u>1,456,472</u>	<u>1,310,982</u>
Total liabilities	214,224,367	272,840,881
Minority Interest in Fenton, Wangler Financial	33,938	34,775
Stockholders' Equity		
Common stock (4,380,032 shares at 06/30/10)	4,380,032	4,380,032
Additional paid-in capital	18,847,800	18,825,734
Retained (deficit) earnings	(18,119,073)	(5,006,144)
Accumulated other comprehensive income	<u>824,757</u>	<u>240,880</u>
Total stockholders' equity	<u>5,933,516</u>	<u>18,440,502</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$220,191,821</u>	<u>\$291,316,158</u>