CVB FINANCIAL CORP
Form 10-Q
November 09, 2007

**FORM 10-Q**
**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**
**Washington, D. C. 20549**

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2007

or

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

For the transition period from ________ to ________

For Quarter Ended September 30, 2007 | Commission File Number: 0-10140

CVB FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

| California | 95-3629339 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 701 North Haven Ave, Suite 350, Ontario, California | 91764 |
| (Address of Principal Executive Offices) | (Zip Code) |
| (Registrant s telephone number, including area code) | (909) 980-4030 |

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 ______

Indicate by check mark whether the registrant is a large accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer __X__ Accelerated filer ______ Non-accelerated filer ______

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 of the registrant: 83,434,643 outstanding as of November 6, 2007.

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**CVB FINANCIAL CORP.**
**2007 QUARTERLY REPORT ON FORM 10-Q**

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**PART I FINANCIAL INFORMATION (UNAUDITED)**

**ITEM 1. FINANCIAL STATEMENTS**

**CVB FINANCIAL CORP. AND SUBSIDIARIES**
**CONSOLIDATED BALANCE SHEETS**
**(unaudited)**
**Dollar amounts in thousands**

| | **September 30, 2007** | **December 31, 2006** |
|---|---|---|
| ASSETS | | |
| Cash and due from banks | $ 125,997 | $ 146,411 |
| Investment securities available-for-sale | 2,390,306 | 2,582,902 |
| Interest-bearing balances due from depository institutions | 570 | |
| Investment in stock of Federal Home Loan Bank (FHLB) | 80,743 | 78,866 |
| Loans and lease finance receivables, net | 3,311,749 | 3,070,196 |
| Allowance for credit losses | (30,428) | (27,737) |
| Total earning assets | 5,752,940 | 5,704,227 |

| | September 30, 2007 | December 31, 2006 |
|---|---|---|
| Premises and equipment, net | 47,048 | 44,963 |
| Intangibles | 21,858 | 10,121 |
| Goodwill | 46,582 | 31,531 |
| Cash value life insurance | 102,434 | 99,861 |
| Accrued interest receivable | 30,091 | 29,146 |
| Deferred tax asset | 11,627 | 13,620 |
| Other assets | 18,816 | 12,368 |
| TOTAL ASSETS | $6,157,393 | $6,092,248 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Liabilities: | | |
| Deposits: | | |
| Noninterest-bearing | $1,292,825 | $1,363,411 |
| Interest-bearing | 2,142,262 | 2,043,397 |
| Total deposits | 3,435,087 | 3,406,808 |
| Demand Note to U.S. Treasury | 180 | 7,245 |
| Repurchase agreements | 580,666 | 344,350 |
| Short-term borrowings | 340,500 | 1,094,900 |
| Long-term borrowings | 1,205,000 | 700,000 |
| Accrued interest payable | 19,146 | 16,156 |
| Deferred compensation | 8,228 | 7,946 |
| Junior subordinated debentures | 115,859 | 108,250 |
| Other liabilities | 45,910 | 19,268 |
| TOTAL LIABILITIES | 5,750,576 | 5,704,923 |
| COMMITMENTS AND CONTINGENCIES | | |
| Stockholders Equity: | | |
| Preferred stock, authorized, 20,000,000 shares without par; none issued or outstanding | | |
| Common stock, authorized, 122,070,312 shares without par; issued and outstanding 83,353,404 (2007) and 84,281,722 (2006) | 356,220 | 366,082 |
| Retained earnings | 60,271 | 34,464 |
| Accumulated other comprehensive loss, net of tax | (9,674) | (13,221) |
| Total stockholders equity | 406,817 | 387,325 |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | $6,157,393 | $6,092,248 |

See accompanying notes to the consolidated financial statements.



**CVB FINANCIAL CORP. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF EARNINGS**
**(unaudited)**
**Dollar amounts in thousands, except per share**

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 |
| Interest income: | | | | |
| Loans, including fees | $58,677 | $50,564 | $165,117 | $142,769 |
| Investment securities: | | | | |
| Taxable | 20,591 | 24,725 | 65,401 | 66,625 |
| Tax-preferred | 7,493 | 6,510 | 22,029 | 19,563 |
| Total investment income | 28,084 | 31,235 | 87,430 | 86,188 |
| Dividends from FHLB stock | 1,047 | 958 | 3,152 | 2,672 |
| Federal funds sold and Interest bearing deposits with other institutions | 72 | 6 | 92 | 92 |
| Total interest income | 87,880 | 82,763 | 255,791 | 231,721 |
| Interest expense: | | | | |
| Deposits | 18,445 | 18,903 | 53,531 | 48,398 |
| Short-term borrowings | 19,886 | 14,503 | 36,505 | 24,934 |
| Long-term borrowings | 5,853 | 5,890 | 40,437 | 24,724 |
| Junior subordinated debentures | 1,988 | 1,737 | 5,563 | 5,024 |
| Total interest expense | 46,172 | 41,033 | 136,036 | 103,080 |
| Net interest income before provision for credit losses | 41,708 | 41,730 | 119,755 | 128,641 |
| Provision for credit losses | | 1,250 | | 2,400 |
| Net interest income after provision for credit losses | 41,708 | 40,480 | 119,755 | 126,241 |
| Other operating income: | | | | |
| Service charges on deposit accounts | 3,340 | 3,253 | 9,827 | 9,833 |
| CitizensTrust | 1,657 | 1,807 | 5,355 | 5,467 |
| Bankcard services | 678 | 697 | 1,918 | 1,857 |
| BOLI income | 981 | 624 | 2,896 | 2,095 |
| Other | 1,207 | 1,461 | 3,361 | 4,377 |
| Gain on sale of securities, net | | 1,029 | | 1,062 |
| Total other operating income | 7,863 | 8,871 | 23,357 | 24,691 |
| Other operating expenses: | | | | |
| Salaries and employee benefits | 13,794 | 11,541 | 41,449 | 37,031 |
| Occupancy and Equipment | 4,605 | 3,986 | 12,905 | 11,591 |
| Professional services | 1,844 | 1,237 | 4,535 | 3,995 |
| Amortization of intangibles | 1,086 | 588 | 2,263 | 1,765 |
| Other | 5,889 | 5,278 | 16,811 | 15,977 |
| Total other operating expenses | 27,218 | 22,630 | 77,963 | 70,359 |
| Earnings before income taxes | 22,353 | 26,721 | 65,149 | 80,573 |
| Income taxes | 6,232 | 8,655 | 17,932 | 25,892 |
| Net earnings | $16,121 | $18,066 | $ 47,217 | $ 54,681 |
| Comprehensive income | $31,779 | $50,664 | $ 50,764 | $ 58,357 |
| Basic earnings per common share | $ 0.19 | $ 0.21 | $ 0.56 | $ 0.65 |
| Diluted earnings per common share | $ 0.19 | $ 0.21 | $ 0.56 | $ 0.64 |
| Cash dividends per common share | $ 0.085 | $ 0.09 | $ 0.255 | $ 0.27 |

See accompanying notes to the consolidated financial statements.

**CVB FINANCIAL CORP. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME (Unaudited)**

| | Common Shares Outstanding | Common Stock | Retained Earnings | Accumulated Other Comprehensive Loss | Comprehensive Income | Total |
|---|---|---|---|---|---|---|
| | | | (amounts and shares in thousands) | | | |
| **Balance January 1, 2007** | 84,282 | $366,082 | $ 34,464 | $(13,221) | | $387,325 |
| Issuance of common stock | 185 | 1,053 | | | | 1,053 |
| Repurchase of common stock | (2,720) | (30,030) | | | | (30,030) |
| Shares issued for the acquisition of First Coastal Bancshares | 1,606 | 18,046 | | | | 18,046 |
| Tax benefit from exercise of stock options | | 317 | | | | 317 |
| Stock-based Compensation Expense | | 752 | | | | 752 |
| Cash dividends ($0.255 per share) | | | (21,410) | | | (21,410) |
| Comprehensive income: | | | | | | |
| Net earnings | | | 47,217 | | $47,217 | 47,217 |
| Other comprehensive income: | | | | | | |
| Unrealized gain on securities available-for-sale, net | | | | 3,547 | 3,547 | 3,547 |
| Comprehensive income | | | | | $50,764 | |
| **Balance September 30, 2007** | 83,353 | $356,220 | $ 60,271 | $ (9,674) | | $406,817 |

| | Common Shares Outstanding | Common Stock | Retained Earnings | Accumulated Other Comprehensive Loss | Comprehensive Income | Total |
|---|---|---|---|---|---|---|
| | | | (amounts and shares in thousands) | | | |
| **Balance January 1, 2006** | 76,430 | $252,717 | $ 102,858 | $(13,386) | | $342,189 |
| Issuance of common stock | 140 | 698 | | | | 698 |
| Tax benefit from exercise of stock options | | 141 | | | | 141 |
| Stock-based Compensation Expense | | 596 | | | | 596 |
| Cash dividends ($0.27 per share) | | | (20,710) | | | (20,710) |
| Comprehensive income: | | | | | | |
| Net earnings | | | 54,681 | | $54,681 | 54,681 |
| Other comprehensive income: | | | | | | |
| Unrealized gain on securities available-for-sale, net | | | | 3,676 | 3,676 | 3,676 |
| Comprehensive income | | | | | $58,357 | |
| **Balance September 30, 2006** | 76,570 | $254,152 | $ 136,829 | $ (9,710) | | $381,271 |

| | At September 30, 2007 | 2006 |
|---|---|---|
| | (amounts and shares in thousands) | |
| **Disclosure of reclassification amount** | | |
| Unrealized gains on securities arising during the period | $ 6,115 | $ 6,335 |
| Tax expense | (2,568) | (2,659) |
| Net unrealized gain on securities | $ 3,547 | $ 3,676 |

See accompanying notes to the consolidated financial statements.



**CVB FINANCIAL CORP. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(unaudited)**

| | For the Nine Months Ended September 30, 2007 | 2006 |
|---|---|---|
| | (Dollar amounts in thousands) | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Interest and dividends received | $ 255,894 | $ 228,030 |
| Service charges and other fees received | 23,810 | 22,854 |
| Interest paid | (133,047) | (101,873) |
| Cash paid to vendors and employees | (76,484) | (62,208) |
| Income taxes paid | (11,250) | (20,750) |
| Net cash provided by operating activities | 58,923 | 66,053 |
| | | |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sale of FHLB Stock | 3,712 | |
| Proceeds from sales of MBS | | 57,132 |
| Proceeds from repayment of MBS | 338,605 | 297,193 |
| Proceeds from repayment of Fed Funds Sold | 52,000 | |
| Proceeds from maturity of investment securities | 35,955 | 4,368 |
| Purchases of investment securities available-for-sale | (72,608) | (193,887) |
| Purchases of MBS | (85,907) | (456,648) |
| Purchases of FHLB stock | (2,927) | (4,629) |
| Net increase in loans and lease finance receivables | (101,124) | (246,985) |
| Proceeds from sales of premises and equipment | 111 | 766 |
| Purchase of premises and equipment | (5,935) | (9,425) |
| Cash paid for purchase of First Coastal Bancshares, net of cash acquired | (743) | |
| Purchase of Bank Owned Life Insurance | | (25,000) |
| Investment in common stock of CVB Statutory Trust III | | (774) |
| Net cash provided by/(used in) investing activities | 161,139 | (577,889) |
| | | |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net decrease in transaction deposits | (145,032) | (135,619) |

| | For the Nine Months Ended September 30, | |
|---|---|---|
| Net (decrease)/increase in time deposits | (20,226) | 235,051 |
| Advances from Federal Home Loan Bank | 600,000 | 350,000 |
| Repayment of advances from Federal Home Loan Bank | (480,000) | (445,000) |
| Net (decrease) increase in short-term borrowings | (381,464) | 498,577 |
| Net increase in repurchase agreements | 236,316 | |
| Cash dividends on common stock | (21,410) | (20,710) |
| Repurchase of common stock | (30,030) | |
| Issuance of junior subordinated debentures | | 25,774 |
| Proceeds from exercise of stock options | 1,053 | 698 |
| Tax benefit related to exercise of stock options | 317 | 141 |
| Net cash (used in)/provided by financing activities | (240,476) | 508,912 |
| NET DECREASE IN CASH AND CASH EQUIVALENTS | (20,414) | (2,924) |
| CASH AND CASH EQUIVALENTS, beginning of period | 146,411 | 130,141 |
| CASH AND CASH EQUIVALENTS, end of period | $ 125,997 | $ 127,217 |

See accompanying notes to the consolidated financial statements.



**CVB FINANCIAL CORP. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**
**(unaudited)**

| | For the Nine Months Ended September 30, 2007 | 2006 |
|---|---|---|
| | (Dollar amounts in thousands) | |
| RECONCILIATION OF NET EARNINGS TO NET CASH PROVIDED BY OPERATING ACTIVITIES: | | |
| Net earnings | $ 47,217 | $54,681 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Gain on sale of investment securities | | (1,062) |
| Gain on sale of premises and equipment | (15) | (441) |
| Increase in cash value of life insurance | (3,127) | (2,095) |
| Net amortization of premiums on investment securities | 2,454 | 5,983 |
| Provisions for credit losses | | 2,400 |
| Stock-based compensation | 752 | 596 |
| Depreciation and amortization | 7,097 | 6,020 |
| Change in accrued interest receivable | (2,583) | (6,844) |
| Change in accrued interest payable | 2,990 | 1,207 |
| Change in other assets and liabilities | 4,138 | 5,608 |
| Total adjustments | 11,706 | 11,372 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | $ 58,923 | $66,053 |
| Supplemental Schedule of Noncash Investing and Financing Activities | | |

| | For the Nine Months Ended September 30, | |
|---|---|---|
| Purchase of First Coastal Bancshares: | | |
| Assets acquired | $ 194,125 | $ |
| Goodwill & Intangibles | 29,051 | |
| Liabilities assumed | (204,387) | |
| Stock issued | (18,046) | |
| Purchase price of acquisition, net of cash received | $ 743 | $ |
| Securities purchased and not settled | $ 22,515 | $ 4,029 |

See accompanying notes to the consolidated financial statements.



**CVB FINANCIAL CORP. AND SUBSIDIARIES**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)
For the nine months ended September 30, 2007 and 2006

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying condensed consolidated unaudited financial statements and notes thereto have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission for Form 10-Q and conform to practices within the banking industry and include all of the information and disclosures required by accounting principles generally accepted in the United States of America for interim financial reporting. The results of operations for the nine months ended September 30, 2007 are not necessarily indicative of the results for the full year. These financial statements should be read in conjunction with the financial statements, accounting policies and financial notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2006 filed with the Securities and Exchange Commission. In the opinion of management, the accompanying condensed consolidated unaudited financial statements reflect all adjustments (consisting only of normal recurring adjustments), which are necessary for a fair representation of financial results for the interim periods presented. A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

***Principles of Consolidation*** The consolidated financial statements include the accounts of CVB Financial Corp. (the Company ) and its wholly owned subsidiary: Citizens Business Bank (the Bank ) after elimination of all intercompany transactions and balances. The Company also has three inactive subsidiaries; CVB Ventures, Inc.; Chino Valley Bancorp; and ONB Bancorp. The Company is also the common stockholder of CVB Statutory Trust I, CVB Statutory Trust II and CVB Statutory Trust III. CVB Statutory Trusts I and II were created in December 2003 and CVB Statutory Trust III was created in January 2006 to issue trust preferred securities in order to raise capital for the Company. The Company also acquired trust preferred securities through the acquisition of First Coastal Bancshares ( FCB ). In accordance with Financial Accounting Standards Board Interpretation No. 46R Consolidation of Variable Interest Entities ( FIN No. 46R ), these trusts do not meet the criteria for consolidation.

***Nature of Operations*** The Company s primary operations are related to traditional banking activities, including the acceptance of deposits and the lending and investing of money through the operations of the Bank. The Bank also provides automobile and equipment leasing and brokers mortgage loans to customers through its Citizens Financial Services Division (formerly known as Golden West Financial Division) and offers trust services to customers through its CitizensTrust Division. The Bank s customers consist primarily of small to mid-sized businesses and individuals located in San Bernardino County, Riverside County, Orange County, Los Angeles County, Madera County, Fresno County, Tulare County, and Kern County. The Bank operates 44 Business Financial Centers with its headquarters located in the city of Ontario.

The Company s operating business units have been combined into two main segments: Business Financial Centers and Treasury. Business Financial Centers (branches) comprise the loans, deposits, products and services the Bank offers to the majority of its customers. The other segment is Treasury, which manages the investment portfolio of the Company. The Company s remaining centralized functions and eliminations

of inter-segment amounts have been aggregated and included in Other.

The internal reporting of the Company considers all business units. Funds are allocated to each business unit based on its need to fund assets (use of funds) or its need to invest funds (source of funds). Net income is determined based on the actual net income of the business unit plus the allocated income or



expense based on the sources and uses of funds for each business unit. Non-interest income and non-interest expense are those items directly attributable to a business unit.

***Correction of Immaterial Error*** The Company revised it s consolidated financial statements for the year ended December 31, 2006, including the quarters therein, due to corrections of immaterial prior years errors identified in the current year. The Company understated tax expense for 2006 and 2005 primarily related to the accounting treatment of tax credits associated with Qualified Zone Academy Bonds and also over-accrued FHLB Stock dividend income. The result was a decrease of previously reported net income by approximately $1.3 million for the year ended December 31, 2006 and $688,000 for the years prior to 2006. For the three and nine months ended September 30, 2006, previously reported net income decreased by $389,000 and $931,000, respectively. Basic and diluted earnings per common share decreased by $.01 per share from previously reported amounts as of the three and nine months ended September 30, 2006.

***Investment Securities*** The Company classifies as held-to-maturity those debt securities that we have the positive intent and ability to hold to maturity. Securities classified as trading are those securities that are bought and held principally for the purpose of selling them in the near term. All other debt and equity securities are classified as available-for-sale. Securities held-to-maturity are accounted for at cost and adjusted for amortization of premiums and accretion of discounts. Trading securities are accounted for at fair value with the unrealized holding gains and losses being included in current earnings. Available-for-sale securities are accounted for at fair value, with the net unrealized gains and losses, net of income tax effects, presented as a separate component of stockholders equity. At each reporting date, available-for-sale securities are assessed to determine whether there is an other-than-temporary impairment. Such impairment, if any, is required to be recognized in current earnings rather than as a separate component of stockholders equity. Realized gains and losses on sales of securities are recognized in earnings at the time of sale and are determined on a specific-identification basis. Purchase premiums and discounts are recognized in interest income using the interest method over the life of the security. For mortgage-related securities (i.e., securities that are collateralized and payments received from underlying mortgage) the amortization or accretion is based on the estimated average lives of the securities. The Company s investment in Federal Home Loan Bank ( FHLB ) stock is carried at cost. At September 30, 2007, all of the Company s investment securities are classified as available-for-sale.

***Loans and Lease Finance Receivables*** Loans and lease finance receivables are reported at the principal amount outstanding, less deferred net loan origination fees. Interest on loans and lease finance receivables is credited to income based on the principal amount outstanding. Interest income is not recognized on loans and lease finance receivables when collection of interest is deemed by management to be doubtful. In the ordinary course of business, the Company enters into commitments to extend credit to its customers. These commitments are not reflected in the accompanying consolidated financial statements. As of September 30, 2007, the Company entered into commitments with certain customers amounting to $857.1 million compared to $680.6 million at December 31, 2006. Letters of credit at September 30, 2007, and December 31, 2006, were $57.6 million and $64.8 million, respectively.

The Bank receives collateral to support loans, lease finance receivables, and commitments to extend credit for which collateral is deemed necessary. The most significant categories of collateral are real estate, principally commercial and industrial income-producing properties, real estate mortgages, and assets utilized in agribusiness.

Nonrefundable fees and direct costs associated with the origination or purchase of loans are deferred and netted against outstanding loan balances. The deferred net loan fees and costs are recognized in interest income over the loan term using the effective yield method.

***Provision and Allowance for Credit Losses*** The determination of the balance in the allowance for credit losses is based on an analysis of the loan and lease finance receivables portfolio using a systematic methodology and reflects an amount that, in management s judgment, is adequate to provide for probable

credit losses inherent in the portfolio, after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience, and such other factors as deserve current recognition in estimating inherent credit losses. The estimate is reviewed quarterly by management and periodically various regulatory entities and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. The provision for credit losses is charged to expense. During the first nine months of 2007, we did not record a provision for credit losses. The allowance for credit losses was $30.4 million as of September 30, 2007. This represents an increase of $2.7 million when compared with an allowance for credit losses of $27.7 million as of December 31, 2006. The increase was primarily due to the $2.7 million allowance for credit losses acquired through FCB, supplemented by net recoveries of $20,000 during the first nine months of 2007.

In addition to the allowance for credit losses, the Company also has a reserve for undisbursed commitments for loans and letters of credit. This reserve is carried on the liabilities section of the balance sheet in other liabilities. Provisions to this reserve are included in other expense. For the nine months of 2007, the Company recorded an increase of $741,000 in the reserve for undisbursed commitments. As of September 30, 2007, the balance in this reserve was $2.5 million.

A loan for which collection of principal and interest according to its original terms is not probable is considered to be impaired. The Company s policy is to record a specific valuation allowance, which is included in the allowance for credit losses, or charge off that portion of an impaired loan that exceeds its fair value. Fair value is usually based on the value of underlying collateral.

At September 30, 2007, impaired loans totaled $2.9 million. These loans were supported by collateral with a fair market value, net of prior liens, of $2.0 million. The amount of reserve for these loans was $900,000 as of September 30, 2007. There were no loans classified as impaired at December 31, 2006.

***Premises and Equipment*** Premises and equipment are stated at cost, less accumulated depreciation, which is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives using the straight-line method. Properties under capital lease and leasehold improvements are amortized over the shorter of estimated economic lives of 15 years or the initial terms of the leases. Estimated lives are 3 to 5 years for computer and equipment, 5 to 7 years for furniture, fixtures and equipment, and 15 to 40 years for buildings and improvements. Long-lived assets are reviewed periodically for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. The impairment is calculated as the difference in fair value of assets and their carrying value. The impairment loss, if any, would be recorded in noninterest expense.

***Other Real Estate Owned*** Other real estate owned represents real estate acquired through foreclosure in satisfaction of commercial and real estate loans and is stated at fair value, minus estimated costs to sell (fair value at time of foreclosure). Loan balances in excess of fair value of the real estate acquired at the date of acquisition are charged against the allowance for credit losses. Any subsequent operating expenses or income, reduction in estimated values, and gains or losses on disposition of such properties are charged to current operations. There was no other real estate owned at September 30, 2007 and December 31, 2006.

***Business Combinations and Intangible Assets*** On June 22, 2007, we acquired First Coastal Bancshares ( FCB ). The Company issued 1,605,523 common shares and $18.0 million in cash to FCB shareholders in connection with the acquisition. FCB had total assets of $194.4 million, total loans of $140.0 million and total deposits of $193.5 million as of the acquisition date, June 22, 2007. FCB had four offices, in Manhattan Beach, El Segundo, Marina Del Rey, and Gardena. These four offices are operating as business financial centers of the Bank. The acquisition was not considered significant to the overall financial position of the Company.

The Company has engaged in the acquisition of financial institutions and the assumption of deposits and purchase of assets from other financial institutions in its market area. The Company has paid



premiums on certain transactions, and such premiums are recorded as intangible assets, in the form of goodwill or other intangible assets. In accordance with the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 142, goodwill is not being amortized whereas identifiable intangible assets with finite lives are amortized over their useful lives. On an annual basis, the Company tests goodwill and intangible assets for impairment.

The Company completed its annual impairment test as of July 1, 2007, and did not record any impairment of goodwill. At September 30, 2007 goodwill was $46.6 million, of which $15.1 million was a result of the FCB acquisition. As of September 30, 2007, intangible assets that continue to be subject to amortization include core deposit premiums of $21.9 million (net of $11.8 million of accumulated amortization), of which $14.0 million was a result of the FCB acquisition. The Company is in the process of obtaining valuations of certain assets and liabilities

acquired from FCB; thus, the allocation of the purchase price and the intangible assets is subject to adjustment. Amortization expense for such intangible assets was $2.3 million for the nine months ended September 30, 2007. Estimated amortization expense, for the remainder of 2007 is expected to be $1.1 million. Estimated amortization expense, for the succeeding five fiscal years is $4.3 million for year one, $3.7 million for year two, $3.7 million for year three, $3.6 million for year four and $2.4 million for year five. The weighted average remaining life of intangible assets is approximately 5.25 years.

***Income Taxes*** Deferred income taxes are recognized for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end, based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income.

The Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, as of January 1, 2007. The Company has two tax jurisdictions: the U.S. Government and the State of California. As of January 1, 2007 and September 30, 2007, the Company did not have any significant liabilities associated with uncertain tax positions. The Company still has the tax years of 2003, 2004, 2005, and 2006 subject to examination by both the Internal Revenue Service and the Franchise Tax Board of the State of California.

The Company will classify any interest required to be paid on an underpayment of income taxes as interest expense. Any penalties accessed by a taxing authority will be classified as other expense.

***Earnings per Common Share*** Basic earnings per common share are computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding during each period. The computation of diluted earnings per common share considers the number of tax-effected shares issuable upon the assumed exercise of outstanding common stock options. Share and per share amounts have been retroactively restated to give effect to all stock dividends and splits. The number of shares outstanding at September 30, 2007 was 84,353,404. The table below presents the reconciliation of earnings per share for the periods indicated.



**Earnings Per Share Reconciliation**
**(Dollars and shares in thousands, except per share amounts)**
**For the Nine Months**
**Ended September 30,**

| | 2007 | | | 2006 | | |
|---|---|---|---|---|---|---|
| | Income (Numerator) | Weighted Average Shares (Denominator) | Per Share Amount | Income (Numerator) | Weighted Average Shares (Denominator) | Per Share Amount |
| BASIC EPS | | | | | | |
| Income available to common stockholders | $47,217 | 83,716 | $ 0.56 | $54,681 | 84,136 | $ 0.65 |
| EFFECT OF DILUTIVE SECURITIES | | | | | | |
| Incremental shares from assumed exercise of outstanding options | | 657 | (0.00) | | 795 | (0.01) |
| DILUTED EPS | | | | | | |
| Income available to common stockholders | $47,217 | 84,373 | $ 0.56 | $54,681 | 84,931 | $ 0.64 |

**Earnings Per Share Reconciliation**
**(Dollars and shares in thousands, except per share amounts)**
**For the Three Months Ended**
**September 30,**

| 2007 | 2006 |
|---|---|

| | Income (Numerator) | Weighted Average Shares (Denominator) | Per Share Amount | Income (Numerator) | Weighted Average Shares (Denominator) | Per Share Amount |
|---|---|---|---|---|---|---|
| BASIC EPS | | | | | | |
| Income available to common stockholders | $16,121 | 84,373 | $0.19 | $18,066 | 84,160 | $0.21 |
| EFFECT OF DILUTIVE SECURITIES | | | | | | |
| Incremental shares from assumed exercise of outstanding options | | 357 | 0.00 | | 910 | 0.00 |
| DILUTED EPS | | | | | | |
| Income available to common stockholders | $16,121 | 84,730 | $0.19 | $18,066 | 85,070 | $0.21 |

***Stock-Based Compensation*** At September 30, 2007, the Company has three stock-based employee compensation plans, which are described more fully in Note 15 in the Company s Annual Report on Form 10-K.

***Statement of Cash Flows*** Cash and cash equivalents as reported in the statements of cash flows include cash and due from banks. Cash flows from loans and deposits are reported net.

***CitizensTrust*** This division provides trust, investment and brokerage related services, as well as financial, estate and business succession planning services. The amount of these funds and the related liability have not been recorded in the accompanying consolidated balance sheets because they are not assets or liabilities of the Bank or Company, with the exception of any funds held on deposit with the Bank.

***Use of Estimates in the Preparation of Financial Statements*** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for credit losses. Other significant estimates which may be



subject to change include fair value disclosures, impairment of investments and goodwill, and valuation of deferred tax assets and other intangibles.

***Recent Accounting Pronouncements*** In September 2006, the Financial Accounting Standards Board ( FASB ) issued Statement No. 157, Fair Value Measurements ( SFAS No. 157 ). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly, does not require any new fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. Management is currently evaluating the effect of adoption of SFAS No. 157.

In September 2006, the Emerging Issues Task Force ( EITF ) reached a final consensus on Issue 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements ( EITF 06-4 ). EITF 06-4 requires that for a split-dollar life insurance arrangement, an employer should recognize a liability for future benefits in accordance with SFAS 106, Employers Accounting for Postretirement Benefits Other Than Pensions or APB Opinion No. 12, Omnibus Opinion 1967. Under the guidance, the purchase of an endorsement type policy does not constitute a settlement since the policy does not qualify as nonparticipating because the policyholders are subject to the favorable and unfavorable experience of the insurance company. EITF 06-4 is effective for fiscal years beginning after December 15, 2007. Management does not expect the adoption of EITF 06-4 to have a material effect on the Company s consolidated financial position or results of operations.

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities-Including an Amendment of FASB Statement No. 115. SFAS 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS 159 are elective; however, the amendment to SFAS 115, Accounting for Certain Investments in Debt and Equity Securities, applies to all entities with available for sale or trading securities. For financial instruments elected to be accounted for at fair value, an entity will report the unrealized gains and losses in earnings. SFAS 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007. Management is currently evaluating the effect of adoption of SFAS No. 159.

***Reclassification*** Certain amounts in the prior periods financial statements and related footnote disclosures have been reclassified to conform to the current presentation with no impact on previously reported net income or stockholders equity.

***Shareholder Rights Plan*** The Company has a shareholder rights plan designed to maximize long-term value and to protect shareholders from improper takeover tactics and takeover bids which are not fair to all shareholders. In accordance with the plan, preferred share purchase rights were distributed as a dividend at the rate of one right to purchase one one-thousandth of a share of the Company s Series A Participating Preferred Stock at an initial exercise price of $50.00 (subject to adjustment as described in the terms of the plan) upon the occurrence of certain triggering events. For additional information concerning this plan, see Note 11 to Consolidated Financial Statements, Commitments and Contingencies contained in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

***Other Contingencies*** In the ordinary course of business, the Company becomes involved in litigation. Based upon the Company s internal records and discussions with legal counsel, the Company records reserves for estimates of the probable unfavorable outcome of all cases brought against them. At September 30, 2007, we are not aware of any material pending legal action or complaints asserted against us.

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***Business Segments*** The Company has identified two principal reportable segments : Business Financial Centers and the Treasury Department. The Company s subsidiary bank has 44 Business Financial Centers (branches), organized in 5 geographic regions, which are the focal points for customer sales and services. The company utilizes an internal reporting system to measure the performance of various operating segments within the Bank which is the basis for determining the Bank s reportable segments. The Bank s geographic regions are considered operating segments and have been aggregated for segment reporting purposes because the products and services are similar and are sold to similar types of customers, have similar production and distribution processes, have similar economic characteristics, and have similar reporting and organizational structures. The Treasury Department s primary focus is managing the Bank s investments, liquidity, and interest rate risk. Information related to the Company s remaining operating segments which include construction lending, dairy and livestock lending, SBA lending and leasing, centralized functions and eliminations of inter-segment amounts have been aggregated and included in Other. In addition, the Company allocates internal funds transfer pricing to the segments using a methodology that charges users of funds interest expense and credits providers of funds interest income with the net effect of this allocation being recorded in administration.

The following table represents the selected financial information for these two business segments. Accounting principles generally accepted in the United States of America do not have an authoritative body of knowledge regarding the management accounting used in presenting segment financial information. The accounting policies for each of the business units is the same as those policies identified for the consolidated Company and identified in the footnote on the summary of significant accounting policies. The income numbers represent the actual income and expenses of each business unit. In addition, each segment has allocated income and expenses based on management s internal reporting system, which allows management to determine the performance of each of its business units. Loan fees, included in the Business Financial Centers category are the actual loan fees paid to the Company by its customers. These fees are eliminated and deferred in the Other category, resulting in deferred loan fees for the consolidated financial statements. All income and expense items not directly associated with the two business segments are grouped in the Other category. Future changes in the Company s management structure or reporting methodologies may result in changes in the measurement of operating segment results.

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The following tables present the operating results and other key financial measures for the individual reportable segments for the three and nine months ended September 30, 2007 and 2006:

| | Three Months Ended September 30, 2007 | | | |
|---|---|---|---|---|
| | **Treasury** | **Other** | **Eliminations** | **Total** |

**Three Months Ended September 30, 2007**

| | Business Financial Centers | | | | |
|---|---|---|---|---|---|
| Interest income, including loan fees | $45,362 | $ 29,224 | $ 13,294 | $ | **$87,880** |
| Credit for funds provided (1) | 16,266 | | 3,764 | (20,030) | |
| Total interest income | 61,628 | 29,224 | 17,058 | (20,030) | **87,880** |
| | | | | | |
| Interest expense | 17,025 | 24,113 | 5,034 | | **46,172** |
| Charge for funds used (1) | 4,477 | 8,365 | 7,188 | (20,030) | |
| Total interest expense | 21,502 | 32,478 | 12,222 | (20,030) | **46,172** |
| Net interest income | 40,126 | (3,254) | 4,836 | | **41,708** |
| Provision for credit losses | | | | | |
| Net interest income after provision for credit losses | $40,126 | ($3,254) | $ 4,836 | $ | **$41,708** |
| Non-interest income | 4,628 | 1 | 3,234 | | **7,863** |
| Non-interest expense | 11,515 | 312 | 15,391 | | **27,218** |
| Segment pretax profit (loss) | $33,239 | ($3,565) | ($7,321) | $ | **$22,353** |

**Three Months Ended September 30, 2006**

| | Business Financial Centers | Treasury | Other | Eliminations | Total |
|---|---|---|---|---|---|
| Interest income, including loan fees | $32,518 | $32,213 | $ 18,032 | $ | **$82,763** |
| Credit for funds provided (1) | 16,809 | | 1,466 | (18,275) | |
| Total interest income | 49,327 | 32,213 | 19,498 | (18,275) | **82,763** |
| | | | | | |
| Interest expense | 14,100 | 24,725 | 2,208 | | **41,033** |
| Charge for funds used (1) | 2,020 | 4,761 | 11,494 | (18,275) | |
| Total interest expense | 16,120 | 29,486 | 13,702 | (18,275) | **41,033** |
| Net interest income | 33,207 | 2,727 | 5,796 | | **41,730** |
| Provision for credit losses | | | 1,250 | | **1,250** |
| Net interest income after provision for credit losses | $33,207 | $ 2,727 | $ 4,546 | $ | **$40,480** |
| Non-interest income | 3,993 | 1,029 | 3,849 | | **8,871** |
| Non-interest expense | 10,246 | 291 | 12,093 | | **22,630** |
| Segment pretax profit (loss) | **$26,954** | **$ 3,465** | **($3,698)** | $ | **$26,721** |

(1) Credit for funds provided and charge for funds used is eliminated in the consolidated presentation.



**Nine Months Ended September 30, 2007**

| | Business Financial | Treasury | Other | Eliminations | Total |
|---|---|---|---|---|---|

| | Nine Months Ended September 30, 2007 | | | | |
|---|---|---|---|---|---|
| | Centers | | | | |
| Interest income, including loan fees | $ 127,191 | $ 90,727 | $ 37,873 | $ | **$ 255,791** |
| Credit for funds provided (1) | 47,252 | | 10,876 | (58,128) | |
| Total interest income | 174,443 | 90,727 | 48,749 | (58,128) | **255,791** |
| | | | | | |
| Interest expense | 47,655 | 74,737 | 13,644 | | **136,036** |
| Charge for funds used (1) | 11,292 | 24,198 | 22,638 | (58,128) | |
| Total interest expense | 58,947 | 98,935 | 36,282 | (58,128) | **136,036** |
| Net interest income | 115,496 | (8,208) | 12,467 | | **119,755** |
| Provision for credit losses | | | | | |
| Net interest income after provision for credit losses | $ 115,496 | ($8,208) | $ 12,467 | $ | **$ 119,755** |
| Non-interest income | 13,586 | 1 | 9,770 | | **23,357** |
| Non-interest expense | 32,695 | 857 | 44,411 | | **77,963** |
| Segment pretax profit (loss) | $ 96,387 | ($9,064) | ($22,174) | $ | **$ 65,149** |
| Segment assets as of September 30, 2007 | $3,479,527 | $1,993,898 | $ 685,927 | $ | **$6,159,352** |

| | Nine Months Ended September 30, 2006 | | | | |
|---|---|---|---|---|---|
| | Business Financial Centers | Treasury | Other | Eliminations | Total |
| Interest income, including loan fees | $ 102,976 | $ 88,989 | $ 39,756 | $ | **$ 231,721** |
| Credit for funds provided (1) | 50,019 | | 5,793 | (55,812) | |
| Total interest income | 152,995 | 88,989 | 45,549 | (55,812) | **231,721** |
| | | | | | |
| Interest expense | 36,002 | 60,710 | 6,368 | | **103,080** |
| Charge for funds used (1) | 5,496 | 18,613 | 31,703 | (55,812) | |
| Total interest expense | 41,498 | 79,323 | 38,071 | (55,812) | **103,080** |
| Net interest income | 111,497 | 9,666 | 7,478 | | **128,641** |
| Provision for credit losses | | | 2,400 | | **2,400** |
| Net interest income after provision for credit losses | $ 111,497 | $ 9,666 | $ 5,078 | $ | **$ 126,241** |
| Non-interest income | 11,384 | 1,063 | 12,244 | | **24,691** |
| Non-interest expense | 29,877 | 800 | 39,682 | | **70,359** |
| Segment pretax profit (loss) | $ 93,004 | $ 9,929 | ($22,360) | $ | **$ 80,573** |
| Segment assets as of September 30, 2006 | $3,221,611 | $2,284,708 | $ 468,329 | $ | **$5,974,648** |

(1) Credit for funds provided and charge for funds used is eliminated in the consolidated presentation.



**ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

## GENERAL

Management s discussion and analysis is written to provide greater insight into the results of operations and the financial condition of CVB Financial Corp. and its subsidiaries. Throughout this discussion, Company refers to CVB Financial Corp. and its subsidiaries as a consolidated entity. CVB refers to CVB Financial Corp. as the unconsolidated parent company and Bank refers to Citizens Business Bank. For a more complete understanding of the Company and its operations, reference should be made to the financial statements included in this report and in the Company s 2006 Annual Report on Form 10-K. Certain statements in this Report on Form 10-Q constitute forward-looking statements under the Private Securities Litigation Reform Act of 1995 which involve risks and uncertainties. Our actual results may differ significantly from the results discussed in such forward-looking statements. Factors that might cause such a difference include, but are not limited to, economic conditions, competition in the geographic and business areas in which we conduct operations, natural disasters, ability to successfully integrate acquisitions, fluctuations in interest rates, credit quality, and government regulations. For additional information concerning these factors and other factors which may cause actual results to differ from the results discussed in our forward-looking statements, see the periodic filings the Company makes with the Securities and Exchange Commission, and in particular Item 1A. Risk Factors contained in the Company s Annual Report on Form 10-K for the year ended December 31, 2006. The Company does not undertake, and specifically disclaims, any obligation to update any forward-looking statements to reflect the occurrence of events or circumstances after the date of such statements except as required by law.

## OVERVIEW

We are a bank holding company with one bank subsidiary, Citizens Business Bank. We have three other inactive subsidiaries: CVB Ventures, Inc.; Chino Valley Bancorp and ONB Bancorp. We are also the common stockholder of CVB Statutory Trust I, CVB Statutory Trust II and CVB Statutory Trust III which were formed to issue trust preferred securities in order to increase the capital of the Company. Through our acquisition of FCB in June 2007, we acquired FCB Capital Trust I and II. We are based in Ontario, California in what is known as the Inland Empire . Our geographical market area encompasses the City of Stockton (the middle of the Central Valley) in the center of California to the City of Laguna Beach (in Orange County) in the southern portion of California. Through our acquisition of FCB our geographic market has expanded to include the South Bay region of Los Angeles County. Our mission is to offer the finest financial products and services to professionals and businesses in our market area.

Our primary source of income is from the interest earned on our loans and investments and our primary area of expense is the interest paid on deposits, borrowings, and salaries and benefits. As such our net income is subject to fluctuations in interest rates and their impact on our income statement. The flat interest rate environment has compressed our net interest margin. We are also subject to competition from other financial institutions, which may affect our pricing of products and services, and the fees and interest rates we can charge on them, as well as our net interest margin.

Economic conditions in our California service area impact our business. As a result of a slowdown in housing sales, we have experienced slower growth in construction loans and a decrease in deposit balances from escrow companies. Unemployment remains low, but job growth is slowing.

Over the past few years, we have been active in acquisitions and we will continue to pursue acquisition targets which will enable us to meet our business objectives and enhance shareholder value. Since 2000, we have acquired four banks and a leasing company, and we have opened four de novo branches; Glendale, Bakersfield, Fresno, and Madera. In May 2007, we opened another de novo branch in Stockton, California.



Our growth in loans and investments for the first nine months of 2007 compared with the first nine months of 2006 has allowed our interest income to grow. The Bank has always had an excellent base of interest free deposits primarily due to our specialization in businesses and professionals as customers. This has allowed us to have a low cost of deposits, currently 2.1% for the nine months of 2007. However, the rise in interest expense resulting primarily from an increase in average interest-bearing liabilities and an increase in the cost of these liabilities has caused our net interest margin (tax-equivalent) to decline to 3.02% for the nine months ended September 30, 2007 from 3.42% for the nine months ended September 30, 2006.

## CRITICAL ACCOUNTING POLICIES

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies upon which our financial condition depends, and which involve the most complex or subjective decisions or assessments are as follows:

**Allowance for Credit Losses:** Arriving at an appropriate level of allowance for credit losses involves a high degree of judgment. Our allowance for credit losses provides for probable losses based upon evaluations of known and inherent risks in the loan portfolio. The determination of the balance in the allowance for credit losses is based on an analysis of the loan and lease finance receivables portfolio using a systematic methodology and reflects an amount that, in our judgment, is adequate to provide for probable credit losses inherent in the portfolio, after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience, and such other factors as deserve current recognition in estimating inherent credit losses. The provision for credit losses is charged to expense. For a full discussion of our methodology of assessing the adequacy of the allowance for credit losses, see the Risk Management section of this Management s Discussion and Analysis of Financial Condition and Results of Operations.

**Investment Portfolio:** The investment portfolio is an integral part of the Company s financial performance. We invest primarily in fixed income securities. Accounting estimates are used in the presentation of the investment portfolio and these estimates do impact the presentation of our financial condition and results of operations. Many of the securities included in the investment portfolio are purchased at a premium or discount. The premiums or discounts are amortized or accreted over the life of the security. For mortgage-related securities (i.e., securities that are collateralized and payments received from underlying mortgages), the amortization or accretion is based on estimated average lives of the securities. The lives of these securities can fluctuate based on the amount of prepayments received on the underlying collateral of the securities. The amount of prepayments varies from time to time based on the interest rate environment (i.e., lower interest rates increase the likelihood of refinances) and the rate of turnover of the mortgages (i.e., how often the underlying properties are sold and mortgages paid-off). We use estimates for the average lives of these mortgage-related securities based on information received from third parties whose business it is to compile mortgage related data and develop a consensus of that data. We adjust the rate of amortization or accretion regularly to reflect changes in the estimated average lives of these securities.

We classify securities as held-to-maturity those debt securities that we have the positive intent and ability to hold to maturity. Securities classified as trading are those securities that are bought and held principally for the purpose of selling them in the near term. All other debt and equity securities are classified as available-for-sale. Securities held-to-maturity are accounted for at cost and adjusted for amortization of premiums and accretion of discounts. Trading securities are accounted for at fair value with the unrealized holding gains and losses being included in current earnings. Securities available-for-sale are accounted for at fair value, with the net unrealized gains and losses, net of income tax effects, presented as a separate component of stockholders equity. At each reporting date, available-for-sale securities



are assessed to determine whether there is an other-than-temporary impairment. Such impairment, if any, is required to be recognized in current earnings rather than as a separate component of stockholders equity. Realized gains and losses on sales of securities are recognized in earnings at the time of sale and are determined on a specific-identification basis. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities, except for mortgage-related securities as discussed in the previous paragraph. Our investment in Federal Home Loan Bank ( FHLB ) stock is carried at cost.

**Income Taxes:** We account for income taxes using the asset and liability method by deferring income taxes based on estimated future tax effects of differences between the tax and book basis of assets and liabilities considering the provisions of enacted tax laws. These differences result in deferred tax assets and liabilities, which are included in our balance sheets. We must also assess the likelihood that any deferred tax assets will be recovered from future taxable income and establish a valuation allowance for those assets determined to not likely be recoverable. Our judgment is required in determining the amount and timing of recognition of the resulting deferred tax assets and liabilities, including projections of future taxable income. Although we have determined a valuation allowance is not required for any of our deferred tax assets, there is no guarantee that these assets are recoverable.

**Goodwill and Intangible Assets:** We have acquired entire banks and branches of banks. Those acquisitions accounted for under the purchase method of accounting have given rise to goodwill and intangible assets. We record the assets acquired and liabilities assumed at their fair value. These fair values are arrived at by use of internal and external valuation techniques. The excess purchase price is allocated to assets and liabilities respectively, resulting in identified intangibles. The identified intangibles are amortized over the estimated lives of the assets or liabilities. Any excess purchase price after this allocation results in goodwill. Goodwill is tested on an annual basis for impairment.

## ANALYSIS OF THE RESULTS OF OPERATIONS

### *Earnings*

We reported net earnings of $47.2 million for the nine months ended September 30, 2007. This represented a decrease of $7.5 million or 13.65%, from net earnings of $54.7 million, for the nine months ended September 30, 2006. Basic and diluted earnings per share for the

nine-month period decreased to $0.56 per share for 2007, compared to $0.65 basic earnings per share for 2006 and $0.64 diluted earnings per share for 2006. The annualized return on average assets was 1.04% for the nine months ended of 2007 compared to an annualized return on average assets of 1.29% for the nine months of 2006. The annualized return on average equity was 15.82% for the nine months ended September 30, 2007, compared to an annualized return of 20.74% for the nine months ended September 30, 2006.

For the quarter ended September 30, 2007, our net earnings were $16.1 million. This represented a decrease of $1.9 million or 10.77%, from net earnings of $18.1 million, for the third quarter of 2006. Basic and diluted earnings per share decreased to $0.19 per share for the third quarter of 2007 compared to $0.21 per share for the second quarter of 2006. The annualized return on average assets was 1.04% for the third quarter of 2007 compared to an annualized return on average assets of 1.21% for the same period last year. The annualized return on average equity was 15.99% for the third quarter of 2007 compared to an annualized return on average equity of 20.35 % for the third quarter of 2006.

***Net Interest Income***

The principal component of our earnings is net interest income, which is the difference between the interest and fees earned on loans and investments (earning assets) and the interest paid on deposits and borrowed funds (interest-bearing liabilities). Net interest margin is the taxable-equivalent of net interest income as a percentage of average earning assets for the period. The level of interest rates and the volume and mix of earning assets and interest-bearing liabilities impact net interest income and net interest margin. The net interest spread is the yield on average earning assets minus the cost of average



interest-bearing liabilities. Our net interest income, interest spread, and net interest margin are sensitive to general business and economic conditions. These conditions include short-term and long-term interest rates, inflation, monetary supply, and the strength of the economy, in general, and the local economies in which we conduct business. Our ability to manage the net interest income during changing interest rate environments will have a significant impact on our overall performance. Our balance sheet is currently liability-sensitive; meaning interest-bearing liabilities will generally reprice more quickly than earning assets. Therefore, our net interest margin is likely to decrease in sustained periods of rising interest rates and increase in sustained periods of declining interest rates. We manage net interest income by affecting changes in the mix of earning assets as well as the mix of interest-bearing liabilities, changes in the level of interest-bearing liabilities in proportion to earning assets, and in the growth of earning assets.

Our net interest income, after the provision for credit losses, totaled $119.8 million for the nine months ended September 30, 2007. This represented a decrease of $6.5 million, or 5.14%, from net interest income, after provision for credit losses, of $126.2 million for the same period in 2006. The decrease in net interest income of $6.5 million resulted from a $24.1 million increase in interest income, offset by a $33.0 million increase in interest expense and $2.4 million provision of credit losses recorded in the first nine months of 2006. The $24.1 million increase in interest income resulted from the $358.5 million increase in average earning assets and an increase in average yield on earning assets to 6.20% for the nine months of 2007 from 6.00% for the same period in 2006. The $33.0 million increase in interest expense resulted from a $419.7 million increase in average interest-bearing liabilities and an increase in the average rate paid on interest-bearing liabilities to 4.18% for the nine months of 2007 from 3.51% for the same period in 2006.

The major reason for the decrease in net interest income was the flattening of the yield curve and its effect on our liabilities. Our interest-bearing liabilities are comprised of customer deposits and borrowings from primarily the FHLB or other correspondent banks. The borrowings are at market rates and have reset upwards as rates have risen. As a result of increased competition, our rates on customer deposits have risen also, but slower than rates on borrowings. In September 2007, the Federal Reserve reduced the target Fed Funds Rate to 4.75% from 5.25%. This change slightly increased our net interest margin for September 2007 due to our ability to reprice our deposits and over-night borrowings downward. This allowed us to compensate for the more than $850 million in variable rate loans which also began to reprice at lower rates.

Interest income totaled $255.8 million for the first nine months of 2007. This represented an increase of $24.1 million, or 10.39%, compared to total interest income of $231.7 million for the same period last year. The increase in interest income was primarily the result of the increase in average earning assets from $5.31 billion in the nine months of 2006 to $5.67 billion in the same period in 2007. This represents a 6.75% increase for the nine months of 2007 over the same period last year. In addition, average yield on earning assets increased by 20 basis points for the first nine months of 2007 compared with the same period last year.

Interest expense totaled $136.0 million for the first nine months of 2007. This represented an increase of $33.0 million, or 31.97%, over total interest expense of $103.1 million for the same period last year. The increase in interest expense was primarily the result of an increase in average interest-bearing liabilities from $3.90 billion to $4.32 billion, and an increase in the cost of these liabilities by 67 basis points.

For the third quarter ended September 30, 2007, the Company s net interest income, after provision for credit losses, totaled $41.7 million. This represented an increase of $1.2 million, or 3.03%, over net interest income of $40.5 million for the same period in 2006. The increase in net interest income of $1.2 million for the third quarter of 2007 resulted from an increase of $5.1 million in interest income, offset by a $5.1 million increase in interest expense and $1.2 million provision of credit losses recorded in the third quarter of 2006. The increase in interest income of $5.1 million resulted from the increase in average earning assets of $176.0 million and an increase in the average yield on earning assets to 6.28% for the

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third quarter of 2007 from 6.13% the same period in 2006. The increase of $5.1 million in interest expense resulted from the increase in the average rate paid on interest-bearing liabilities to 4.16% for the third quarter of 2007 from 3.90% the same period in 2006 and a $218.5 million increase in average interest-bearing liabilities.

Interest income totaled $87.9 million for the third quarter of 2007. This represented an increase of $5.1 million, or 6.18%, compared to total interest income of $82.8 million for the same period last year. The increase in interest income for the third quarter ending September 30, 2007 as compared to the third quarter ending September 30, 2006 was primarily the result of the increase in average earning assets of $176.0 million and an increase in the average yield on earning assets of 15 basis points between the third quarter of 2007 and the third quarter of 2006.

Interest expense totaled $46.2 million for the third quarter of 2007. This represented an increase of $5.1 million or 12.53%, over total interest expense of $41.0 million for the same period last year. The increase in interest expense for the third quarter ending September 30, 2007 as compared to the third quarter ending September 30, 2006 was primarily the result of the increase in average interest bearing liabilities of $218.5 million and an increase of 26 basis points in the average yield paid on interest-bearing liabilities.

Table 1 shows the average balances of assets, liabilities, and stockholders equity and the related interest income, expense, and yields/rates for the nine-month and three-month periods ended September 30, 2007 and 2006. Yields for tax-preferenced investments are shown on a taxable equivalent basis using a 35% tax rate.

| | Nine-month period ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | |
| ASSETS | Average Balance | Interest | Average Rate | Average Balance | Interest | Average Rate |
| | (amounts in thousands) | | | | | |
| Investment Securities | | | | | | |
| Taxable | $1,746,192 | $ 65,401 | 5.00% | $1,885,771 | $ 66,625 | 4.72% |
| Tax preferenced (1) | 663,680 | 22,029 | 5.92% | 591,343 | 19,563 | 5.94% |
| Investment in FHLB stock | 81,041 | 3,152 | 5.19% | 73,333 | 2,672 | 4.86% |
| Federal Funds Sold & Interest Bearing | | | | | | |
| Deposits with other institutions | 2,010 | 92 | 6.10% | 2,464 | 92 | 4.98% |
| Loans (2) (3) | 3,178,242 | 165,117 | 6.95% | 2,759,778 | 142,769 | 6.92% |
| Total Earning Assets | 5,671,165 | 255,791 | 6.20% | 5,312,689 | 231,721 | 6.00% |
| Total Non Earning Assets | 380,047 | | | 360,633 | | |
| Total Assets | $6,051,212 | | | $5,673,322 | | |
| | | | | | | |
| LIABILITIES AND STOCKHOLDERS EQUITY | | | | | | |
| Savings Deposits (4) | $1,290,946 | $ 24,531 | 2.54% | $1,210,910 | $ 18,769 | 2.07% |
| Time Deposits | 854,353 | 29,000 | 4.54% | 939,699 | 29,629 | 4.22% |
| Total Deposits | 2,145,299 | 53,531 | 3.34% | 2,150,609 | 48,398 | 3.01% |
| Other Borrowings | 2,174,278 | 82,505 | 5.00% | 1,749,222 | 54,682 | 4.12% |
| Interest Bearing Liabilities | 4,319,577 | 136,036 | 4.18% | 3,899,831 | 103,080 | 3.51% |

| | Nine-month period ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| Non-interest bearing deposits | 1,289,429 | | | 1,358,135 | | |
| Other Liabilities | 43,210 | | | 62,800 | | |
| Stockholders Equity | 398,996 | | | 352,556 | | |
| Total Liabilities and Stockholders Equity | $6,051,212 | | | $5,673,322 | | |
| Net interest income | | $119,755 | | | $128,641 | |
| Net interest spread tax equivalent | | | 2.02% | | | 2.49% |
| Net interest margin | | | 2.84% | | | 3.26% |
| Net interest margin tax equivalent | | | 3.02% | | | 3.42% |
| Net interest margin excluding loan fees | | | 2.79% | | | 3.18% |
| Net interest margin excluding loan fees tax equivalent | | | 2.92% | | | 3.30% |

(1) Includes tax-exempt income of $7.4 million for 2007 and $6.4 million for 2006. Non tax equivalent rate was 4.43% for 2007 and 4.47% for 2006.

(2) Loan fees are included in total interest income as follows, (000)s omitted: 2007, $4,106; 2006, $4,633

(3) Non performing loans are included in net loans as follows, (000)s omitted: 2007, $3,474; 2006, $0

(4) Includes interest bearing demand and money market accounts



| | Three-month period ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | |
| ASSETS | Average Balance | Interest | Average Rate | Average Balance | Interest | Average Rate |
| | (amounts in thousands) | | | | | |
| Investment Securities | | | | | | |
| Taxable | $1,643,382 | $20,591 | 5.02% | $2,018,439 | $24,725 | 4.99% |
| Tax preferenced (1) | 671,883 | 7,493 | 5.97% | 602,341 | 6,510 | 5.81% |
| Investment in FHLB stock | 81,410 | 1,047 | 5.03% | 75,118 | 958 | 4.99% |
| Federal Funds Sold & Interest Bearing | | | | | | |
| Deposits with other institutions | 5,377 | 72 | 5.24% | 32 | 6 | 73.37% |
| Loans (2) (3) | 3,327,462 | 58,677 | 7.00% | 2,857,573 | 50,564 | 7.02% |
| Total Earning Assets | 5,729,514 | 87,880 | 6.28% | 5,553,503 | 82,763 | 6.13% |
| Total Non Earning Assets | 399,936 | | | 378,083 | | |
| Total Assets | $6,129,450 | | | $5,931,586 | | |
| LIABILITIES AND STOCKHOLDERS EQUITY | | | | | | |

| | Three-month period ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| Savings Deposits (4) | $1,299,069 | $ 8,218 | 2.51% | $1,201,319 | $ 7,137 | 2.36% |
| Time Deposits | 901,710 | 10,227 | 4.50% | 1,032,525 | 11,766 | 4.52% |
| Total Deposits | 2,200,779 | 18,445 | 3.33% | 2,233,844 | 18,903 | 3.36% |
| Other Borrowings | 2,165,624 | 27,727 | 5.01% | 1,914,016 | 22,130 | 4.52% |
| Interest Bearing Liabilities | 4,366,403 | 46,172 | 4.16% | 4,147,860 | 41,033 | 3.90% |
| Non-interest bearing deposits | 1,316,035 | | | 1,344,239 | | |
| Other Liabilities | 47,069 | | | 87,216 | | |
| Stockholders Equity | 399,943 | | | 352,271 | | |
| Total Liabilities and Stockholders Equity | $6,129,450 | | | $5,931,586 | | |
| Net interest income | | $41,708 | | | $41,730 | |
| Net interest spread tax equivalent | | | 2.12% | | | 2.23% |
| Net interest margin | | | 2.93% | | | 3.04% |
| Net interest margin tax equivalent | | | 3.11% | | | 3.20% |
| Net interest margin excluding loan fees | | | 2.94% | | | 3.05% |
| Net interest margin excluding loan fees tax equivalent | | | 2.99% | | | 3.09% |

(1) Includes tax-exempt income of $2.5 million for 2007 and $2.2 million for 2006. Non tax equivalent rate was 4.46% for 2007 and 4.84% for 2006.

(2) Loan fees are included in total interest income as follows, (000)s omitted: 2007, $1,726; 2006, $1,600

(3) Non performing loans are included in net loans as follows, (000)s omitted: 2007, $3,474; 2006, $0

(4) Includes interest bearing demand and money market accounts

As stated above, the net interest margin measures net interest income as a percentage of average earning assets. Our tax effected (TE) net interest margin was 3.02% for the nine months of 2007, compared to 3.42% for the nine months of 2006. The decrease in the net interest margin as compared with the first nine months of 2006 is the result of the increasing interest rate environment, which impacted interest earned and interest paid as a percent of earning assets. Although the yield on earning assets increased, this was offset by higher interest paid on interest-bearing liabilities.

It is difficult to attribute the net interest margin changes to any one factor. However, the banking and financial services businesses in our market areas are highly competitive. This competition has an influence on the strategies we employ. The general increase in interest rates had an impact on interest earned and interest paid as a percent of earning assets. Rates on deposits have risen due to increased competition. In addition, our cost of borrowings has increased due to lower cost borrowings maturing and being replaced with higher cost borrowings.

Our average non-interest-bearing deposits for the nine-month period ended September 30, 2007 declined as compared with our average non-interest-bearing deposits for the nine-month period ended September 30, 2006. This was due primarily to the competition for these types of deposits. As a result, we needed to borrow more funds, increasing our costs and decreasing our net interest income.

The decline in net interest margin is due to the cost of interest-bearing liabilities rising faster than the increase in yields on earning assets. This decline in net interest margin has been mitigated by the growth in the balance sheet. Average earning assets increased from $5.31 billion for the nine months ended September 30, 2006 to $5.67 billion for the nine months ended September 30, 2007. This represents an increase of 6.75%.

The net interest spread is the difference between the yield on average earning assets and the cost of average interest-bearing liabilities. The net interest spread is an indication of our ability to manage interest rates received on loans and investments and paid on deposits and borrowings in a competitive and changing interest rate environment. Our net interest spread (TE) was 2.02% for the nine months of 2007 and 2.49% for the same period last year. The decrease in the net interest spread for the nine months ended September 30, 2007 resulted from a 20 basis point increase in the yield on earning assets offset by a 67 basis point increase in the cost of interest-bearing liabilities, thus generating a 47 basis point decrease in the net interest spread from the same period last year.

For the third quarter of 2007 the Company s net interest spread (TE) was 2.12% as compared to 2.23% for the same period last year. The decrease in the net interest spread for the third quarter ended September 30, 2007 resulted from a 26 basis point increase in the cost of interest-bearing liabilities offset by a 15 basis point increase in the yield on earning assets, thus generating a 11 basis point decrease in the net interest spread over the same period last year.

The yield (TE) on earning assets increased to 6.20% for the nine months of 2007, from 6.00% for the same period last year, and reflects an increasing interest rate environment and a change in the mix of earning assets. Average loans as a percent of earning assets increased to 56.04% in the nine months of 2007 from 51.95% for the same period in 2006. Average investments as a percent of earning assets decreased to 42.49% in the nine months of 2007 from 46.63% for the same period in 2006. The yield on loans for the first nine months of 2007 increased to 6.95% as compared to 6.92% for the same period in 2006 as a result of the growth in average loans and the increasing interest rate environment during that period. The yield (TE) on investments for the first nine months of 2007 increased to 5.25% compared to 5.01% for the same period in 2006 as a result of an increase in interest rates.

The cost of average interest-bearing liabilities increased to 4.18% for the first nine months of 2007 as compared to 3.51% for the same period in 2006, reflecting the continued increase in interest rates and a change in the mix of interest-bearing liabilities. Average borrowings as a percent of average interest-bearing liabilities increased to 50.34% during the first nine months of 2007 as compared to 44.85% for the same period in 2006. The cost of borrowings for the first nine months of 2007 increased to 5.00% as compared to 4.12% for the same period in 2006, reflecting the continued increase in interest rates. Borrowings typically have a higher cost than interest-bearing deposits. The cost of interest-bearing deposits for the first nine months of 2007 increased to 3.34% as compared to 3.01% for the same period in 2006, also reflecting the continued increase in interest rates and the competition for interest-bearing deposits. The FDIC has approved the payment of interest on certain demand deposit accounts. This could have a negative impact on our net interest margin, net interest spread, and net earnings, should this be implemented fully. Currently, we pay interest on NOW and Money Market Accounts.

Table 2 presents a comparison of interest income and interest expense resulting from changes in the volumes and rates on average earning assets and average interest-bearing liabilities for the years indicated. Changes in interest income or expense attributable to volume changes are calculated by multiplying the change in volume by the initial average interest rate. The change in interest income or expense attributable to changes in interest rates is calculated by multiplying the change in interest rate by the initial volume. The changes attributable to both interest rate and volume changes are calculated by multiplying the change in rate times the change in volume.



| | Comparison of nine months ended September 30, 2007 Compared to 2006 Increase (Decrease) Due to | | | |
|---|---|---|---|---|
| | Volume | Rate | Rate/ Volume | Total |
| | (amounts in thousands) | | | |
| Interest Income: | | | | |
| Taxable investment securities | $ (4,919) | $ 3,959 | $ (264) | $ (1,224) |
| Tax-advantaged securities | 3,172 | (89) | (617) | 2,466 |
| Fed funds sold & interest-bearing deposits with other institutions | (17) | 21 | (4) | |
| Investment in FHLB stock | 281 | 181 | 18 | 480 |
| Loans | 21,659 | 619 | 70 | 22,348 |
| Total interest on earning assets | 20,176 | 4,691 | (797) | 24,070 |

| | Comparison of nine months ended September 30, 2007 Compared to 2006 Increase (Decrease) Due to | | | |
|---|---|---|---|---|
| Interest Expense: | | | | |
| Savings deposits | 1,239 | 4,257 | 286 | 5,782 |
| Time deposits | (2,694) | 2,249 | (204) | (649) |
| Other borrowings | 13,280 | 11,673 | 2,870 | 27,823 |
| Total interest on interest-bearing liabilities | 11,825 | 18,179 | 2,952 | 32,956 |
| Net Interest Income | $ 8,351 | $ (13,488) | $ (3,749) | $ (8,886) |

| | Comparison of quarters ended September 30, 2007 Compared to 2006 Increase (Decrease) Due to | | | |
|---|---|---|---|---|
| | Volume | Rate | Rate/ Volume | Total |
| | (amounts in thousands) | | | |
| Interest Income: | | | | |
| Taxable investment securities | $ (4,659) | $ 151 | $ 374 | $ (4,134) |
| Tax-advantaged securities | 1,003 | 241 | (261) | 983 |
| Fed funds sold & interest-bearing deposits with other institutions | 980 | (5) | (909) | 66 |
| Investment in FHLB stock | 78 | 8 | 3 | 89 |
| Loans | 8,314 | (144) | (57) | 8,113 |
| Total interest on earning assets | 5,716 | 251 | (850) | 5,117 |
| Interest Expense: | | | | |
| Savings deposits | 581 | 454 | 46 | 1,081 |
| Time deposits | (1,490) | (52) | 3 | (1,539) |
| Other borrowings | 2,906 | 2,397 | 294 | 5,597 |
| Total interest on interest-bearing liabilities | 1,997 | 2,799 | 343 | 5,139 |
| Net Interest Income | $ 3,719 | $ (2,548) | $ (1,193) | $ (22) |

***Interest and Fees on Loans***

Our major source of revenue and primary component of interest income is interest and fees on loans. Interest and fees on loans totaled $165.1 million for the first nine months of 2007. This represented an increase of $22.3 million, or 15.65%, over interest and fees on loans of $142.8 million for the same period in 2006. The increase in interest and fees on loans for the first nine months of 2007 reflects increases in the average balance of loans and the increase in interest rates between periods. The yield on loans increased to 6.95% for the first nine months of 2007, compared to 6.92% for the same period in 2006. Average loans increased 15.16% from $2.76 billion for the first nine months of 2006 to $3.18 billion for the first nine months of 2007.



Interest and fees on loans totaled $58.7 million for the third quarter of 2007. This represented an increase of $8.1 million, or 16.04%, over interest and fees on loans of $50.6 million for the same period in 2006. The increase was primarily due to increases in the average balance of

loans and an increase in interest rates during 2007.

In general, we stop accruing interest on a loan after its principal or interest becomes 90 days or more past due. When a loan is placed on nonaccrual, all interest previously accrued but not collected is charged against earnings. There was no interest income that was accrued and not reversed on non-performing loans at September 30, 2007 and 2006.

Fees collected on loans are an integral part of the loan pricing decision. Loan fees and the direct costs associated with the origination of loans are deferred and deducted from the loan balance. Deferred net loan fees are recognized in interest income over the term of the loan using the effective yield method. We recognized loan fee income of $4.1 million for the first nine months of 2007, as compared to $4.6 million for the same period in 2006, a decrease of $527,000 or 11.38%.

***Interest on Investments***

The second most important component of interest income is interest on investments, which totaled $90.7 million for the first nine months of 2007. This represented an increase of $1.7 million, or 1.94%, over interest on investments of $89.0 million for the same period in 2006. The increase in interest on investments for the nine months of 2007 over the same period last year reflected the increase in interest rates partially offset by decreases in average balances. The interest rate environment and the investment strategies we employ directly affect the yield on the investment portfolio. We continually adjust our investment strategies in response to the changing interest rate environment in order to maximize the rate of total return consistent within prudent risk parameters, and to minimize the overall interest rate risk of the Company. The weighted-average yield (TE) on investments increased to 5.25% for the nine months of 2007, compared to 5.01% for the same period in 2006 as a result of the increase in interest rates.

For the third quarter of 2007, interest income on investments totaled $29.2 million. This represented a decrease of $3.0 million, or 9.30%, from interest on investments of $32.2 million for the same period in 2006. The decrease in interest on investments for the third quarter of 2007 from the same period last year reflected decreases in the average balance of investments by $293.9 million, or 10.90%. This was offset by an increase in interest rates. The weighted-average yield (TE) on investments increased to 5.29% for the third quarter of 2007, compared to 5.18% for the same period in 2006.

***Provision for Credit Losses***

We maintain an allowance for inherent credit losses that is increased by a provision for credit losses charged against operating results. The provision for credit losses is determined by management as the amount to be added to the allowance for probable credit losses after net charge-offs have been deducted to bring the allowance to an adequate level which, in management s best estimate, is necessary to absorb probable credit losses within the existing loan portfolio. We did not make a provision for credit losses during the first nine months of 2007. We acquired loans with $2.7 million of loan loss reserve from the FCB acquisition in June 2007. We made a provision for credit losses of $2.4 million and $1.2 million during the first nine-months and three-months ended September 30, 2006. We believe the allowance is appropriate. The ratio of the allowance for credit losses to total loans as of September 30, 2007 and 2006 was 0.92%. No assurance can be given that economic conditions which adversely affect the Company s service areas or other circumstances will not be reflected in increased provisions for credit losses in the future. The nature of this process requires considerable judgment. The net recoveries totaled $20,000 for the first nine months of 2007 and $1.3 million during the same period of 2006. See Risk Management Credit Risk herein.



***Other Operating Income***

Other operating income for the Company includes income derived from special services offered by the Bank, such as CitizensTrust, merchant card, international banking, and other business services. Also included in other operating income are service charges and fees, primarily from deposit accounts; gains (net of losses) from the sale of investment securities, other real estate owned, and fixed assets; and other revenues not included as interest on earning assets.

Other operating income totaled $23.4 million for the first nine months of 2007. This represents a decrease of $1.3 million, or 5.40%, from other operating income of $24.7 million for the same period in 2006. Other operating income as a percent of net revenues (net interest income before loan loss provision plus other operating income) was 16.32% for the first nine months of 2007, as compared to 16.10% for the same period in 2006.

***Other Operating Expenses***

Other operating expenses for the Company include expenses for salaries and benefits, occupancy, equipment, stationary and supplies, professional services, amortization of intangibles, and other expenses. Other operating expenses totaled $78.0 million for the first nine months of 2007. This represents an increase of $7.6 million, or 10.81% over other operating expenses of $70.4 million for the same period in 2006.

For the third quarter of 2007, other operating expenses totaled $27.2 million. This represents an increase of $4.6 million, or 20.27% over other operating expenses of $22.6 million for the same period last year.

The increases in other operating expenses for the third quarter and for the nine months ending September 30, 2007 were primarily due to the increases in salary and occupancy expenses related to the acquisition of FCB. In addition, intangible expense increased by $498,000 for the estimated amortization of intangibles acquired from FCB. The Company also made a $741,000 provision to the reserve for undisbursed credit commitments in the third quarter of 2007.

At September 30, 2007, we employed 692 full time equivalent employees, compared to 653 full time equivalent employees at September 30, 2006.

For the most part, other operating expenses reflect the direct expenses and related administrative expenses associated with staffing, maintaining, promoting, and operating branch facilities. Our ability to control other operating expenses in relation to asset growth can be measured in terms of other operating expenses as a percentage of average assets. Operating expenses measured as a percentage of average assets was 1.72% and 1.66% for the first nine months of 2007 and 2006, respectively.

Our ability to control other operating expenses in relation to the level of net revenue (net interest income plus other operating income) is measured by the efficiency ratio and indicates the percentage of net revenue that is used to cover expenses. For the first nine months of 2007, the efficiency ratio was 54.48%, compared to a ratio of 46.62% for the same period in 2006. The increase was primarily due to the decrease in net interest income while our operating expenses increased 10.81% over the same period last year.

For the third quarter of 2007, the efficiency ratio increased to 54.91% as compared to 45.86% for the same period last year. The increase is primarily attributed to an increase in operating expenses of 20.27% over the same period last year due to the FCB acquisition and the provision to the reserve for undisbursed credit commitments in the third quarter of 2007.



***Income Taxes***

The Company s effective tax rate for the nine months of 2007 was 27.52%, compared to 32.13% for the same period in 2006. The effective tax rates are below the nominal combined Federal and State tax rates as a result of the increase in tax-preferenced income from certain investments and municipal loans/leases as a percentage of total income for each period. In 2007, the percentage of tax-preferenced income to total income increased, resulting in lower tax rate compared to prior year. The majority of tax preferenced income is derived from municipal securities.

## ANALYSIS OF FINANCIAL CONDITION

The Company reported total assets of $6.16 billion at September 30, 2007. This represented an increase of $65.1 million, or 1.07%, from total assets of $6.09 billion at December 31, 2006. Earning assets totaled $5.75 billion at September 30, 2007. This represented an increase of $48.7 million, or 0.85%, from total earning assets of $5.70 billion at December 31, 2006. Total liabilities were $5.75 billion at September 30, 2007, up $45.7 million, or 0.80%, from total liabilities of $5.70 billion at December 31, 2006. Total equity increased $19.5 million, or 5.03%, to $406.8 million at September 30, 2007, compared with total equity of $387.3 million at December 31, 2006.

***Investment Securities***

The Company reported total investment securities of $2.39 billion at September 30, 2007. This represented a decrease of $192.6 million, or 7.46%, from total investment securities of $2.58 billion at December 31, 2006. This is consistent with our plan of allowing the securities portfolio to roll off by not reinvesting the cash flows. Investment securities comprise 41.55% of the Company s total earning assets at September 30, 2007.

In accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities , securities held as available-for-sale are reported at current market value for financial reporting purposes. The related unrealized gains or losses, net of income taxes, are recorded in stockholders equity. At September 30, 2007, securities held as available-for-sale had a fair market value of $2.39 billion, representing 100% of

total investment securities, with an amortized cost of $2.41 billion. At September 30, 2007, the net unrealized holding loss on securities available-for-sale was $16.7 million and that resulted in accumulated other comprehensive loss of $9.7 million (net of $7.0 million in deferred taxes). At December 31, 2006, the Company reported net unrealized loss on investment securities available-for-sale of $22.8 million and accumulated other comprehensive income of $13.2 million (net of deferred taxes of $9.6 million).

Table 3 sets forth investment securities at September 30, 2007 and December 31, 2006.

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| | September 30, 2007 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Holding Gain | Gross Unrealized Holding Loss | Market Value | Total Percent |
| | (Amounts in thousands) | | | | |
| Investment Securities Available-for-Sale: | | | | | |
| U.S. Treasury securities | $ 987 | $ 4 | $ | $ 991 | 0.04% |
| Government agency & government-sponsored enterprises | 66,188 | 437 | (106) | 66,519 | 2.78% |
| Mortgage-backed securities | 1,037,604 | 1,764 | (21,380) | 1,017,988 | 42.59% |
| CMO s / REMIC s | 616,264 | 1,762 | (3,459) | 614,567 | 25.71% |
| Municipal bonds | 685,944 | 10,787 | (6,490) | 690,241 | 28.88% |
| Other securities | | | | | 0.00% |
| Total Investment Securities | $2,406,987 | $14,754 | $(31,435) | $2,390,306 | 100.00% |

| | December 31, 2006 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Holding Gain | Gross Unrealized Holding Loss | Market Value | Total Percent |
| | (Amounts in thousands) | | | | |
| Investment Securities Available-for-Sale: | | | | | |
| U.S. Treasury securities | $ 971 | $ | $ (1) | $ 970 | 0.04% |
| Government agency & government-sponsored enterprises | 68,679 | 124 | (503) | 68,300 | 2.64% |
| Mortgage-backed securities | 1,103,664 | 1,793 | (27,606) | 1,077,851 | 41.73% |
| CMO s / REMIC s | 791,265 | 2,589 | (6,584) | 787,270 | 30.48% |
| Municipal bonds | 638,391 | 12,249 | (4,855) | 645,785 | 25.00% |
| Other securities | 2,726 | | | 2,726 | 0.11% |
| Total Investment Securities | $2,605,696 | $16,755 | $(39,549) | $2,582,902 | 100.00% |

The weighted-average yield (TE) on the investment portfolio at September 30, 2007 was 4.91% with a weighted-average life of 4.7 years. This compares to a yield of 4.61% at December 31, 2006 with a weighted-average life of 4.7 years and a yield of 5.01% at September 30, 2006 with a weighted-average life of 4.5 years. The weighted average life is the average number of years that each dollar of unpaid principal due remains outstanding. Average life is computed as the weighted-average time to the receipt of all future cash flows, using as the weights the dollar amounts of the principal paydowns.

Approximately 68% of the portfolio represents securities issued by the U.S government or U.S. government-sponsored enterprises, which guarantee payment of principal and interest.

The remaining CMO/REMICs are backed by agency-pooled collateral or whole loan collateral. All non-agency CMO/REMIC issues held are rated AAA by either Standard & Poor s or Moody s, as of September 30, 2007 and December 31, 2006.

| | September 30, 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 months | | 12 months or longer | | Total | |
| | Fair Value | Gross Unrealized Holding Losses | Fair Value | Gross Unrealized Holding Losses | Fair Value | Gross Unrealized Holding Losses |
| Description of Securities | (amounts in thousands) | | | | | |
| U.S. Treasury Obligation | $ | $ | $ | $ | $ | $ |
| Government agency & government-sponsored enterprises | | | 10,375 | 106 | 10,375 | 106 |
| Mortgage-backed securities | 97,333 | 841 | 757,768 | 20,539 | 855,101 | 21,380 |
| CMO/REMICs | 91,235 | 487 | 315,918 | 2,972 | 407,153 | 3,459 |
| Municipal bonds | 319,309 | 4,632 | 75,509 | 1,858 | 394,818 | 6,490 |
| | $507,877 | $5,960 | $1,159,570 | $25,475 | $1,667,447 | $31,435 |



| | December 31, 2006 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 months | | 12 months or longer | | Total | |
| | Fair Value | Gross Unrealized Holding Losses | Fair Value | Gross Unrealized Holding Losses | Fair Value | Gross Unrealized Holding Losses |
| Description of Securities | (amounts in thousands) | | | | | |
| U.S. Treasury & Government Securities | $ 970 | $ 1 | $ | $ | $ 970 | $ 1 |
| Government agency & government-sponsored enterprises | 12,040 | 45 | 41,101 | 458 | 53,141 | 503 |
| Mortgage-backed securities | 74,274 | 388 | 880,162 | 27,218 | 954,436 | 27,606 |
| CMO/REMICs | 53,681 | 241 | 454,693 | 6,343 | 508,374 | 6,584 |
| Municipal bonds | 276,512 | 3,474 | 60,065 | 1,381 | 336,577 | 4,855 |
| | $417,477 | $4,149 | $1,436,021 | $35,400 | $1,853,498 | $39,549 |

The tables above show the Company s investment securities gross unrealized losses and fair value by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2007 and December 31, 2006. The Company has reviewed individual securities classified as available-for-sale to determine whether a decline in fair value below the amortized cost basis is other-than-temporary. If it is probable that the Company will be unable to collect all amounts due according to the contractual terms of a debt security not impaired at acquisition, an other-than-temporary impairment shall be considered to have occurred. If an other-than-temporary impairment occurs, the cost basis of the security would be written down to its fair value as a new cost basis and the write down accounted for as a realized loss.

The following summarizes our analysis of these securities and the unrealized losses. This assessment was based on the following factors: i) the length of the time and the extent to which the market value has been less than cost; ii) the financial condition and near-term prospects of the issuer; iii) the intent and ability of the Company to retain its investment in a security for a period of time sufficient to allow for any anticipated recovery in market value; and iv) general market conditions which reflect prospects for the economy as a whole, including interest rates and

sector credit spreads.

*U.S. Treasury Obligations and Government Agency & Government Sponsored Enterprises* The U.S. Treasury Obligations and government agency are backed by the full faith and credit of the U.S. Treasury and Agencies of the U.S. Government. These securities are bullet securities, that is, they have a defined maturity date on which the principal is paid. The contractual term of these investments provides that the Bank will receive the face value of the bond at maturity which will equal the amortized cost of the bond. Interest is received throughout the life of the security. At September 30, 2007, the unrealized loss greater than 12 months of $106,000 is comprised of one FNMA issue. This security matures within 1 year. The agencies are rated AAA and, although FNMA has had some accounting difficulties in the past few years, this has not impacted its credit worthiness. Because the decline in market value is attributable to the changes in interest rates and not credit quality, and the Bank has the ability and intent to hold this security until recovery of fair value, which may be at maturity, the Bank does not consider this investment to be other than temporarily impaired at September 30, 2007.

*Mortgaged-Backed Securities and CMO/REMICs* Almost all of the mortgage-backed and CMO/REMICs securities are issued by the government sponsored enterprises such as Ginnie Mae, Fannie Mac and Freddie Mac. These securities are collateralized or backed by the underlying mortgages. All mortgage-backed securities are rated AAA with average life of approximately 3.3 years. The contractual cash flows of 96.3% of these investments are guaranteed by agencies of the U.S. government. The remaining 3.7% are issued by banks. Accordingly, it is expected the securities would not be settled at a price less than the amortized cost of the bond. The unrealized loss greater than 12 months on these securities at September 30, 2007 is $23.5 million. This loss is comprised of three main blocks of securities: FNMA s with a loss of $12.0 million, Freddie Mac with a loss of $10.6 million and non-government sponsored enterprises such as financial institutions with a loss of $854,000. Because we believe the decline in market value is attributable to the changes in interest rates and not



credit quality, and the Company has the ability and intent to hold these securities until recovery of fair value, which may be at maturity, management does not consider these investments to be other than temporarily impaired at September 30, 2007.

*Municipal Bonds* The municipal bonds in the Bank s portfolio are all rated AAA and they are insured by the largest bond insurance companies with maturities of approximately 8.4 years. The unrealized loss greater than 12 months on these securities at September 30, 2007 is $1.9 million. As with the other securities in the portfolio, we believe this loss is due to the rising rate environment and not the credit risk of these securities. The Bank diversifies its holdings by owning selections of securities from different issuers and by holding securities from geographically diversified municipal issuers, thus reducing the Bank s exposure to any single adverse event. Because the decline in market value is attributable to the changes in interest rates and not credit quality, and the Bank has the ability and intent to hold these securities until recovery of fair value, which may be at maturity, the Bank does not consider these investments to be other than temporarily impaired at September 30, 2007.

Although we do not feel these securities are other-than-temporarily impaired, we will continue to monitor the available-for-sale portfolio in the light of economic, credit and market factors. In addition, we will look at the potential for improving the overall performance of the portfolio and the income of the Company. Accordingly, subsequent changes in some of these factors may indicate that we should sell some of these securities even though we have disclosed that we currently intend to hold these securities to maturity.

At September 30, 2007 and December 31, 2006, investment securities having an amortized cost of approximately $2.31 billion and $2.44 billion respectively, were pledged to secure public deposits, short and long-term borrowings, and for other purposes as required or permitted by law.

***Loans***

At September 30, 2007, we reported total loans, net of deferred loan fees, of $3.31 billion. This represents an increase of $241.6 million, or 7.87%, over total loans, net of deferred loan fees, of $3.07 billion at December 31, 2006. Total loans, net of deferred loan fees, comprise 57.57% of our total earning assets.

| | **September 30, 2007** | | **December 31, 2006** | |
|---|---|---|---|---|
| Commercial and Industrial | $ 345,697 | 10.4% | $ 264,416 | 8.6% |
| Real Estate: | | | | |
| Construction | 307,506 | 9.3% | 299,112 | 9.7% |
| Commercial Real Estate | 1,775,812 | 53.4% | 1,642,370 | 53.3% |
| SFR Mortgage | 363,765 | 10.9% | 284,725 | 9.2% |

| | September 30, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| Consumer | 62,979 | 1.9% | 54,125 | 1.8% |
| Municipal lease finance receivables | 143,399 | 4.3% | 126,393 | 4.1% |
| Auto and equipment leases, net of unearned discount | 58,958 | 1.8% | 51,420 | 1.7% |
| Dairy and Livestock | 265,806 | 8.0% | 358,259 | 11.6% |
| Gross Loans | 3,323,922 | 100.0% | 3,080,820 | 100.0% |
| Less: | | | | |
| Allowance for credit losses | (30,428) | | (27,737) | |
| Deferred net loan fees | (12,173) | | (10,624) | |
| Net Loans | $3,281,321 | | $3,042,459 | |

Commercial and industrial loans are loans and leases to commercial entities to finance capital purchases or improvements, or to provide cash flow for operations. Real estate loans are loans secured by conforming first trust deeds on real property, including property under construction, commercial property and single family and multifamily residences. Consumer loans include installment loans to consumers as well as home equity loans and other loans secured by junior liens on real property. Municipal lease



finance receivables are leases to municipalities. Dairy and livestock loans are loans to finance the operating needs of wholesale dairy farm operations, cattle feeders, livestock raisers, and farmers.

***Non-performing Assets***

We had non-performing assets of $3.5 million at September 30, 2007. Non-performing assets represent 0.10% of total loans and 0.06% of total assets at September 30, 2007. We had no non-performing assets at December 31, 2006. Non-performing assets include non-performing loans plus other real estate owned (foreclosed property). Non-performing loans include non-accrual loans, loans past due 90 or more days and still accruing interest, and restructured loans. We had $2.9 million loans classified as impaired at September 30, 2007. There were no loans classified as impaired at December 31, 2006. Impaired loans measured 0.09% of gross loans as of September 30, 2007.

With the exception of assets discussed above, we are not aware of any other loans as of September 30, 2007 for which known credit problems of the borrower would cause serious doubts as to the ability of such borrowers to comply with their present loan repayment terms, or any known events that would result in the loan being designated as non-performing at some future date. We cannot, however, predict the extent to which the deterioration in general economic conditions, real estate values, increase in general rates of interest, change in the financial conditions or business of a borrower may adversely affect a borrower s ability to pay. See Risk Management Credit Risk herein.

At September 30, 2007 and December 31, 2006, the Company held no properties as other real estate owned.

***Deposits***

The primary source of funds to support earning assets (loans and investments) is the generation of deposits from our customer base. The ability to grow the customer base and subsequently deposits is a crucial element in the performance of the Company.

At September 30, 2007, total deposits were $3.43 billion, representing an increase of $28.3 million, or 0.83%, from total deposits of $3.41 billion at December 31, 2006. Average total deposits for the nine months of 2007 were $3.43 billion. The comparison of average balances for the nine months of 2007 has historically been more representative of our Company s growth in deposits as it excludes the historical seasonal peak in deposits at year-end. The composition of deposits is as follows:

| | September 30, 2007 | December 31, 2006 |
|---|---|---|
| | (Amounts in thousands) | |
| Non-interest bearing deposits | | |

| | September 30, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| Demand deposits | $1,292,825 | 37.6% | $1,363,411 | 40.0% |
| Interest bearing deposits | | | | |
| Savings Deposits | 1,278,939 | 37.3% | 1,215,419 | 35.7% |
| Time deposits | 863,323 | 25.1% | 827,978 | 24.3% |
| Total deposits | $3,435,087 | 100.0% | $3,406,808 | 100.0% |

The amount of non-interest-bearing demand deposits in relation to total deposits is an integral element in achieving a low cost of funds. Demand deposits totaled $1.29 billion at September 30, 2007, representing a decrease of $70.6 million, or 5.18%, from total demand deposits of $1.36 billion at December 31, 2006. Non-interest-bearing demand deposits represented 37.64% of total deposits as of September 30, 2007 and 40.02% of total deposits as of December 31, 2006.



Savings deposits, which include savings, interest-bearing demand, and money market accounts, totaled $1.28 billion at September 30, 2007, representing an increase of $63.5 million, or 5.23%, over savings deposits of $1.22 billion at December 31, 2006.

Time deposits totaled $863.3 million at September 30, 2007. This represented an increase of $35.3 million, or 4.27%, over total time deposits of $828.0 million at December 31, 2006.

***Other Borrowed Funds***

To achieve the desired growth in earning assets and to fully utilize our capital, we fund this growth through generating sources of funds other than deposits. The first source of funds we pursue is non-interest-bearing deposits (the lowest cost of funds to the Company). Next we pursue the growth in interest-bearing deposits and finally we supplement the growth in deposits with borrowed funds. Average borrowed funds, as a percent of average total funding (total deposits plus demand notes plus borrowed funds) was 37.53% as of September 30, 2007, as compared to 38.65% as of December 31, 2006.

During 2007 and 2006, we entered into short-term borrowing agreements (borrowings with maturities of less than one year) with the Federal Home Loan Bank (FHLB) and other institutions. The Bank had outstanding balances of $340.5 million and $1.09 billion under these agreements at September 30, 2007 and December 31, 2006, respectively. The decrease is due to borrowings maturing during the first nine months of 2007. The weighted average annual interest rate was 5.10% and 4.47% at September 30, 2007 and December 31, 2006, respectively. The FHLB holds certain investment securities of the Bank as collateral for these borrowings.

In June 2006, the Company purchased securities totaling $250.0 million. This purchase was funded by a repurchase agreement of $250.0 million with a double cap embedded in the repurchase agreement. The interest rate on this agreement is tied to three-month LIBOR and reset quarterly. In November 2006, we began a repurchase agreement product with our customers. This product, known as Citizens Sweep Manager, sells our securities overnight to our customers under an agreement to repurchase them the next day. Total funds borrowed under both of these repurchase agreements were $580.7 million as of September 30, 2007 and $344.4 million as of December 31, 2006, respectively. The weighted average annual interest rate was 4.38% and 5.81% at September 30, 2007 and December 31, 2006, respectively.

We also entered into long-term borrowing agreements (borrowings with maturities of one year or longer) with the FHLB. We had outstanding balances of $1.20 billion and $700.0 million under these agreements at September 30, 2007 and December 31, 2006, respectively. The weighted average annual interest rate was 4.87% and 4.90% at September 30, 2007 and December 31, 2006, respectively. The FHLB holds certain investment securities of the Bank as collateral for these borrowings.

The Bank acquired subordinated debt of $5.0 million from the acquisition of FCB in June 2007 which is included in long-term borrowings in Item 1 Financial Statements. The debt has a variable interest rate which resets quarterly at three-month LIBOR plus 1.65%. The debt matures on January 7, 2016, but becomes callable on January 7, 2011.

The Bank has an agreement, known as the Treasury Tax & Loan ( TT&L ) Note Option Program with the Federal Reserve Bank and the U.S. Department of Treasury in which federal tax deposits made by depositors can be held by the bank until called (withdrawn) by the U.S. Department of Treasury. The maximum amount of accumulated federal tax deposits allowable to be held by the Bank, as set forth in the

agreement, is $15.0 million. On September 30, 2007 and December 31, 2006 the amounts held by the Bank in the TT&L Note Option Program were $180,000 and $7.2 million, collateralized by securities, respectively. Amounts are payable on demand. The Bank borrows at a variable rate of 98 and 75 basis points less than the average weekly federal funds rate, which was 5.18% and 5.08% at September 30, 2007 and December 31, 2006, respectively.



At September 30, 2007, borrowed funds totaled $2.13 billion, representing a decrease of $20.1 million, or 0.94%, over total borrowed funds of $2.15 billion at December 31, 2006.

***Aggregate Contractual Obligations***

The following table summarizes our contractual commitments as of September 30, 2007:

| | | Maturity by Period | | | |
|---|---|---|---|---|---|
| | **Total** | **Less Than One Year** | **One Year to Three Years** | **Four Year to Five Years** | **After Five Years** |
| | | | (amounts in thousands) | | |
| Deposits | $3,435,087 | $3,413,631 | $ 17,293 | $ 824 | $ 3,339 |
| FHLB and Other Borrowings | 2,126,346 | 671,346 | 1,100,000 | 350,000 | 5,000 |
| Junior Subordinated Debentures | 115,859 | | | | 115,859 |
| Deferred Compensation | 8,228 | 751 | 1,502 | 1,380 | 4,595 |
| Operating Leases | 21,433 | 4,615 | 8,435 | 3,211 | 5,172 |
| Total | $5,706,953 | $4,090,343 | $1,127,230 | $355,415 | $133,965 |

Deposits represent non-interest bearing, money market, savings, NOW, certificates of deposits, brokered and all other deposits.

FHLB borrowings represent the amounts that are due to the Federal Home Loan Bank. These borrowings have fixed maturity dates. Other borrowings represent the amounts that are due to overnight Federal funds purchases, repurchase agreements and TT&L.

Junior subordinated debentures represent the amounts that are due from the Company to CVB Statutory Trust I, CVB Statutory Trust II & CVB Statutory Trust III. The debentures have the same maturity as the Trust Preferred Securities. CVB Statutory Trust I and II, which mature in 2033 and become callable in whole or in part in 2008. CVB Statutory Trust III which matures in 2036 and becomes callable in whole or in part in 2011. It also represents two Trust Preferred Securities acquired through the FCB acquisition in June 2007. FCB Capital Trust I matures in 2028 and is currently callable. FCB Capital Trust II matures in 2033 and becomes callable in 2008.

Deferred compensation primarily represents the amounts that are due to former employees salary continuation agreements as a result of acquisitions.

Operating leases represent the total minimum lease payments under noncancelable operating leases.

***Off-Balance Sheet Arrangements***

At September 30, 2007, we had commitments to extend credit of approximately $857.1 million and obligations under letters of credit of $57.6 million and available lines of credit totaling $1.03 billion from certain institutions. Commitments to extend credit are agreements to lend to customers, provided there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Commitments are generally variable rate, and many of these commitments are expected to expire without being drawn upon. As such, the total commitment amounts do not necessarily represent future cash requirements. The Bank uses the same credit underwriting policies in granting or accepting such commitments or contingent obligations as it does for on-balance-sheet instruments, which consist of evaluating customers creditworthiness individually. The Company has a reserve for undisbursed commitments of $2.5 million as of September 30, 2007.

Standby letters of credit written are conditional commitments issued by the Bank to guarantee the financial performance of a customer to a third party. Those guarantees are primarily issued to support private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. When deemed necessary, the Bank holds appropriate collateral supporting those commitments.

The following table summarizes the off-balance sheet arrangements at September 30, 2007:

| | Maturity by Period |
|---|---|