

LAKELAND FINANCIAL CORP
Form 10-Q
May 07, 2008

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2008

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

LAKELAND FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Indiana
(State or other jurisdiction
Of incorporation)

0-11487
(Commission File Number)

35-1559596
(IRS Employer
Identification No.)

202 East Center Street, P.O. Box 1387, Warsaw, Indiana 46581-1387

(Address of principal executive offices)(Zip Code)

(574) 267-6144

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 [X] NO []

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Indicate by check mark whether registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Act). (check one):

Large accelerated filer [] Accelerated filer [X] Non-accelerated filer [] (do not check if a smaller reporting company) Smaller reporting company []

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES [] NO [X]

Number of shares of common stock outstanding at April 30, 2008: 12,230,973

LAKELAND FINANCIAL CORPORATION

Form 10-Q Quarterly Report

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PART 1**LAKELAND FINANCIAL CORPORATION****ITEM 1 FINANCIAL STATEMENTS****LAKELAND FINANCIAL CORPORATION****CONSOLIDATED BALANCE SHEETS**

As of March 31, 2008 and December 31, 2007

(in thousands except for share data)

(Page 1 of 2)

	March 31, 2008 (Unaudited)	December 31, 2007
ASSETS		
Cash and due from banks	\$ 170,651	\$ 56,278
Short-term investments	8,448	11,413
Total cash and cash equivalents	179,099	67,691
Securities available for sale (carried at fair value)	340,602	327,757
Real estate mortgage loans held for sale	974	537
Loans, net of allowance for loan losses of \$16,758 and \$15,801	1,585,658	1,507,919
Land, premises and equipment, net	27,314	27,525
Bank owned life insurance	33,166	21,543
Accrued income receivable	8,750	9,126
Goodwill	4,970	4,970
Other intangible assets	568	619
Other assets	23,894	21,446
Total assets	\$ 2,204,995	\$ 1,989,133

(continued)

LAKELAND FINANCIAL CORPORATION

CONSOLIDATED BALANCE SHEETS

As of March 31, 2008 and December 31, 2007

(in thousands except for share data)

(Page 2 of 2)

	March 31, 2008 (Unaudited)	December 31, 2007
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Noninterest bearing deposits	\$ 342,432	\$ 255,348
Interest bearing deposits	1,234,166	1,223,570
Total deposits	1,576,598	1,478,918
Short-term borrowings		
Federal funds purchased	99,500	70,010
Securities sold under agreements to repurchase	164,348	154,913
U.S. Treasury demand notes	1,317	1,242
Other short-term borrowings	163,700	90,000
Total short-term borrowings	428,865	316,165
Accrued expenses payable	16,276	15,497
Other liabilities	1,239	1,311
Long-term borrowings	43	44
Subordinated debentures	30,928	30,928
Total liabilities	2,053,949	1,842,863
STOCKHOLDERS' EQUITY		
Common stock: 180,000,000 shares authorized, no par value		
12,230,973 shares issued and 12,130,676 outstanding as of March 31, 2008	1,453	1,453
12,207,723 shares issued and 12,111,703 outstanding as of December 31, 2007	18,557	18,078
Additional paid-in capital	132,621	129,090
Retained earnings	(158)	(1,010)
Accumulated other comprehensive loss	(1,427)	(1,341)
Treasury stock, at cost (2008 - 100,297 shares, 2007 - 96,020 shares)	151,046	146,270
Total stockholders' equity	\$ 2,204,995	\$ 1,989,133
Total liabilities and stockholders' equity		

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

LAKELAND FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

For the Three Months Ended March 31, 2008 and 2007

(in thousands except for share and per share data)

(Unaudited)

(Page 1 of 2)

	Three Months Ended March 31,	
	2008	2007
NET INTEREST INCOME		
Interest and fees on loans		
Taxable	\$ 25,475	\$ 24,720
Tax exempt	32	50
Interest and dividends on securities		
Taxable	3,380	2,678
Tax exempt	614	602
Interest on short-term investments	91	208
Total interest income	29,592	28,258
Interest on deposits	12,047	13,098
Interest on borrowings		
Short-term	2,424	1,430
Long-term	615	632
Total interest expense	15,086	15,160
NET INTEREST INCOME	14,506	13,098
Provision for loan losses	1,153	641
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	13,353	12,457
NONINTEREST INCOME		
Wealth advisory fees	809	689
Investment brokerage fees	283	243
Service charges on deposit accounts	1,769	1,632
Loan, insurance and service fees	655	581
Merchant card fee income	810	764
Other income	458	493
Net gains on sales of real estate mortgage loans held for sale	315	165
Net securities gains (losses)	28	36
Gain on redemption of Visa shares	642	0
Total noninterest income	5,769	4,603

(continued)

LAKELAND FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

For the Three Months Ended March 31, 2008 and 2007

(in thousands except for share and per share data)

(Unaudited)

(Page 2 of 2)

	Three Months Ended March 31,	
	2008	2007
NONINTEREST EXPENSE		
Salaries and employee benefits	6,253	5,855
Net occupancy expense	796	674
Equipment costs	441	445
Data processing fees and supplies	840	701
Credit card interchange	535	489
Other expense	2,517	2,106
Total noninterest expense	11,382	10,270
INCOME BEFORE INCOME TAX EXPENSE	7,740	6,790
Income tax expense	2,499	2,032
NET INCOME	\$ 5,241	\$ 4,758
Other comprehensive income, net of tax:		
Amortization of net actuarial loss on pension and SERP plans	14	0
Unrealized gain on securities available for sale	838	600
TOTAL COMPREHENSIVE INCOME	\$ 6,093	\$ 5,358
BASIC WEIGHTED AVERAGE COMMON SHARES	12,215,561	12,159,768
BASIC EARNINGS PER COMMON SHARE	\$ 0.43	\$ 0.39
DILUTED WEIGHTED AVERAGE COMMON SHARES	12,424,643	12,419,975
DILUTED EARNINGS PER COMMON SHARE	\$ 0.42	\$ 0.38

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

LAKELAND FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three Months Ended March 31, 2008 and 2007

(in thousands)

(Unaudited)

(Page 1 of 2)

	2008	2007
Cash flows from operating activities:		
Net income	\$ 5,241	\$ 4,758
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	449	410
Provision for loan losses	1,153	641
Write down of other real estate owned	105	0
Amortization of intangible assets	51	51
Amortization of loan servicing rights	107	108
Net change in loan servicing rights valuation allowance	(6)	(18)
Loans originated for sale	(16,691)	(11,435)
Net gain on sales of loans	(315)	(165)
Proceeds from sale of loans	16,427	12,595
Net gain on redemption of Visa shares	(642)	0
Net (gain) loss on sale of premises and equipment	0	(4)
Net gain on sales of securities available for sale	(28)	(36)
Net securities amortization	54	239
Stock compensation expense	45	45
Earnings on life insurance	(218)	(171)
Tax benefit of stock option exercises	(87)	(290)
Net change:		
Accrued income receivable	376	421
Accrued expenses payable	794	2,572
Other assets	(2,238)	189
Other liabilities	(75)	101
Total adjustments	(739)	5,253
Net cash from operating activities	4,502	10,011
Cash flows from investing activities:		
Proceeds from sale of securities available for sale	28	13,530
Proceeds from maturities, calls and principal paydowns of securities available for sale	17,966	8,798
Purchases of securities available for sale	(29,484)	(23,668)
Purchase of life insurance	(11,405)	(112)
Net increase in total loans	(78,892)	(24,435)
Proceeds from sales of land, premises and equipment	58	60
Purchases of land, premises and equipment	(296)	(699)
Net cash from investing activities	(102,025)	(26,526)

(Continued)

LAKELAND FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three Months Ended March 31, 2008 and 2007

(in thousands)

(Unaudited)

(Page 2 of 2)

	2008	2007
Cash flows from financing activities:		
Net increase in total deposits	97,680	22,237
Net increase (decrease) in short-term borrowings	112,700	(47,999)
Payments on long-term borrowings	(1)	(1)
Dividends paid	(1,710)	(1,516)
Proceeds from stock option exercise	348	870
Purchase of treasury stock	(86)	(113)
Net cash from financing activities	208,931	(26,522)
Net change in cash and cash equivalents	111,408	(43,037)
Cash and cash equivalents at beginning of the period	67,691	119,699
Cash and cash equivalents at end of the period	\$ 179,099	\$ 76,662
Cash paid during the period for:		
Interest	\$ 15,670	\$ 13,174

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

LAKELAND FINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2008

(In thousands)

(Unaudited)

NOTE 1. BASIS OF PRESENTATION

This report is filed for Lakeland Financial Corporation (the Company) and its wholly-owned subsidiary, Lake City Bank (the Bank). All significant inter-company balances and transactions have been eliminated in consolidation. Also included is the Bank's wholly-owned subsidiary, LCB Investments II, Inc. (LCB Investments). LCB Investments also owns LCB Funding, Inc. (LCB Funding), a real estate investment trust.

The unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with instructions for Form 10-Q. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (all of which are normal and recurring in nature) considered necessary for a fair presentation have been included. Operating results for the three-month period ending March 31, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008. The 2007 Lakeland Financial Corporation Annual Report on Form 10-K should be read in conjunction with these statements.

NOTE 2. EARNINGS PER SHARE

Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options. Stock options for 29,000 and 3,000 shares as of March 31, 2008 and March 31, 2007, respectively, were not considered in computing diluted earnings per common share because they were antidilutive. Earnings and dividends per share are restated for all stock splits and dividends through the date of issuance of the financial statements. The common shares included in Treasury Stock for 2008 and 2007 reflect the acquisition of 100,297 and 96,020 shares, respectively, of Lakeland Financial Corporation common stock that have been purchased under a directors' deferred compensation plan. Because these shares are held in trust for the participants, they are treated as outstanding when computing the weighted-average common shares outstanding for the calculation of both basic and diluted earnings per share.

NOTE 3. LOANS

	March 31, 2008	December 31, 2007
Commercial and industrial loans	\$ 1,047,367	\$ 968,336
Commercial real estate - multifamily loans	16,660	16,839
Commercial real estate construction loans	83,378	84,498
Agri-business and agricultural loans	180,344	170,921
Residential real estate mortgage loans	115,953	124,107
Home equity loans	108,558	108,429
Installment loans and other consumer loans	50,250	50,516
Subtotal	1,602,510	1,523,646
Less: Allowance for loan losses	(16,758)	(15,801)
Net deferred loan (fees)/costs	(94)	74
Loans, net	\$ 1,585,658	\$ 1,507,919
Impaired loans	\$ 6,591	\$ 6,748
Non-performing loans	\$ 7,360	\$ 7,448
Allowance for loan losses to total loans	1.05%	1.04%

Changes in the allowance for loan losses are summarized as follows:

	Three Months Ended	
	March 31, 2008	2007
Balance at beginning of period	\$ 15,801	\$ 14,463
Provision for loan losses	1,153	641
Charge-offs	(262)	(458)
Recoveries	66	112
Net loans charged-off	(196)	(346)
Balance at end of period	\$ 16,758	\$ 14,758

NOTE 4. SECURITIES

The fair values of securities available for sale were as follows:

	March 31, 2008	December 31, 2007
U.S. Treasury securities	\$ 1,027	\$ 1,206
U.S. Government agencies	15,804	18,555
Mortgage-backed securities	268,221	250,495
State and municipal securities	55,550	57,501
Total	\$ 340,602	\$ 327,757

As of March 31, 2008, net unrealized gains on the total securities available for sale portfolio totaled \$1.6 million, which included gross unrealized losses of \$3.3 million. As of December 31, 2007, net unrealized gains on the total securities available for sale portfolio totaled \$246,000. Management considers the unrealized gains to be market driven and no gain is expected to be realized unless the securities are sold. All of the securities are backed by the U.S. Government, government agencies, government sponsored agencies or are A rated or better, except for certain non-local municipal securities. None of the securities have call provisions (with the exception of the municipal securities) and payments as originally agreed are being received. There are no concerns of credit losses and there is nothing to indicate that full principal will not be received. The Company does not have a history of actively trading securities, but keeps the securities available for sale should liquidity or other needs develop that would warrant the sale of securities. While these securities are held in the available for sale portfolio, the current intent and ability is to hold them until maturity.

NOTE 5. EMPLOYEE BENEFIT PLANS

Components of Net Periodic Benefit Cost

	Three Months Ended March 31, Pension Benefits		SERP Benefits	
	2008	2007	2008	2007
Interest cost	\$ 35	\$ 35	\$ 18	\$ 19
Expected return on plan assets	(48)	(43)	(25)	(23)
Recognized net actuarial loss	12	11	13	14
Net pension expense	\$ (1)	\$ 3	\$ 6	\$ 10

The Company previously disclosed in its financial statements for the year ended December 31, 2007 that it expected to contribute \$0 to its pension plan and \$13,000 to its SERP plan in 2008. As of March 31, 2008, \$0 had been contributed to the pension plan and \$0 to the SERP plan. The Company presently anticipates contributing \$13,000 to its SERP plan in 2008.

NOTE 6. NEW ACCOUNTING PRONOUNCEMENTS

The Company adopted FASB Statement of Financial Accounting Standards No. 157 (SFAS No. 157), Fair Value Measurements on January 1, 2008. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This Statement emphasizes that fair value is a market-based measurement and should be determined based on assumptions that a market participant would use when pricing an asset or liability. This Statement clarifies that market participant assumptions should include assumptions about risk as well as the effect of a restriction on the sale or use of an asset. Additionally, this Statement establishes a fair value hierarchy that provides the highest priority to quoted prices in active markets and the lowest priority to unobservable data. In February 2008, Financial Accounting Standards Board Staff Position (FSP) No. 157-2, Effective Date of FASB Statement No. 157, was issued that delayed the application of SFAS No. 157 for nonfinancial assets and nonfinancial liabilities, until January 1, 2009. The Company adopted the provisions of SFAS No. 157 except for those nonfinancial assets and nonfinancial liabilities subject to deferral as a result of FSP No. 157-2. The adoption of SFAS No. 157 did not have any material effect on the Company's operating results or financial condition.

The Company adopted FASB Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 on January 1, 2008. SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. This statement also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. The Company did not elect the fair value option for any financial assets or liabilities as of March 31, 2008.

The Company adopted Staff Accounting Bulletin No. 109 (SAB No. 109), Written Loan Commitments Recorded at Fair Value through Earnings which supersedes SAB 105, Application of Accounting Principles to Loan Commitments which stated that in measuring the fair value of a derivative loan commitment, a company should not incorporate the expected net future cash flows related to the associated servicing of the loan. SAB 109 states that the expected net future cash flows related to the associated servicing of the loan should be included in measuring fair value for all written loan commitments that are accounted for at fair value through earnings. SAB 105 also states that internally-developed intangible assets should not be recorded as part of the fair value of a derivative loan commitment, and SAB 109 retains that view. The adoption of this standard did not have any material effect on the Company's operating results or financial condition.

In March 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 161 (SFAS No. 161), Disclosures about Derivative Instruments and Hedging Activities. SFAS No. 161 establishes, among other things, the disclosure requirements for derivative instruments and for hedging activities. This Statement amends and expands the disclosure requirements of Statement 133 with the intent to provide users of financial statements with an enhanced understanding of: how and why an entity uses derivative instruments; how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations; how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This Statement requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-

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related contingent features in derivative agreements. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company will adopt SFAS No. 161 on January 1, 2009, and does not expect the adoption to have a material impact on the financial statements.

NOTE 7. FAIR VALUE DISCLOSURES

As discussed in Note 6. New Accounting Pronouncements, effective January 1, 2008 the Company adopted SFAS No. 157, which provides a framework for measuring fair value under GAAP.

The Company also adopted SFAS No. 159, on January 1, 2008. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. This statement also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. The Company did not elect the fair value option for any financial assets or liabilities, does not have any material derivative instruments, does not participate in any significant hedging activities and the Company valued securities available for sale at fair value prior to the adoption of SFAS 157 and 159, therefore there is no transition adjustment resulting from the adoption of SFAS 157 and SFAS 159.

SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market, as well as certain U.S. Treasury, other U.S. Government and agency mortgage-backed debt securities that are highly liquid and are actively traded in over-the-counter markets.
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments and securities whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes certain U.S. Government and agency mortgage-backed debt securities, private mortgage-backed debt securities, corporate debt securities, municipal bonds, foreclosed assets and residential mortgage loans held-for-sale.

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Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes residential mortgage servicing rights.

The fair values of securities available for sale are determined on a recurring basis by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or pricing models utilizing significant observable inputs such as matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

The table below presents the balances of assets measured at fair value on a recurring basis:

	March 31, 2008			Assets at Fair Value
	Fair Value Measurements Using Level 1	Level 2	Level 3	
<u>Assets</u>				
Securities available for sale	\$ 1,027	\$339,575	\$ 0	\$ 340,602
Total assets	\$ 1,027	\$339,575	\$ 0	\$ 340,602

Also, the Company may be required, from time to time, to measure certain other financial assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-fair-value accounting or write-downs of individual assets. The table below presents the balances of assets measured at fair value on a nonrecurring basis:

	March 31, 2008			Assets at Fair Value
	Fair Value Measurements Using Level 1	Level 2	Level 3	
<u>Assets</u>				
Impaired loans	\$ 0	\$ 6,591	\$ 0	\$ 6,591
Mortgage servicing rights	0	0	138	138
Total assets	\$ 0	\$ 6,591	\$ 138	\$ 6,729

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying amount of \$6.6 million, with a valuation allowance of \$24,000, resulting in an additional provision for loan losses of \$24,000 for the period. In addition, \$6,000 in impairment of mortgage servicing rights, measured using Level 3 inputs within the fair value hierarchy, was reversed during the first quarter of 2008. The \$6,000 reversal was recorded in loan, insurance and service fees.

NOTE 8. RECLASSIFICATIONS

Certain amounts appearing in the financial statements and notes thereto for prior periods have been reclassified to conform with the current presentation. The reclassification had no effect on net income or stockholders' equity as previously reported.

Part 1

LAKELAND FINANCIAL CORPORATION

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION

and

RESULTS OF OPERATIONS

March 31, 2008

OVERVIEW

Lakeland Financial Corporation is the holding company for Lake City Bank. The Company is headquartered in Warsaw, Indiana and operates 43 offices in 12 counties in northern Indiana. The Company earned \$5.2 million for the first three months of 2008, versus \$4.8 million in the same period of 2007, an increase of 10.2%. The increase was driven by a \$1.4 million increase in net interest income as well as an increase of \$1.2 million in noninterest income. Offsetting these positive impacts was an increase of \$1.1 million in noninterest expense and an increase of \$512,000 in the provision for loan losses. Basic earnings per share for the first three months of 2008 were \$0.43 per share, versus \$0.39 per share for the first three months of 2007. Diluted earnings per share reflect the potential dilutive impact of stock options granted under the stock option plan. Diluted earnings per share for the first three months of 2008 were \$0.42 per share, versus \$0.38 for the first three months of 2007.

RESULTS OF OPERATIONS

Net Interest Income