

PROVIDENT FINANCIAL SERVICES INC  
Form 10-Q  
November 10, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended September 30, 2008

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-31566

**PROVIDENT FINANCIAL SERVICES, INC.**

(Exact Name of Registrant as Specified in Its Charter)

|   |  |
|---|--|
| <b>Delaware</b><br>(State or Other Jurisdiction of<br>Incorporation or Organization)          | <b>42-1547151</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>830 Bergen Avenue, Jersey City, New Jersey</b><br>(Address of Principal Executive Offices) | <b>07306-4599</b><br>(Zip Code)                              |
| <b>(201) 333-1000</b><br>(Registrant's Telephone Number, Including Area Code)                 |  |

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve 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  NO

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company   
Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

As of November 1, 2008 there were 83,209,293 shares issued and 60,049,720 shares outstanding of the Registrant's Common Stock, par value \$0.01 per share, including 438,563 shares held by the First Savings Bank Directors' Deferred Fee Plan not otherwise considered outstanding under U.S. generally accepted accounting principles.

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**PROVIDENT FINANCIAL SERVICES, INC.**

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## Consolidated Statements of Financial Condition

September 30, 2008 (Unaudited) and December 31, 2007

(Dollars in thousands, except share data)

|  | September 30,<br>2008 | December 31,<br>2007 |
|--|-----------------------|----------------------|
| <b><u>ASSETS</u></b>   |                       |                      |
| Cash and due from banks  | \$ 84,970             | \$ 83,737            |
| Federal funds sold   |                       | 18,000               |
| Short-term investments   | 3,664                 | 38,892               |
| <b>Total cash and cash equivalents</b>   | <b>88,634</b>         | <b>140,629</b>       |
| Investment securities held to maturity (market value of \$347,193 (unaudited) and \$359,699 at September 30, 2008 and December 31, 2007, respectively) | 354,112               | 358,491              |
| Securities available for sale, at fair value   | 832,659               | 769,615              |
| Federal Home Loan Bank ( FHLB ) stock  | 43,149                | 39,764               |
| Loans  | 4,378,148             | 4,296,291            |
| Less allowance for loan losses   | 43,329                | 40,782               |
| <b>Net loans</b>   | <b>4,334,819</b>      | <b>4,255,509</b>     |
| Foreclosed assets, net   | 3,556                 | 1,041                |
| Banking premises and equipment, net  | 77,078                | 79,138               |
| Accrued interest receivable  | 23,587                | 24,665               |
| Intangible assets  | 516,031               | 520,722              |
| Bank-owned life insurance ( BOLI )   | 125,654               | 121,674              |
| Other assets   | 51,826                | 48,143               |
| <b>Total assets</b>  | <b>\$ 6,451,105</b>   | <b>\$ 6,359,391</b>  |
| <b><u>LIABILITIES AND STOCKHOLDERS EQUITY</u></b>  |                       |                      |
| Deposits:  |                       |                      |
| Demand deposits  | \$ 1,732,534          | \$ 1,553,625         |
| Savings deposits   | 904,596               | 1,031,725            |
| Certificates of deposit of \$100,000 or more   | 431,744               | 480,362              |
| Other time deposits  | 1,067,003             | 1,159,108            |
| <b>Total deposits</b>  | <b>4,135,877</b>      | <b>4,224,820</b>     |
| Mortgage escrow deposits   | 19,648                | 18,075               |
| Borrowed funds   | 1,244,794             | 1,075,104            |
| Other liabilities  | 35,218                | 40,598               |
| <b>Total liabilities</b>   | <b>5,435,537</b>      | <b>5,358,597</b>     |

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Stockholders' Equity:

|   |              |              |
|---|--------------|--------------|
| Preferred stock, \$0.01 par value, 50,000,000 shares authorized, none issued  |              |              |
| Common stock, \$0.01 par value, 200,000,000 shares authorized, 83,209,293 shares issued and 59,609,837 shares outstanding at September 30, 2008, and 59,646,936 shares outstanding at December 31, 2007 | 832          | 832          |
| Additional paid-in capital  | 1,013,080    | 1,009,120    |
| Retained earnings   | 451,856      | 437,503      |
| Accumulated other comprehensive income  | 186          | 4,335        |
| Treasury stock, at cost   | (384,852)    | (383,407)    |
| Unallocated common stock held by Employee Stock Ownership Plan ( ESOP )   | (65,534)     | (67,589)     |
| Common stock acquired by the Directors' Deferred Fee Plan ( DDFP )  | (7,690)      | (7,759)      |
| Deferred compensation - DDFP  | 7,690        | 7,759        |
| Total stockholders' equity  | 1,015,568    | 1,000,794    |
| Total liabilities and stockholders' equity  | \$ 6,451,105 | \$ 6,359,391 |

See accompanying notes to unaudited consolidated financial statements.

**Table of Contents****PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY**

## Consolidated Statements of Income

Three and nine months ended September 30, 2008 and 2007 (Unaudited)

(Dollars in thousands, except per share data)

|  | Three months ended<br>September 30, |               | Nine months ended<br>September 30, |                |
|--|-------------------------------------|---------------|------------------------------------|----------------|
|  | 2008                                | 2007          | 2008                               | 2007           |
| <b>Interest income:</b>                                    |                                     |               |                                    |                |
| Real estate secured loans                                  | \$ 42,465                           | \$ 42,791     | \$ 124,406                         | \$ 125,315     |
| Commercial loans   | 10,665                              | 11,547        | 32,568                             | 29,880         |
| Consumer loans   | 9,106                               | 10,227        | 27,932                             | 29,061         |
| Investment securities                                      | 3,606                               | 3,802         | 10,860                             | 11,664         |
| Securities available for sale                              | 10,770                              | 9,418         | 32,372                             | 28,614         |
| Other short-term investments                               | 26                                  | 37            | 329                                | 115            |
| Federal funds sold   |                                     | 5             | 164                                | 110            |
| <b>Total interest income</b>                               | <b>76,638</b>                       | <b>77,827</b> | <b>228,631</b>                     | <b>224,759</b> |
| <b>Interest expense:</b>                                   |                                     |               |                                    |                |
| Deposits   | 20,133                              | 30,307        | 68,945                             | 83,663         |
| Borrowed funds   | 11,154                              | 8,237         | 32,577                             | 24,501         |
| <b>Total interest expense</b>                              | <b>31,287</b>                       | <b>38,544</b> | <b>101,522</b>                     | <b>108,164</b> |
| <b>Net interest income</b>                                 | <b>45,351</b>                       | <b>39,283</b> | <b>127,109</b>                     | <b>116,595</b> |
| <b>Provision for loan losses</b>                           | <b>3,800</b>                        | <b>1,300</b>  | <b>6,600</b>                       | <b>2,800</b>   |
| <b>Net interest income after provision for loan losses</b> | <b>41,551</b>                       | <b>37,983</b> | <b>120,509</b>                     | <b>113,795</b> |
| <b>Non-interest income:</b>                                |                                     |               |                                    |                |
| Fees   | 7,281                               | 6,435         | 18,287                             | 18,599         |
| Gain on insurance settlement                               |                                     |               |                                    | 5,947          |
| BOLI   | 1,320                               | 1,339         | 3,980                              | 4,026          |
| Net (loss) gain on securities transactions                 | (966)                               | 2             | (565)                              | (61)           |
| Other income   | 140                                 | 297           | 1,525                              | 1,490          |
| <b>Total non-interest income</b>                           | <b>7,775</b>                        | <b>8,073</b>  | <b>23,227</b>                      | <b>30,001</b>  |
| <b>Non-interest expense:</b>                               |                                     |               |                                    |                |
| Compensation and employee benefits                         | 16,591                              | 20,842        | 50,768                             | 54,784         |
| Net occupancy expense                                      | 5,195                               | 4,938         | 15,626                             | 14,451         |
| Data processing expense                                    | 2,296                               | 2,249         | 6,903                              | 6,913          |
| Amortization of intangibles                                | 1,373                               | 1,677         | 4,706                              | 4,915          |
| Advertising and promotion expense                          | 1,160                               | 1,089         | 2,989                              | 3,341          |
| Other operating expenses                                   | 5,343                               | 4,916         | 16,210                             | 14,775         |
| <b>Total non-interest expense</b>                          | <b>31,958</b>                       | <b>35,711</b> | <b>97,202</b>                      | <b>99,179</b>  |
| <b>Income before income tax expense</b>                    | <b>17,368</b>                       | <b>10,345</b> | <b>46,534</b>                      | <b>44,617</b>  |

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|                                    |            |            |            |            |
|------------------------------------|------------|------------|------------|------------|
| Income tax expense                 | 4,205      | 2,085      | 12,325     | 11,932     |
| Net income                         | \$ 13,163  | \$ 8,260   | \$ 34,209  | \$ 32,685  |
| Basic earnings per share           | \$ 0.23    | \$ 0.14    | \$ 0.61    | \$ 0.55    |
| Average basic shares outstanding   | 56,078,691 | 58,968,076 | 56,006,174 | 59,787,076 |
| Diluted earnings per share         | \$ 0.23    | \$ 0.14    | \$ 0.61    | \$ 0.55    |
| Average diluted shares outstanding | 56,078,870 | 58,968,076 | 56,006,234 | 59,787,076 |

See accompanying notes to unaudited consolidated financial statements.

**Table of Contents****PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY**

Consolidated Statements of Changes in Stockholders' Equity for the Nine Months Ended September 30, 2008 and 2007 (Unaudited)

(Dollars in thousands)

|  | COMMON<br>STOCK | ADDITIONAL<br>PAID-IN<br>CAPITAL | RETAINED<br>EARNINGS | ACCUMULATED<br>OTHER<br>COMPREHENSIVE<br>(LOSS)<br>INCOME | TREASURY<br>STOCK | UNALLOCATED<br>ESOP<br>SHARES | COMMON<br>STOCK<br>ACQUIRED<br>BY DDFP | DEFERRED<br>COMPENSATION<br>DDFP | TOTAL<br>STOCKHOLDERS'<br>EQUITY |
|--|-----------------|----------------------------------|----------------------|---|-------------------|-------------------------------|--|----------------------------------|----------------------------------|
| Balance at<br>December 31, 2006  | \$ 799          | \$ 937,616                       | \$ 424,958           | \$ (7,150)  | \$ (266,587)      | \$ (70,480)                   | \$ (13,010)                            | \$ 13,010                        | \$ 1,019,156                     |
| Comprehensive<br>income:   |                 |                                  |                      |   |                   |                               |  |                                  |                                  |
| Net income   |                 |                                  | 32,685               |   |                   |                               |  |                                  | 32,685                           |
| Other<br>comprehensive<br>income:  |                 |                                  |                      |   |                   |                               |  |                                  |                                  |
| Unrealized holding<br>gains on securities<br>arising during the<br>period (net of tax of<br>\$1,821) |                 |                                  |                      | 2,444   |                   |                               |  |                                  | 2,444                            |
| Reclassification<br>adjustment for<br>losses included in<br>net income (net of<br>tax of (\$27))     |                 |                                  |                      | 34  |                   |                               |  |                                  | 34                               |
| Amortization<br>related to<br>post-retirement<br>obligations (net of<br>tax of (\$124))              |                 |                                  |                      | (179)   |                   |                               |  |                                  | (179)                            |
| Total<br>comprehensive<br>income   |                 |                                  |                      |   |                   |                               |  |                                  | \$ 34,984                        |
| Common stock<br>issued in<br>connection with the<br>First Morris<br>acquisition, net                 | 33              | 61,902                           |                      |   |                   |                               |  |                                  | 61,935                           |
| Cash dividends<br>declared   |                 |                                  | (19,894)             |   |                   |                               |  |                                  | (19,894)                         |
| Tax contingency<br>reserve reversal  |                 | 2,048                            |                      |   |                   |                               |  |                                  | 2,048                            |
| Distributions from<br>DDFP   |                 | 47                               |                      |   |                   |                               | 166                                    | (166)                            | 47                               |
| Purchase of<br>treasury stock  |                 |                                  |                      |   | (80,275)          |                               |  |                                  | (80,275)                         |
| Allocation of ESOP<br>shares   |                 | (21)                             |                      |   |                   | 2,047                         |  |                                  | 2,026                            |
|  |                 | 3,763                            |                      |   |                   |                               |  |                                  | 3,763                            |



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|                               |        |              |            |            |              |             |             |           |    |           |
|-------------------------------|--------|--------------|------------|------------|--------------|-------------|-------------|-----------|----|-----------|
| Allocation of SAP shares      |        |              |            |            |              |             |             |           |    |           |
| Allocation of stock options   |        |              |            | 2,585      |              |             |             |           |    | 2,585     |
| Balance at September 30, 2007 |        |              |            |            |              |             |             |           |    |           |
|                               | \$ 832 | \$ 1,007,940 | \$ 437,749 | \$ (4,851) | \$ (346,862) | \$ (68,433) | \$ (12,844) | \$ 12,844 | \$ | 1,026,375 |

See accompanying notes to unaudited consolidated financial statements.

**Table of Contents****PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY**

Consolidated Statements of Changes in Stockholders' Equity for the Nine Months Ended September 30, 2008 and 2007 (Unaudited) (Continued)

(Dollars in thousands)

|   | COMMON<br>STOCK | ADDITIONAL<br>PAID-IN<br>CAPITAL | RETAINED<br>EARNINGS | ACCUMULATED<br>OTHER<br>COMPREHENSIVE<br>INCOME | TREASURY<br>STOCK | UNALLOCATED<br>ESOP<br>SHARES | COMMON<br>STOCK<br>ACQUIRED<br>BY<br>DDFP | DEFERRED<br>COMPENSATION<br>DDFP | TOTAL<br>STOCKHOLDERS'<br>EQUITY |
|---|-----------------|----------------------------------|----------------------|---|-------------------|-------------------------------|---|----------------------------------|----------------------------------|
| Balance at<br>December 31, 2007   | \$ 832          | \$ 1,009,120                     | \$ 437,503           | \$ 4,335  | \$ (383,407)      | \$ (67,589)                   | \$ (7,759)                                | \$ 7,759                         | \$ 1,000,794                     |
| Comprehensive<br>income:  |                 |                                  |                      |   |                   |                               |   |                                  |                                  |
| Net income  |                 |                                  | 34,209               |   |                   |                               |   |                                  | 34,209                           |
| Other<br>comprehensive<br>income:   |                 |                                  |                      |   |                   |                               |   |                                  |                                  |
| Unrealized holding<br>losses on securities<br>arising during the<br>period (net of tax of<br>(\$3,057)) |                 |                                  |                      | (4,784)   |                   |                               |   |                                  | (4,784)                          |
| Reclassification<br>adjustment for losses<br>included in net<br>income (net of tax of<br>(\$226))       |                 |                                  |                      | 339   |                   |                               |   |                                  | 339                              |
| Amortization related<br>to post-retirement<br>obligations (net of<br>tax of \$204)                      |                 |                                  |                      | 296   |                   |                               |   |                                  | 296                              |
| Total comprehensive<br>income   |                 |                                  |                      |   |                   |                               |   |                                  | \$30,060                         |
| Cash dividends<br>declared  |                 |                                  | (19,856)             |   |                   |                               |   |                                  | (19,856)                         |
| Distributions from<br>DDFP  |                 | (3)                              |                      |   |                   |                               | 69  | (69)                             | (3)                              |
| Purchases of<br>treasury stock  |                 |                                  |                      |   | (1,445)           |                               |   |                                  | (1,445)                          |
| Allocation of ESOP<br>shares  |                 | (324)                            |                      |   |                   | 2,055                         |   |                                  | 1,731                            |
| Allocation of SAP<br>shares   |                 | 2,513                            |                      |   |                   |                               |   |                                  | 2,513                            |
| Allocation of stock<br>options  |                 | 1,774                            |                      |   |                   |                               |   |                                  | 1,774                            |
| Balance at<br>September 30, 2008  | \$ 832          | \$ 1,013,080                     | \$ 451,856           | \$ 186  | \$ (384,852)      | \$ (65,534)                   | \$ (7,690)                                | \$ 7,690                         | \$ 1,015,568                     |

See accompanying notes to unaudited consolidated financial statements.



**Table of Contents****PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY**

## Consolidated Statements of Cash Flows

Nine months ended September 30, 2008 and 2007 (Unaudited)

(Dollars in thousands)

|  | Nine months ended<br>September 30, |               |
|--|------------------------------------|---------------|
|  | 2008                               | 2007          |
| Cash flows from operating activities:  |                                    |               |
| Net income   | \$ 34,209                          | \$ 32,685     |
| Adjustments to reconcile net income to net cash provided by operating activities:          |                                    |               |
| Depreciation and amortization of intangibles   | 10,531                             | 10,425        |
| Provision for loan losses  | 6,600                              | 2,800         |
| Deferred tax benefit   | (4,495)                            | (4,545)       |
| Increase in cash surrender value of BOLI   | (3,980)                            | (4,026)       |
| Net amortization of premiums and discounts on securities                                   | 229                                | 797           |
| Accretion of net deferred loan fees  | (1,608)                            | (1,575)       |
| Amortization of premiums on purchased loans, net   | 1,966                              | 2,477         |
| Net increase in loans originated for sale  | (13,281)                           | (6,209)       |
| Proceeds from sales of loans originated for sale   | 13,275                             | 6,284         |
| Proceeds from sales of foreclosed assets, net  | 4,953                              | 689           |
| Allocation of ESOP shares  | 1,731                              | 2,026         |
| Allocation of SAP shares   | 2,513                              | 3,763         |
| Allocation of stock options  | 1,774                              | 2,585         |
| Net loss (gain) on sale of loans   | 6                                  | (75)          |
| Net gain on securities available for sale  | (844)                              | (61)          |
| Impairment charge on securities  | 1,409                              |               |
| Net gain on sale of premises and equipment   | (87)                               | (153)         |
| Net gain on sale of foreclosed assets  | (1)                                |               |
| Decrease (increase) in accrued interest receivable   | 1,078                              | (984)         |
| (Increase) decrease in other assets  | (3,587)                            | 9,887         |
| (Decrease) increase in other liabilities   | (5,380)                            | 1,056         |
| <b>Net cash provided by operating activities</b>   | <b>47,011</b>                      | <b>57,846</b> |
| Cash flows from investing activities:  |                                    |               |
| Proceeds from maturities, calls and paydowns of investment securities                      | 35,855                             | 32,638        |
| Purchases of investment securities   | (31,774)                           | (8,642)       |
| Proceeds from sales of securities available for sale                                       | 7,731                              | 43,287        |
| Proceeds from maturities and paydowns of securities available for sale                     | 159,087                            | 163,207       |
| Purchases of securities available for sale   | (181,918)                          | (21,680)      |
| Purchases of loans   | (228,426)                          | (58,353)      |
| Net decrease (increase) in loans   | 83,098                             | (52,597)      |
| Cash consideration paid to acquire First Morris, net of cash and cash equivalents received |                                    | (1,383)       |
| Proceeds from sales of premises and equipment  | 818                                | 328           |
| Purchases of premises and equipment, net   | (4,496)                            | (6,959)       |
| <b>Net cash (used in) provided by investing activities</b>                                 | <b>(160,025)</b>                   | <b>89,846</b> |
| Cash flows from financing activities:  |                                    |               |
| Net decrease in deposits   | (88,943)                           | (61,099)      |

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|  |            |            |
|--|------------|------------|
| Increase (decrease) in mortgage escrow deposits      | 1,573      | (99)       |
| Purchases of treasury stock                          | (1,445)    | (80,275)   |
| Cash dividends paid to stockholders                  | (19,856)   | (19,894)   |
| Proceeds from long-term borrowings                   | 390,600    | 110,000    |
| Payments on long-term borrowings                     | (327,601)  | (143,062)  |
| Net increase in short-term borrowings                | 106,691    | 65,629     |
| <br>   |            |            |
| Net cash provided by (used in) financing activities  | 61,019     | (128,800)  |
| <br>   |            |            |
| Net (decrease) increase in cash and cash equivalents | (51,995)   | 18,892     |
| Cash and cash equivalents at beginning of period     | 140,629    | 92,057     |
| <br>   |            |            |
| Cash and cash equivalents at end of period           | \$ 88,634  | \$ 110,949 |
| <br>   |            |            |
| Cash paid during the period for:                     |            |            |
| Interest on deposits and borrowings                  | \$ 102,063 | \$ 107,241 |
| <br>   |            |            |
| Income taxes   | \$ 10,371  | \$ 15,538  |

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**PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY**

Consolidated Statements of Cash Flows

Nine months ended September 30, 2008 and 2007 (Unaudited) (Continued)

(Dollars in thousands)

|   | <b>Nine months ended<br/>September 30,</b> |             |
|---|--|-------------|
|   | <b>2008</b>                                | <b>2007</b> |
| Non cash investing activities:                    |  |             |
| Transfer of loans receivable to foreclosed assets | \$ 7,896                                   | \$ 761      |
| Loan securitizations                              | \$ 55,217                                  | \$          |
| Fair value of assets acquired                     | \$   | \$ 554,284  |
| Goodwill and core deposit intangible              | \$   | \$ 96,952   |
| Liabilities assumed                               | \$   | \$ 527,256  |
| Common stock issued for First Morris acquisition  | \$   | \$ 61,935   |

See accompanying notes to unaudited consolidated financial statements.

**Table of Contents****PROVIDENT FINANCIAL SERVICES, INC. AND SUBSIDIARY****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****Note 1. Summary of Significant Accounting Policies****A. Basis of Presentation**

The accompanying unaudited consolidated financial statements include the accounts of Provident Financial Services, Inc. and its wholly-owned subsidiary, The Provident Bank (the Bank), together with Provident Financial Services, Inc., the Company).

The interim unaudited consolidated financial statements reflect all normal and recurring adjustments, which are, in the opinion of management, considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. The results of operations for the three and nine months ended September 30, 2008 are not necessarily indicative of the results of operations that may be expected for all of 2008.

Certain information and note disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission.

These unaudited consolidated financial statements should be read in conjunction with the December 31, 2007 Annual Report to Stockholders on Form 10-K.

**B. Earnings Per Share**

The following is a reconciliation of the numerators and denominators of the basic and diluted earnings per share calculations:

|   | For the three months ended September 30, |            |           |          |            |           | For the nine months ended September 30, |            |           |           |            |           |
|---|--|------------|-----------|----------|------------|-----------|---|------------|-----------|-----------|------------|-----------|
|   | 2008                                     |            | Per Share | 2007     |            | Per Share | 2008                                    |            | Per Share | 2007      |            | Per Share |
|   | Income                                   | Shares     | Amount    | Income   | Shares     | Amount    | Income                                  | Shares     | Amount    | Income    | Shares     | Amount    |
| Net income                              | \$ 13,163                                |            |           | \$ 8,260 |            |           | \$ 34,209                               |            |           | \$ 32,685 |            |           |
| Basic earnings per share:               |  |            |           |          |            |           |   |            |           |           |            |           |
| Income available to common stockholders | \$ 13,163                                | 56,078,691 | \$ 0.23   | \$ 8,260 | 58,968,076 | \$ 0.14   | \$ 34,209                               | 56,006,174 | \$ 0.61   | \$ 32,685 | 59,787,076 | \$ 0.55   |
| Dilutive shares                         |  | 179        |           |          |            |           |   | 60         |           |           |            |           |
| Diluted earnings per share:             |  |            |           |          |            |           |   |            |           |           |            |           |
| Income available to common stockholders | \$ 13,163                                | 56,078,870 | \$ 0.23   | \$ 8,260 | 58,968,076 | \$ 0.14   | \$ 34,209                               | 56,006,234 | \$ 0.61   | \$ 32,685 | 59,787,076 | \$ 0.55   |

Anti-dilutive stock options and awards totaling 4,263,178 shares at September 30, 2008, were excluded from the earnings per share calculations.

**Table of Contents****Note 2. Loans and Allowance for Loan Losses**

Loans receivable at September 30, 2008 and December 31, 2007 are summarized as follows (in thousands):

|                            | September 30,<br>2008 | December 31,<br>2007 |
|----------------------------|-----------------------|----------------------|
| Mortgage loans:            |                       |                      |
| Residential                | \$ 1,787,599          | \$ 1,705,747         |
| Commercial                 | 997,149               | 847,907              |
| Multi-family               | 55,244                | 67,546               |
| Construction               | 229,420               | 309,569              |
| Total mortgage loans       | 3,069,412             | 2,930,769            |
| Commercial loans           | 671,636               | 712,062              |
| Consumer loans             | 626,670               | 644,134              |
| Total other loans          | 1,298,306             | 1,356,196            |
| Premium on purchased loans | 11,051                | 9,793                |
| Unearned discounts         | (523)                 | (661)                |
| Net deferred (fees) costs  | (98)                  | 194                  |
|                            | \$ 4,378,148          | \$ 4,296,291         |

The activity in the allowance for loan losses for the three and nine months ended September 30, 2008 and 2007 is summarized as follows (in thousands):

|   | Three months ended<br>September 30, |           | Nine months ended<br>September 30, |           |
|---|-------------------------------------|-----------|------------------------------------|-----------|
|   | 2008                                | 2007      | 2008                               | 2007      |
| Balance at beginning of period                          | \$ 41,118                           | \$ 36,764 | \$ 40,782                          | \$ 32,434 |
| Provision charged to operations                         | 3,800                               | 1,300     | 6,600                              | 2,800     |
| Allowance for loan losses transferred from First Morris |                                     |           |                                    | 2,825     |
| Recoveries of loans previously charged off              | 700                                 | 346       | 1,903                              | 1,753     |
| Loans charged off                                       | (2,289)                             | (819)     | (5,956)                            | (2,221)   |
| Balance at end of period                                | \$ 43,329                           | \$ 37,591 | \$ 43,329                          | \$ 37,591 |

**Note 3. Deposits**

Deposits at September 30, 2008 and December 31, 2007 are summarized as follows (in thousands):

|              | September 30,<br>2008 | December 31,<br>2007 |
|--------------|-----------------------|----------------------|
| Savings      | \$ 904,596            | \$ 1,031,725         |
| Money market | 680,006               | 598,344              |
| NOW          | 589,328               | 467,868              |



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|                         |              |              |
|-------------------------|--------------|--------------|
| Non-interest bearing    | 463,200      | 487,413      |
| Certificates of deposit | 1,498,747    | 1,639,470    |
|                         | \$ 4,135,877 | \$ 4,224,820 |

**Table of Contents****Note 4. Components of Net Periodic Benefit Cost**

The Bank has a noncontributory defined benefit pension plan (the Plan) covering its full-time employees who had attained age 21 with at least one year of service as of April 1, 2003. The Plan was frozen on April 1, 2003. The Plan provides for 100% vesting after five years of service. The Plan's assets are invested in investment funds and group annuity contracts managed by the Principal Financial Group and Allmerica Financial.

In addition to pension benefits, certain health care and life insurance benefits are currently made available to retired employees. The costs of such benefits are accrued based on actuarial assumptions from the date of hire to the date the employee is fully eligible to receive the benefits. Effective January 1, 2003, eligibility for retiree health care benefits was frozen as to new entrants and benefits were eliminated for employees with less than ten years of service as of December 31, 2002. Effective January 1, 2007, eligibility for retiree life insurance benefits was frozen to new entrants and retiree life insurance benefits were eliminated for employees with less than ten years of service as of December 31, 2006.

Net periodic benefit costs for the three and nine months ended September 30, 2008 and 2007 include the following components (in thousands):

|  | Pension benefits                 |       | Other post-retirement benefits   |       | Pension benefits                |         | Other post-retirement benefits  |       |
|--|----------------------------------|-------|----------------------------------|-------|---------------------------------|---------|---------------------------------|-------|
|  | Three months ended September 30, |       | Three months ended September 30, |       | Nine months ended September 30, |         | Nine months ended September 30, |       |
|  | 2008                             | 2007  | 2008                             | 2007  | 2008                            | 2007    | 2008                            | 2007  |
| Service cost   | \$                               |       | 41                               | 47    | \$                              |         | 140                             | 181   |
| Interest cost  | 267                              | 234   | 252                              | 237   | 761                             | 724     | 764                             | 759   |
| Expected return on plan assets                       | (389)                            | (413) |                                  |       | (1,168)                         | (1,212) |                                 |       |
| Amortization of unrecognized transitional obligation |                                  |       |                                  | 58    |                                 |         |                                 | 123   |
| Amortization of prior service cost                   |                                  |       | (1)                              | (1)   |                                 |         | (3)                             | (3)   |
| Amortization of the net (gain) loss                  |                                  |       | (174)                            | (162) |                                 |         | (496)                           | (423) |
| Net periodic benefit (increase) cost                 | \$ (122)                         | (179) | 118                              | 179   | \$ (407)                        | (488)   | 405                             | 637   |

The Company previously disclosed in its consolidated financial statements for the year ended December 31, 2007 that it does not expect to contribute to its defined benefit pension plan in 2008. As of September 30, 2008, no contributions to the defined benefit pension plan have been made.

The net periodic benefit (increase) costs for pension benefits and other post-retirement benefits for the three and nine months ended September 30, 2008 were calculated using the results of the January 1, 2008 Statement of Financial Accounting Standards (SFAS) No. 87 and SFAS No. 106 valuations.

**Note 5. Impact of Recent Accounting Pronouncements**

In October 2008, Financial Accounting Standards Board Staff Position (FSP) 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active, was issued. FSP 157-3 clarifies the application of SFAS No. 157, Fair Value Measurements, in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP 157-3 was effective upon issuance, including prior periods for which financial statements have not been issued. The Company considered the guidance in FSP 157-3 in determining the fair value of financial instruments as discussed in Note 6 to the unaudited consolidated financial statements.

In June 2008, FSP EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities, was issued. FSP EITF 03-6-1 requires unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents to be treated as participating securities as defined in Emerging Issues Task Force (EITF) Issue No. 03-6, Participating Securities and the Two-Class Method under FASB Statement No. 128, and, therefore, included in the earnings allocation in computing earnings per share under the two-class method described in SFAS No. 128, Earnings Per Share. FSP EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008,



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and interim periods within those years. Upon adoption, all previously reported earnings per share data must be retroactively adjusted to conform with the requirements of the FSP. The Company is currently evaluating the impact of the adoption of FSP EITF 03-6-1 on its calculation of earnings per share.

In March 2008, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 161, Disclosure about Derivative Instruments and Hedging activities, an Amendment of FASB Statement No. 133. The new standard establishes enhanced disclosure requirements about (a) how and why an entity uses derivative instruments; (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations; and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, and is not expected to have a significant impact on the Company's financial condition, results of operations or financial statement disclosures.

On January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. The adoption of SFAS No. 157 on January 1, 2008 did not have a material impact on the Company's financial condition or results of operations.

Effective January 1, 2008, the Company adopted the provisions of EITF Issue No. 06-11, Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards. EITF 06-11 states that a realized income tax benefit from dividends or dividend equivalents that are charged to retained earnings and are paid to employees for equity classified unvested equity shares, unvested equity share units, and outstanding equity share options should be recognized as an increase in additional paid-in capital. The amount recognized in additional paid-in capital for the realized income tax benefit from dividends on those awards should be included in the pool of excess tax benefits available to absorb potential future tax deficiencies on share-based payment awards. The adoption of EITF 06-11 did not have a material impact on the Company's financial condition, results of operations or financial statement disclosures.

In February 2008, FSP No. 157-2, Effective Date of FASB Statement No. 157, was issued. FSP No. 157-2 delayed the application of SFAS No. 157 for non-financial assets and non-financial liabilities until January 1, 2009. The Company is currently evaluating the impact of the adoption of FSP No. 157-2 on its financial statement disclosures.

On January 1, 2008, the Company adopted SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities Including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure selected financial assets and liabilities at fair value. The adoption of SFAS No. 159 did not impact the Company's financial condition, results of operations or financial statement disclosures, as the Company did not elect the fair value option for any assets or liabilities.

In December 2007, the FASB issued SFAS No. 141 (Revised 2007), Business Combinations ( SFAS No. 141R ), which replaces SFAS No. 141, Business Combinations, and applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS No. 141R requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost-allocation process required under SFAS No. 141 whereby the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their estimated fair value. SFAS No. 141R requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed, as was previously the case under SFAS No. 141. Under SFAS No. 141R, the requirements of SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities, would have to be met in order to accrue for a restructuring plan in purchase accounting. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting and, instead, that contingency would be subject to the probable and estimable recognition criteria of SFAS No. 5, Accounting for Contingencies. SFAS No. 141R is effective for all business combinations closing on or after January 1, 2009 and could have a significant impact on the Company's accounting for business combinations on or after such date.

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In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB Statement No. 51. This standard amends the guidance in Accounting Research Bulletin ( ARB ) No. 51, Consolidated Financial Statements. The new standard establishes accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is an ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, SFAS No. 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. It also requires disclosure, on the face of the consolidated income statement, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. SFAS No. 160 is effective on January 1, 2009, and is not expected to have a significant impact on the Company's financial condition, results of operations or financial statement disclosures.

In November 2007, the Securities and Exchange Commission ( SEC ) issued SEC Staff Accounting Bulletin ( SAB ) No. 109, Written Loan Commitments Recorded at Fair Value Through Earnings. SAB No. 109 supersedes SAB No. 105, Application of Accounting Principles to Loan Commitments, and indicates that the expected net future cash flows related to the associated servicing of the loan should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The guidance in SAB No. 109 is applied on a prospective basis to derivative loan commitments issued or modified in fiscal quarters beginning after December 15, 2007. The Company's adoption of SAB No. 109 did not have a material impact on its financial condition, results of operations or financial statement disclosures.

**Note 6. Fair Value Measurement of Assets and Liabilities**

SFAS No. 157 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of fair value hierarchy under SFAS No. 157 are as follows:

- Level 1: Unadjusted quoted market prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2: Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability; and
- Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The following table presents the assets and liabilities reported on the consolidated statements of financial condition at their fair value as of September 30, 2008 by level within the fair value hierarchy.

| (Dollars in thousands)   | September 30,<br>2008 | Fair Value Measurements at Reporting Date Using:                        |  |  |
|--|-----------------------|---|--|--|
|  |                       | Quoted Prices in<br>Active Markets for<br>Identical Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs (Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Securities available for sale  | \$ 832,659            | \$ 102,195  | \$ 730,464   | \$   |
| Loans measured for impairment based on the fair value of the underlying collateral in accordance with SFAS No. 114 | 2,208                 |   |  | 2,208  |

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The following valuation techniques are based upon the unpaid principal balance only and exclude any accrued interest or dividends at the measurement date. Interest income and expense and dividend income are recorded within the consolidated statements of income depending on the nature of the instrument using the effective interest method based on acquired discount or premium.

The valuation techniques described below were used to measure fair value of financial instruments in the preceding table on a recurring basis during the three and nine months ended September 30, 2008.

For securities available for sale, fair value was estimated using a market approach. The majority of the Company's securities are fixed income instruments that are not quoted on an exchange, but are traded in active markets. Prices for these instruments are obtained through third party data service providers or dealer market participants with which the Company has historically transacted both purchases and sales of securities. Prices obtained from these sources include market quotations and matrix pricing. Matrix pricing, a Level 2 input as defined by SFAS No. 157, is a mathematical technique used principally to value certain securities to benchmark or comparable securities. The Company also holds equity securities and debt instruments issued by the U.S. government and U.S. government-sponsored agencies that are traded in active markets with readily accessible quoted market prices that are considered Level 1 inputs.

The valuation techniques described below were used to measure fair value of financial instruments in the preceding table on a non-recurring basis during the three and nine months ended September 30, 2008.

For loans measured for impairment based on the fair value of the underlying collateral in accordance with SFAS No. 114, Accounting by Creditors for Impairment of a Loan, fair value was estimated using a market approach. The Company measures the fair value of collateral underlying impaired loans primarily through obtaining independent appraisals that rely upon market prices for similar assets in active markets. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience, and are considered Level 3 inputs. The Company recognized impairment charges of \$1.2 million via specific reserves established through the provision for loan losses in connection with loans measured for impairment based on the fair value of the underlying collateral in accordance with SFAS No. 114 during the nine months ended September 30, 2008.

There were no changes to the valuation techniques for fair value measurement during the three and nine months ended September 30, 2008.

Certain non-financial assets and non-financial liabilities measured at fair value on a non-recurring basis include goodwill and other intangible assets and other non-financial long-lived assets. As stated in Note 5, SFAS No. 157 will be applicable to these fair value measurements beginning January 1, 2009.

## **Note 7. Subsequent Event**

On October 28, 2008, Visa Inc. announced that it has agreed to settle litigation with Discover Financial Services, originally filed in 2004, for \$1.89 billion. The settlement includes \$1.74 billion from the litigation escrow created under Visa's retrospective responsibility plan, \$80.0 million from Visa Inc. to obtain releases from MasterCard for all potential claims against Visa, including those related to Visa's former Settlement Service Fee, and an additional \$65.0 million which will be refunded by Morgan Stanley under a separate agreement related to the settlement.

This settlement is subject to approval by Visa's former U.S. member financial institutions. The settlement agreement ends all current litigation between Discover, Visa USA, Visa International, and MasterCard and it releases Visa and its members from all potential liability related to Visa's existing rules or agreements with member financial institutions. As a former U.S. member financial institution, the Company's total liability with respect to the Discover settlement is approximately \$107,000, of which \$40,000 was recorded in a previous quarter.

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### **Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS. Forward Looking Statements**

Certain statements contained herein are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such forward-looking statements may be identified by reference to a future period or periods or by the use of forward-looking terminology, such as may, will, believe, expect, estimate, anticipate, continue, or similar terms, variations on those terms, or the negative of those terms. Forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, those related to the economic environment, particularly in the market areas in which the Company operates, competitive products and pricing, fiscal and monetary policies of the U.S. Government, changes in government regulations affecting financial institutions, including regulatory fees and capital requirements, changes in prevailing interest rates, acquisitions and the integration of acquired businesses, credit risk management, asset-liability management, the financial and securities markets and the availability of and costs associated with sources of liquidity.

The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The Company wishes to advise that the factors listed above could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements. The Company does not undertake and specifically declines any obligation to publicly release the result of any revisions, which may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

#### **Critical Accounting Policies**

The calculation of the allowance for loan losses is a critical accounting policy of the Company. The allowance for loan losses is a valuation account that reflects management's evaluation of the probable losses inherent in the loan portfolio. The Company maintains the allowance for loan losses through provisions for loan losses that are charged to income. Charge-offs against the allowance for loan losses are taken on loans where management determines that the collection of loan principal is unlikely. Recoveries made on loans that have been charged-off are credited to the allowance for loan losses.

The Company's evaluation of the adequacy of the allowance for loan losses includes a review of all loans on which the collectibility of principal may not be reasonably assured. For residential mortgage and consumer loans, this is determined primarily by delinquency and collateral values. For commercial real estate and commercial loans, an extensive review of financial performance, payment history and collateral values is conducted on a quarterly basis.

As part of the evaluation of the adequacy of the allowance for loan losses, each quarter management prepares a worksheet. This worksheet categorizes the entire loan portfolio by certain risk characteristics such as loan type (residential mortgage, commercial mortgage, construction, commercial, etc.) and loan risk rating.

When assigning a risk rating to a loan, management utilizes a nine point internal risk rating system. Loans deemed to be acceptable quality are rated one through four, with a rating of one established for loans with minimal risk. Loans deemed to be of questionable quality are rated five (watch) or six (special mention). Loans with adverse classifications (substandard, doubtful or loss) are rated seven, eight or nine, respectively. Commercial mortgage, commercial and construction loans are rated individually and each lending officer is responsible for risk rating loans in his or her portfolio. These risk ratings are then reviewed by the department manager and/or the Chief Lending Officer and the Credit Administration Department. The risk ratings are then confirmed by the Loan Review Department and, for loans requiring Credit Committee approval, they are periodically reviewed by the Credit Committee in the credit renewal or approval process.

Management believes the primary risks inherent in the portfolio are a decline in the economy, generally, a decline in real estate market values, and possible increases in interest rates. Any one or a combination of these events may adversely affect borrowers' ability to repay the loans, resulting in increased delinquencies, loan losses and future levels of provisions. Accordingly, the Company has provided for loan losses at the current level to address the current risk in its loan portfolio. Management considers it important to maintain the ratio of the allowance for loan losses to total loans at an acceptable level given current economic conditions, interest rates and the composition of the portfolio.

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Although management believes that the Company has established and maintained the allowance for loan losses at adequate levels, additions may be necessary if future economic and other conditions differ substantially from the current operating environment. In addition, various regulatory agencies periodically review the adequacy of the Company's allowance for loan losses as an integral part of their examination process. Such agencies may require the Company to recognize additions to the allowance or additional write-downs based on their judgments about information available to them at the time of their examination. Although management uses the best information available, the level of the allowance for loan losses remains an estimate that is subject to significant judgment and short-term change.

Additional critical accounting policies relate to judgments about other asset impairments, including goodwill, investment securities and deferred tax assets. The Company engages an independent third party to perform an annual analysis during the fourth quarter to test the aggregate balance of goodwill for impairment. For purposes of goodwill impairment evaluation, the Bank is identified as the reporting unit. The fair value of goodwill is determined in the same manner as goodwill recognized in a business combination and uses standard valuation methodologies, including a review of comparable transactions and discounted cash flow analysis. A continuing period of market disruption resulting in the Company's stock price remaining below its book value per share may adversely impact the goodwill valuation. If the carrying amount of goodwill pursuant to this analysis were to exceed the implied fair value of goodwill, an impairment loss would be recognized. No impairment loss was required to be recognized for the three or nine months ended September 30, 2008 or 2007.

The Company's available for sale securities portfolio is carried at estimated fair value, with any unrealized gains or losses, net of taxes, reported as accumulated other comprehensive income or loss in stockholders' equity. Estimated fair values are based on market quotations or matrix pricing as discussed in Note 6 to the unaudited consolidated financial statements. Securities which the Company has the positive intent and ability to hold to maturity are classified as held to maturity and carried at amortized cost. The Company conducts a periodic review and evaluation of the securities portfolio to determine if any declines in the fair values of securities are other than temporary. If such a decline were deemed other than temporary, the Company would write down the security to fair value through a charge to current period operations. The market value of the securities portfolio is significantly affected by changes in interest rates. In general, as interest rates rise, the market value of fixed-rate securities decreases and as interest rates fall, the market value of fixed-rate securities increases. The Company evaluates its intent and ability to hold securities for a sufficient time to recover the recorded principal balance. The Company also has investments in common stock issued by several publicly-traded financial institutions, the valuation of which is affected by the institutions' performance and market conditions. During the three and nine months ended September 30, 2008, the Company recognized impairment charges totaling \$1.4 million related to investments in a debt security issued by Lehman Brothers Holdings, Inc. and the common stock of two publicly-traded financial institutions.

The determination of whether deferred tax assets will be realizable is predicated on estimates of future taxable income. Such estimates are subject to management's judgment. A valuation allowance is established when management is unable to conclude that it is more likely than not that it will realize deferred tax assets based on the nature and timing of these items.

**COMPARISON OF FINANCIAL CONDITION AT SEPTEMBER 30, 2008 AND DECEMBER 31, 2007**

Total assets at September 30, 2008 increased \$91.7 million, or 1.4%, to \$6.45 billion compared to \$6.36 billion at December 31, 2007, due primarily to increases in loans and securities available for sale.

Securities available for sale, at fair value, increased \$63.0 million, or 8.2%, to \$832.7 million at September 30, 2008, compared to \$769.6 million at December 31, 2007. The increase in the securities available for sale portfolio included \$55.2 million of residential mortgage loan pools that were securitized by the Company in the first quarter of 2008 and are held as securities available for sale. The investment portfolio consists primarily of Agency-guaranteed mortgage-backed securities and bank-qualified municipal bonds. There are no preferred or trust preferred equity securities, or common or preferred stock of Fannie Mae or Freddie Mac in the portfolio. The weighted average life of the Company's available for sale securities portfolio was 4.8 years at September 30, 2008.



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Federal Home Loan Bank stock increased \$3.4 million, or 8.5%, to \$43.1 million at September 30, 2008, compared to \$39.8 million at December 31, 2007. The Company invests in stock of the Federal Home Loan Bank of New York ( FHLB-NY ) as required under the terms of membership. The level of required stock holdings is dependent, in part, on outstanding borrowings by the Company from the FHLB-NY.

Total net loans at September 30, 2008 increased \$79.3 million, or 1.9%, to \$4.33 billion, compared to \$4.26 billion at December 31, 2007, as year-to-date loan originations and purchases more than offset the securitization of \$55.2 million of conforming one- to four-family 30-year fixed-rate residential mortgage loans during the first quarter of 2008. Loan originations totaled \$952.6 million and loan purchases totaled \$228.4 million for the nine months ended September 30, 2008. Compared with December 31, 2007, commercial mortgage and multi-family loans increased \$136.9 million, and residential mortgage loans increased \$81.9 million, while construction loans decreased \$80.1 million, commercial loans decreased \$40.4 million, and consumer loans decreased \$17.5 million. Commercial loans, consisting of commercial real estate, construction and commercial loans, totaled \$1.95 billion, or 44.7% of the loan portfolio at September 30, 2008, compared to \$1.94 billion, or 45.2% of the loan portfolio at December 31, 2007. The Company intends to continue to focus on the origination of commercial loans. Retail loans, which consist of residential mortgage loans and consumer loans, such as fixed-rate home equity loans and lines of credit, totaled \$2.41 billion and accounted for 55.3% of the loan portfolio at September 30, 2008, compared to \$2.35 billion, or 54.8% of the portfolio at December 31, 2007.

At September 30, 2008, the allowance for loan losses totaled \$43.3 million, or 0.99% of total loans, compared with \$40.8 million, or 0.95% of total loans at December 31, 2007. Total non-performing loans were \$35.3 million, or 0.81% of total loans at September 30, 2008, compared to \$34.6 million, or 0.81% of total loans at December 31, 2007. The Company had one loan with an outstanding balance of \$1.1 million at September 30, 2008, for which terms have been modified under a troubled debt restructuring. This loan was current as to principal and interest prior to restructuring and has continued to perform in accordance with the modified terms; therefore it is not included in non-performing loans at September 30, 2008. No impairment charge has been required with respect to this loan. Non-performing assets were \$38.8 million, or 0.60% of total assets at September 30, 2008, compared to \$35.7 million, or 0.56% of total assets at December 31, 2007.

At September 30, 2008, the Company identified two commercial real estate loans and one commercial loan with total outstanding balances of \$22.5 million that are potential problem loans. These loans were not past due at September 30, 2008, but known information about possible credit problems of the borrowers causes management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in these loans being included later in non-performing loans.

At September 30, 2008, the Company held \$3.6 million of foreclosed assets, compared with \$1.0 million at December 31, 2007. The increase in foreclosed assets was primarily attributable to one commercial real estate line of credit secured by a number of properties that was previously classified as impaired.

Total deposits decreased \$88.9 million to \$4.14 billion at September 30, 2008, from \$4.22 billion at December 31, 2007. However, core deposits, which consist of all demand and savings deposits, increased \$51.8 million, or 2.0%, to \$2.64 billion at September 30, 2008, compared to \$2.59 billion at December 31, 2007. Within core deposits, NOW checking account balances increased \$121.5 million, to \$589.3 million at September 30, 2008, and money market account balances increased \$81.7 million, to \$680.0 million at September 30, 2008. These increases were primarily due to increases in relationship checking and money market account balances, increases in business money market accounts, and a shift in customer deposits out of short-term certificates of deposit and lower-rate savings accounts. Certificates of deposit decreased \$140.7 million, or 8.8%, to \$1.50 billion at September 30, 2008, compared to \$1.64 billion at December 31, 2007. Certain higher-cost certificates of deposit that matured were replaced with borrowed funds at more favorable rates, as the Company continued to emphasize relationship banking in its deposit acquisition strategy. Core deposits increased to 63.8% of total deposits at September 30, 2008, from 61.2% of total deposits at December 31, 2007. Borrowed funds increased \$169.7 million, or 15.8%, to \$1.24 billion at September 30, 2008, from \$1.08 billion at December 31, 2007.

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Total stockholders' equity increased \$14.8 million, or 1.5%, to \$1.02 billion at September 30, 2008, compared to \$1.00 billion at December 31, 2007. This increase was primarily attributable to net income of \$34.2 million and the allocation of shares to stock-based compensation plans of \$6.0 million, partially offset by cash dividends declared totaling \$19.9 million, an increase of \$4.8 million in unrealized securities losses, net of tax, and common stock repurchases totaling \$1.4 million. At September 30, 2008, book value per share and tangible book value per share were \$17.04 and \$8.38, respectively, compared with \$16.78 and \$8.05, respectively, at December 31, 2007.

*Liquidity and Capital Resources.* The Company's primary sources of funds are deposits, FHLB-NY advances, repurchase agreements, loan repayments and sales, maturities and sales of investments and cash flows from mortgage-backed securities. Scheduled loan amortization is a fairly predictable source of funds, while loan and mortgage-backed securities prepayments and deposit flows are influenced by interest rates, local economic conditions and the competitive marketplace. Additional sources of liquidity that are available to the Company, should the need arise, are a \$100.0 million overnight line of credit and a \$100.0 million one-month line of credit with the FHLB-NY. As of September 30, 2008, the Company had \$50.0 million in outstanding borrowings against these lines of credit.

Cash needs for the nine months ended September 30, 2008, were provided for primarily from income and principal payments on loans, investments and mortgage-backed securities, borrowings and sales of residential mortgage loans, mortgage-backed securities and investments. The cash was used primarily to fund interest and operating expenses, current loan originations and purchases, securities purchases, and the net reduction in deposits.

As of September 30, 2008, the Bank and the Company exceeded all regulatory capital requirements as follows:

|                                    | At September 30, 2008  |       |            |       |
|------------------------------------|------------------------|-------|------------|-------|
|                                    | Required               |       | Actual     |       |
|                                    | Amount                 | Ratio | Amount     | Ratio |
|                                    | (Dollars in thousands) |       |            |       |
| <b>Bank:</b>                       |                        |       |            |       |
| Regulatory Tier 1 leverage capital | \$ 235,521             | 4.00% | \$ 383,866 | 6.52% |
| Tier 1 risk-based capital          | 160,578                | 4.00  | 383,866    | 9.56  |
| Total risk-based capital           | 321,155                | 8.00  | 427,195    | 10.64 |
| <b>Company:</b>                    |                        |       |            |       |
| Regulatory Tier 1 leverage capital | \$ 236,188             | 4.00% | \$ 500,246 | 8.47% |
| Tier 1 risk-based capital          | 161,171                | 4.00  | 500,246    | 12.42 |
| Total risk-based capital           | 322,341                | 8.00  | 543,575    | 13.49 |

**COMPARISON OF OPERATING RESULTS FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2008 AND 2007**

*General.* The Company reported net income of \$13.2 million for the three months ended September 30, 2008 and \$34.2 million for the nine months ended September 30, 2008, compared to \$8.3 million and \$32.7 million for the same periods in 2007. Basic and diluted earnings per share were \$0.23 for the quarter and \$0.61 for the nine months ended September 30, 2008, compared with basic and diluted earnings per share of \$0.14 for the same quarter in 2007 and \$0.55 for the nine months ended September 30, 2007. The annualized return on average assets was 0.82% and 0.72% for the three and nine months ended September 30, 2008, respectively, compared with 0.53% and 0.73% for the same respective periods in 2007. Annualized return on average equity was 5.17% and 4.53% for the three and nine months ended September 30, 2008, compared with 3.18% and 4.22% for the same respective periods in 2007.

Earnings and per share data for the nine months ended September 30, 2008 reflect severance costs totaling \$503,000, net of tax, recognized during the second quarter of 2008. In addition, the Company recorded other-than-temporary impairment charges on investments in a debt security issued by Lehman Brothers Holdings, Inc. and the common stock of two publicly-traded financial

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institutions totaling \$869,000, net of tax, during the quarter ended September 30, 2008. Results for the nine months ended September 30, 2008, were also impacted by a \$180,000 net after-tax gain recorded in connection with the ownership and mandatory redemption of a portion of the Company's Class B Visa, Inc. shares as part of Visa's initial public offering in the first quarter of 2008, and a \$175,000 net after-tax gain resulting from the sale of a branch office in the first quarter of 2008.

Earnings and per share data for the three and nine months ended September 30, 2007 were impacted by severance charges totaling \$1.9 million, net of tax. Earnings and per share data for the nine months ended September 30, 2007 were further impacted by the settlement of an insurance claim which resulted in a recovery of \$3.5 million, net of tax, related to a fraud loss that occurred and was recognized in 2002, and one-time expenses of \$246,000, net of tax, related to the April 1, 2007 acquisition of First Morris Bank & Trust (First Morris).

*Net Interest Income.* Total net interest income increased \$6.1 million, or 15.4%, to \$45.4 million for the quarter ended September 30, 2008, compared to \$39.3 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, total net interest income increased \$10.5 million, or 9.0%, to \$127.1 million, compared to \$116.6 million for the same period in 2007. Interest income for the third quarter of 2008 decreased \$1.2 million, or 1.5%, to \$76.6 million, compared to \$77.8 million for the same period in 2007. For the nine months ended September 30, 2008, interest income increased \$3.9 million, or 1.7%, to \$228.6 million, compared to \$224.8 million for the nine months ended September 30, 2007. Interest expense decreased \$7.3 million, or 18.8%, to \$31.3 million for the quarter ended September 30, 2008, compared to \$38.5 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, interest expense decreased \$6.6 million, or 6.1%, to \$101.5 million, compared to \$108.2 million for the nine months ended September 30, 2007. The changes in interest income and expense for the three months ended September 30, 2008, versus the comparable 2007 period reflected decreased short-term interest rates and a steepening yield curve, as the Federal Open Market Committee of the Federal Reserve Bank reduced the Federal funds rate by 225 basis points from 4.25% through April of 2008. The changes in interest income and expense for the nine months ended September 30, 2008, versus the comparable 2007 period were also impacted by increases in the average volume of interest-earning assets and interest-bearing liabilities attributable to the April 1, 2007 acquisition of First Morris.

The Company's net interest margin increased 30 basis points to 3.27% for the quarter ended September 30, 2008, compared to 2.97% for the quarter ended September 30, 2007. The net interest margin for the quarter ended September 30, 2008, increased 17 basis points from the trailing quarter net interest margin of 3.10%. The net interest margin increased 8 basis points to 3.08% for the nine months ended September 30, 2008, from 3.00% for the same period in 2007. The net interest spread was 2.96% for the quarter ended September 30, 2008, compared with 2.53% for the same period in 2007 and 2.76% for the trailing quarter. For the nine months ended September 30, 2008, the net interest spread was 2.74%, compared with 2.55% for the same period in 2007.

The average yield on interest-earning assets decreased 36 basis points to 5.51% for the quarter ended September 30, 2008, compared to 5.87% for the comparable quarter in 2007. Compared to the trailing quarter, the yield on interest-earning assets increased 1 basis point from 5.50%. For the nine months ended September 30, 2008, the yield on interest-earning assets decreased 26 basis points to 5.54%, from 5.80% for the same period in 2007.

The average cost of interest-bearing liabilities decreased 79 basis points to 2.55% for the quarter ended September 30, 2008, compared to 3.34% for the quarter ended September 30, 2007. Compared to the trailing quarter, the average cost of interest-bearing liabilities decreased 19 basis points from 2.74%. For the nine months ended September 30, 2008, the average cost of interest-bearing liabilities decreased 45 basis points to 2.80%, from 3.25% for the same period in 2007.

The average balance of net loans increased \$175.9 million, or 4.3%, to \$4.29 billion for the quarter ended September 30, 2008, compared to \$4.12 billion for the same period in 2007. Income on loans secured by real estate decreased \$326,000, or 0.8%, to \$42.5 million for the three months ended September 30, 2008, compared to \$42.8 million for the three months ended September 30, 2007. Interest income on commercial loans decreased \$882,000, or 7.6%, to \$10.7 million for the quarter ended September 30, 2008, compared to \$11.5 million for the quarter ended September 30, 2007. Consumer loan interest income decreased \$1.1 million, or 11.0%, to \$9.1 million for the quarter ended September 30, 2008, compared to \$10.2 million for the quarter ended September 30, 2007. The average loan yield for the three months ended September 30, 2008 was 5.78%, compared with 6.24% for the same period in 2007.

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For the nine months ended September 30, 2008, the average balance of net loans increased \$269.4 million, or 6.8%, to \$4.24 billion, compared to \$3.98 billion for the same period in 2007. Income on loans secured by real estate decreased \$909,000, or 0.7%, to \$124.4 million for the nine months ended September 30, 2008, compared to \$125.3 million for the nine months ended September 30, 2007. Interest income on commercial loans increased \$2.7 million, or 9.0%, to \$32.6 million for the nine months ended September 30, 2008, compared to \$29.9 million for the nine months ended September 30, 2007. Consumer loan interest income decreased \$1.1 million, or 3.9%, to \$27.9 million for the nine months ended September 30, 2008, compared to \$29.1 million for the nine months ended September 30, 2007. The average loan yield for the nine months ended September 30, 2008, was 5.81%, compared with 6.19% for the same period in 2007.

Interest income on investment securities held to maturity decreased \$196,000, or 5.2%, to \$3.6 million for the quarter ended September 30, 2008, compared to \$3.8 million for the quarter ended September 30, 2007. Average investment securities held to maturity totaled \$354.6 million for the quarter ended September 30, 2008, compared with \$369.5 million for the same period last year. For the nine months ended September 30, 2008, interest income on investment securities held to maturity decreased \$804,000, or 6.9%, to \$10.9 million, compared to \$11.7 million for the same period in 2007. Average investment securities held to maturity totaled \$354.7 million for the nine months ended September 30, 2008, compared with \$377.5 million for the same period last year.

Interest income on securities available for sale increased \$1.4 million, or 14.4%, to \$10.8 million for the quarter ended September 30, 2008, compared to \$9.4 million for the quarter ended September 30, 2007. Average securities available for sale were \$855.0 million for the three months ended September 30, 2008, compared with \$765.5 million for the same period in 2007. For the nine months ended September 30, 2008, interest income on securities available for sale increased \$3.8 million, or 13.1%, to \$32.4 million, compared to \$28.6 million for the nine months ended September 30, 2007. Average securities available for sale were \$843.6 million for the nine months ended September 30, 2008, compared with \$786.0 million for the same period in 2007. The average yield on all securities was 4.59% and 4.64% for the three and nine months ended September 30, 2008, respectively, compared with 4.55% and 4.50% for the same respective periods in 2007.

The average balance of interest-bearing core deposit accounts increased \$81.2 million, or 3.9%, to \$2.17 billion for the quarter ended September 30, 2008, compared to \$2.09 billion for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, average interest-bearing core deposits increased \$148.1 million, or 7.4%, to \$2.14 billion, compared with \$1.99 billion for the same period in 2007. Average time deposit account balances decreased \$213.9 million, or 12.5%, to \$1.49 billion for the quarter ended September 30, 2008, compared to \$1.71 billion for the same period in 2007. For the nine months ended September 30, 2008, average time deposits decreased \$105.5 million, or 6.3%, to \$1.56 billion, compared with \$1.66 billion for the same period in 2007. Interest paid on deposit accounts decreased \$10.2 million, or 33.6%, to \$20.1 million for the quarter ended September 30, 2008, compared to \$30.3 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, interest paid on deposit accounts decreased \$14.7 million, or 17.6%, to \$68.9 million, compared to \$83.7 million for the nine months ended September 30, 2007. The average cost of interest-bearing deposits was 2.19% and 2.49% for the three and nine months ended September 30, 2008, respectively, compared with 3.17% and 3.06% for the three and nine months ended September 30, 2007, respectively.

Average borrowings increased \$441.3 million, or 56.2%, to \$1.23 billion for the quarter ended September 30, 2008, compared to \$785.8 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, average borrowings increased \$350.9 million, or 44.7%, to \$1.14 billion, compared to \$785.6 million for the nine months ended September 30, 2007. Interest paid on borrowed funds increased \$2.9 million, or 35.4%, to \$11.2 million for the quarter ended September 30, 2008, from \$8.2 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008, interest paid on borrowed funds increased \$8.1 million, or 33.0%, to \$32.6 million, from \$24.5 million for the nine months ended September 30, 2007. The average cost of borrowings was 3.62% and 3.83% for the three and nine months ended September 30, 2008, respectively, compared with 4.16% and 4.17% for the three and nine months ended September 30, 2007, respectively.

*Provision for Loan Losses.* Provisions for loan losses are charged to operations in order to maintain the allowance for loan losses at a level management considers adequate to absorb probable credit losses inherent in the loan portfolio. In determining the level of the allowance for loan losses, management considers past and current loss experience, evaluations of real estate collateral, current economic conditions, volume and type of lending, adverse situations that may affect a borrower's ability to repay the loan

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and the levels of non-performing and other classified loans. The amount of the allowance is based on estimates, and the ultimate losses may vary from such estimates as more information becomes available or later events change. Management assesses the allowance for loan losses on a quarterly basis and makes provisions for loan losses in order to maintain the adequacy of the allowance. The Company's emphasis on continued diversification of the loan portfolio through the origination of commercial mortgage loans, commercial loans and construction loans has been one of the more significant factors management has considered in evaluating the allowance for loan losses and provision for loan losses. In the event the Company further increases the amount of such types of loans in the portfolio, management may determine that additional or increased provisions for loan losses are necessary, which could adversely affect earnings.

The Company recorded provisions for loan losses of \$3.8 million and \$6.6 million for the three and nine months ended September 30, 2008, respectively. This compares with provisions for loan losses of \$1.3 million and \$2.8 million recorded for the three and nine months ended September 30, 2007, respectively. The increase in the provision for loan losses for the three and nine months ended September 30, 2008, compared with the same periods in 2007, was attributable to an increase in non-performing loans, year-over-year growth in the loan portfolio, and an increase in commercial loans as a percentage of the loan portfolio to 44.7% at September 30, 2008, from 44.0% at September 30, 2007, as well as ongoing uncertainty with respect to general economic conditions. Total non-performing loans as a percentage of total loans were 0.81% at September 30, 2008, compared with 0.81% at December 31, 2007, and 0.26% at September 30, 2007. The Company had net charge-offs of \$1.6 million and \$4.1 million for the three and nine months ended September 30, 2008, respectively, compared to net charge-offs of \$473,000 and \$468,000 for the same respective periods in 2007. The allowance for loan losses was \$43.3 million, or 0.99% of total loans at September 30, 2008, compared to \$40.8 million, or 0.95% of total loans at December 31, 2007, and \$37.6 million, or 0.89% of total loans at September 30, 2007.

*Non-Interest Income.* Non-interest income totaled \$7.8 million for the quarter ended September 30, 2008, a decrease of \$298,000 compared to the same period in 2007. Net losses on securities transactions totaled \$966,000 for the quarter ended September 30, 2008, compared with net gains of \$2,000 for the same period last year. The net securities losses for the current quarter included \$1.4 million of other-than-temporary impairment charges recognized on investments in a debt security issued by Lehman Brothers Holdings, Inc. and the common stock of two publicly-traded financial institutions. Partially offsetting the net securities losses, fee income for the quarter ended September 30, 2008 increased \$846,000, or 13.1%, compared to the same period in 2007, primarily as a result of increases in the value of equity fund holdings. In addition, other income declined \$157,000 for the quarter ended September 30, 2008, compared with the same period in 2007, as a result of a non-recurring gain on the sale of real estate recognized in 2007.

For the nine months ended September 30, 2008, non-interest income totaled \$23.2 million, a decrease of \$6.8 million, or 22.6%, compared to the same period in 2007. In 2007, the Company recorded a one-time gain on an insurance settlement of \$5.9 million, before taxes, related to the resolution of previously disclosed litigation. In addition, net losses on securities transactions totaled \$565,000 for the nine months ended September 30, 2008, compared with net losses of \$61,000 for the same period in 2007.

*Non-Interest Expense.* For the three months ended September 30, 2008, non-interest expense decreased \$3.7 million, or 10.5%, to \$32.0 million, compared to \$35.7 million for the three months ended September 30, 2007. For the three months ended September 30, 2008, compensation and benefits expense decreased \$4.3 million, compared with the same period in 2007. Compensation and benefits expense decreased as a result of previous staff reductions and lower stock-based compensation costs. The Company recorded \$3.2 million in severance charges during the quarter ended September 30, 2007. Amortization of intangibles decreased \$304,000 for the three months ended September 30, 2008, compared with the same period in 2007, as a result of scheduled reductions in the amortization of core deposit intangibles. Partially offsetting these decreases, other operating expenses increased \$427,000 for the quarter ended September 30, 2008, compared with the same period in 2007, due primarily to expenses related to foreclosed assets.

For the nine months ended September 30, 2008, non-interest expense decreased \$2.0 million, or 2.0%, to \$97.2 million, compared to \$99.2 million for the nine months ended September 30, 2007. Compensation and benefits expense decreased \$4.0 million, as a result of previous staff reductions and lower stock-based compensation costs. The Company incurred \$773,000 in pre-tax severance costs during the second quarter of 2008, compared with \$3.2 million in severance charges recognized during the quarter ended September 30, 2007. Advertising costs decreased \$352,000 for the nine months ended September 30, 2008, compared with the same period in 2007, as prior year costs included charges related to the First Morris acquisition. Amortization of intangibles

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decreased \$209,000 for the nine months ended September 30, 2008, compared with the same period in 2007, as a result of scheduled reductions in the amortization of core deposit intangibles. Partially offsetting these decreases, other operating expenses increased \$1.4 million for the nine months ended September 30, 2008, compared with the same period in 2007, due to increases in several categories, including an expense of \$356,000 associated with the Company's proportionate share of a litigation reserve established by Visa, as well as increases in attorney fees and costs associated with foreclosed assets. Net occupancy expense increased \$1.2 million for the nine months ended September 30, 2008, compared with the same period in 2007, due primarily to the addition of nine branch locations in connection with the acquisition of First Morris.

The Company's annualized non-interest expense as a percentage of average assets improved to 1.98% for the quarter ended September 30, 2008, compared with 2.30% for the same period in 2007. For the nine months ended September 30, 2008, non-interest expense as a percentage of average assets was 2.04%, compared with 2.21% for the same period in 2007. The efficiency ratio (non-interest expense divided by the sum of net interest income and non-interest income) improved to 60.16% for the quarter ended September 30, 2008, compared with 75.41% for the same period in 2007. For the nine months ended September 30, 2008, the efficiency ratio was 64.66%, compared with 67.65% for the same period in 2007.

*Income Tax Expense.* For the three months ended September 30, 2008, the Company's income tax expense was \$4.2 million, compared with \$2.1 million for the same period in 2007. For the nine months ended September 30, 2008, the Company's income tax expense was \$12.3 million, compared with \$11.9 million for the same period in 2007. The increase in income tax expense was primarily attributable to increased income before income taxes. For the three and nine months ended September 30, 2008, the Company's effective tax rates were 24.2% and 26.5%, respectively, compared with 20.2% and 26.7% for the three and nine months ended September 30, 2007, respectively. The effective tax rates for the three and nine months ended September 30, 2008 were favorably impacted by the utilization of capital losses on securities transactions. The effective tax rates for the three and nine months ended September 30, 2007 reflected a larger proportion of the Company's income being derived from tax-exempt sources, primarily as a result of lower pre-tax income in 2007 due to \$3.2 million in severance charges recorded during the quarter ended September 30, 2007.

**Table of Contents****Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

*Qualitative Analysis.* Interest rate risk is the exposure of a bank's current and future earnings and capital arising from adverse movements in interest rates. The guidelines of the Company's interest rate risk policy seek to limit the exposure to changes in interest rates that affect the underlying economic value of assets and liabilities, earnings and capital. To minimize interest rate risk, the Company generally sells all 20- and 30-year fixed-rate mortgage loans at origination. Commercial real estate loans generally have interest rates that reset in five years, and other commercial loans such as construction loans and commercial lines of credit reset with changes in the prime rate, the federal funds rate or LIBOR. Investment securities purchases generally have maturities of five years or less, and mortgage-backed securities have weighted average lives between three and five years.

The Asset/Liability Committee meets on a monthly basis to review the impact of interest rate changes on net interest income, net interest margin, net income and the economic value of equity. The Asset/Liability Committee reviews a variety of strategies that project changes in asset or liability mix, various interest rate scenarios and the impact of those changes on projected net interest income and net income.

The Company endeavors to acquire and retain core deposit accounts and expand customer relationships in order to maintain a less interest rate sensitive funding base. The Company's ability to retain maturing certificate of deposit accounts is the result of its strategy to remain competitively priced within its marketplace, typically within the upper quartile of rates offered by its competitors. Pricing strategy may vary depending upon current funding needs and the ability of the Company to fund operations through alternative sources, primarily by accessing short-term lines of credit with the FHLB-NY during periods of pricing dislocation.

*Quantitative Analysis.* Current and future sensitivity to changes in interest rates are measured through the use of balance sheet and income simulation models. The analyses capture changes in net interest income using flat rates as a base, a most likely rate forecast and rising and declining interest rate forecasts. Changes in net interest income and net income for the forecast period, generally twelve to twenty-four months, are measured and compared to policy limits for acceptable change. The Company periodically reviews historical deposit re-pricing activity and makes modifications to certain assumptions used in its income simulation model regarding the interest rate sensitivity of deposits without maturity dates. These modifications are made to more precisely reflect most likely results under the various interest rate change scenarios. Since it is inherently difficult to predict the sensitivity of interest-bearing deposits to changes in interest rates, the changes in net interest income due to changes in interest rates cannot be precisely predicted. There are a variety of reasons that may cause actual results to vary considerably from the predictions presented below which include, but are not limited to, the timing, magnitude, and frequency of changes in interest rates, interest rate spreads, prepayments, and actions taken in response to such changes. Specific assumptions used in the simulation model include:

Parallel yield curve shifts for market rates;

Current asset and liability spreads to market interest rates are fixed;

Traditional savings and interest-bearing demand accounts move at 10% of the rate ramp in either direction;

Money Market accounts move at 5% of the rate ramp in either direction; and

Higher-balance demand deposit tiers and promotional demand accounts move at 50% of the rate ramp in either direction.

The following table sets forth the results of a twelve-month net interest income projection model as of September 30, 2008 (dollars in thousands):

| Change in Interest Rates in | Net Interest Income |               |                |
|-----------------------------|---------------------|---------------|----------------|
|                             | Dollar Amount       | Dollar Change | Percent Change |
| Basis Points (Rate Ramp)    |                     |               |                |
| -200                        | \$ 187,099          | \$ 831        | 0.4%           |

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|               |         |         |        |
|---------------|---------|---------|--------|
| <b>-100</b>   | 188,059 | 1,791   | 1.0%   |
| <b>Static</b> | 186,268 |         |        |
| <b>+100</b>   | 184,310 | (1,958) | (1.1%) |
| <b>+200</b>   | 182,082 | (4,186) | (2.2%) |



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The preceding table indicates that as of September 30, 2008, in the event of a 200 basis point increase in interest rates whereby rates ramp up evenly over a twelve-month period, net interest income would decrease 2.2%, or \$4.2 million. In the event of a 200 basis point decrease in interest rates, net interest income is projected to increase 0.4%, or \$831,000.

Another measure of interest rate sensitivity is to model changes in economic value of equity through the use of immediate and sustained interest rate shocks. The following table illustrates the result of the economic value of equity model as of September 30, 2008 (dollars in thousands):

| Change in Interest Rates<br>(Basis Points) | Present Value of Equity |                  |                   | Present Value of Equity as<br>Percent of Present Value<br>of Assets |                   |
|--|-------------------------|------------------|-------------------|---|-------------------|
|  | Dollar<br>Amount        | Dollar<br>Change | Percent<br>Change | Present Value<br>Ratio  | Percent<br>Change |
| -200                                       | \$ 1,405,241            | \$ 84,856        | 6.4%              | 20.4%   | 4.1%              |
| -100                                       | 1,381,287               | 60,902           | 4.6               | 20.2  | 3.1               |
| Flat                                       | 1,320,385               |                  |                   | 19.6  |                   |
| +100                                       | 1,235,473               | (84,912)         | (6.4)             | 18.7  | (4.8)             |
| +200                                       | 1,118,046               | (202,339)        | (15.3)            | 17.2  | (12.2)            |

The above table indicates that as of September 30, 2008, in the event of an immediate and sustained 200 basis point increase in interest rates, the present value of equity is projected to decrease 15.3%, or \$202.3 million. If rates were to decrease 200 basis points, the model forecasts a 6.4%, or \$84.9 million increase in the present value of equity.

Certain shortcomings are inherent in the methodologies used in the above interest rate risk measurements. Modeling changes in net interest income requires the use of certain assumptions regarding prepayment and deposit decay rates, which may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. While management believes such assumptions are reasonable, there can be no assurance that assumed prepayment rates and decay rates will approximate actual future loan prepayment and deposit withdrawal activity. Moreover, the net interest income table presented assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or re-pricing of specific assets and liabilities. Accordingly, although the net interest income table provides an indication of the Company's interest rate risk exposure at a particular point in time, such measurement is not intended to and does not provide a precise forecast of the effect of changes in market interest rates on the Company's net interest income and will differ from actual results.

**Item 4. CONTROLS AND PROCEDURES.**

Under the supervision and with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934) were evaluated at the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. There has been no change in the Company's internal control over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II OTHER INFORMATION****Item 1. Legal Proceedings**

The Company is involved in various legal actions and claims arising in the normal course of business. In the opinion of management, these legal actions and claims are not expected to have a material adverse impact on the Company's financial condition and results of operations.

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**Item 1A. Risk Factors**

Except for the additional risk factor described below, there are no material changes to the risk factors as previously disclosed in Item 1A of Part I of the Company's 2007 Form 10-K.

**Our Expenses Will Increase As A Result Of Increases In FDIC Insurance Premiums**

The Federal Deposit Insurance Corporation ( FDIC ) imposes an assessment against financial institutions for deposit insurance. This assessment is based on the risk category of the institution and currently ranges from 5 to 43 basis points of the institution's deposits. Federal law requires that the designated reserve ratio for the deposit insurance fund be established by the FDIC at 1.15% to 1.50% of estimated insured deposits. If this reserve ratio drops below 1.15% or the FDIC expects that it will do so within six months, the FDIC must, within 90 days, establish and implement a plan to restore the designated reserve ratio to 1.15% of estimated insured deposits within five years (absent extraordinary circumstances).

Recent bank failures coupled with deteriorating economic conditions have significantly reduced the deposit insurance fund's reserve ratio. As of June 30, 2008, the designated reserve ratio was 1.01% of estimated insured deposits at March 31, 2008. As a result of this reduced reserve ratio, on October 16, 2008, the FDIC published a proposed rule that would restore the reserve ratios to its required level. The proposed rule would raise the current deposit insurance assessment rates uniformly for all institutions by 7 basis points (to a range from 12 to 50 basis points) for the first quarter of 2009. The proposed rule would also alter the way the FDIC calculates federal deposit insurance assessment rates beginning in the second quarter of 2009 and thereafter.

Under the proposed rule, the FDIC would first establish an institution's initial base assessment rate. This initial base assessment rate would range, depending on the risk category of the institution, from 10 to 45 basis points. The FDIC would then adjust the initial base assessment (higher or lower) to obtain the total base assessment rate. The adjustments to the initial base assessment rate would be based upon an institution's levels of unsecured debt, secured liabilities, and brokered deposits. The total base assessment rate would range from 8 to 77.5 basis points of the institution's deposits.

In addition, the Emergency Economic Stabilization Act of 2008 (EESA) temporarily increased the limit on FDIC insurance coverage for deposits to \$250,000 through December 31, 2009, and the FDIC took action to provide coverage for newly-issued senior unsecured debt and non-interest bearing transaction accounts in excess of the \$250,000 limit, for which institutions will be assessed additional premiums.

These actions will significantly increase the Company's non-interest expense in 2009 and in future years as long as the increased premiums are in place.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.****ISSUER PURCHASES OF EQUITY SECURITIES**

| <b>Period</b>                                | <b>(a) Total Number of Shares (or Units) Purchased</b> | <b>(b) Average Price Paid per Share (or Unit)</b> | <b>(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (1)</b> | <b>(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased under the Plans or Programs (1)</b> |
|--|--|---|--|--|
| July 1, 2008 through July 31, 2008           | 3,987  | \$ 14.49  | 3,987  | 2,212,185  |
| August 1, 2008 through August 31, 2008       | 60,932   | 14.47   | 60,932   | 2,151,253  |
| September 1, 2008 through September 30, 2008 | 1,105  | 19.50   | 1,105  | 2,150,148  |
| <b>Total</b>                                 | <b>66,024</b>  | <b>\$ 14.56</b>                                   | <b>66,024</b>  |  |

- (1) On October 24, 2007, the Company's Board of Directors approved the purchase of up to 3,107,077 shares of its common stock under a seventh general repurchase program which commenced upon completion of the previous program. The repurchase program has no expiration date.

**Item 3. Defaults Upon Senior Securities.**

Not Applicable

**Item 4. Submission of Matters to a Vote of Security Holders.**

None.

**Item 5. Other Information.**

None.

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**Item 6. Exhibits.**

The following exhibits are filed herewith:

- 3.1 Certificate of Incorporation of Provident Financial Services, Inc.\*
- 3.2 Second Amended and Restated Bylaws of Provident Financial Services, Inc.\*\*\*\*\*
- 4.1 Form of Common Stock Certificate of Provident Financial Services, Inc. \*
- 10.1 Form of Employment Agreement between Provident Financial Services, Inc. and certain executive officers. \*
- 10.2 Form of Change in Control Agreement between Provident Financial Services, Inc. and certain executive officers. \*
- 10.3 Amended and Restated Employee Savings Incentive Plan, as amended. \*\*
- 10.4 Employee Stock Ownership Plan\* and Amendment No. 1 to the Employee Stock Ownership Plan. \*\*
- 10.5 Amended and Restated Supplemental Executive Retirement Plan. \*\*
- 10.6 Amended and Restated Supplemental Executive Savings Plan, as amended. \*\*
- 10.7 Retirement Plan for the Board of Directors of The Provident Bank, as amended. \*
- 10.8 Amendment No. 1 and Amendment No. 2 to The Provident Bank Amended and Restated Board of Directors Voluntary Fee Deferral Plan. \*\*
- 10.9 Voluntary Bonus Deferral Plan, as amended. \*
- 10.10 Provident Financial Services, Inc. Board of Directors Voluntary Fee Deferral Plan, as amended. \*\*
- 10.11 First Savings Bank Directors Deferred Fee Plan, as amended. \*\*\*
- 10.12 The Provident Bank 2005 Board of Directors Voluntary Fee Deferral Plan. \*\*\*\*
- 10.13 The Provident Bank Non-Qualified Supplemental Employee Stock Ownership Plan. \*\*\*\*
- 10.14 Provident Financial Services, Inc. 2003 Stock Option Plan. \*\*\*\*\*
- 10.15 Provident Financial Services, Inc. 2003 Stock Award Plan. \*\*\*\*\*
- 10.16 Provident Financial Services, Inc. 2008 Long-Term Equity Incentive Plan. \*\*\*\*\*
- 10.17 Separation Agreement by and between Provident Financial Services, Inc., The Provident Bank and Kevin J. Ward dated December 20, 2007. \*\*\*\*\*
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

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- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- \* Filed as exhibits to the Company's Registration Statement on Form S-1, and any amendments thereto, with the Securities and Exchange Commission (Registration No. 333-98241).
- \*\* Filed as exhibits to the Company's June 30, 2004 Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission (File No. 001-31566).
- \*\*\* Filed as an exhibit to the Company's September 30, 2004 Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission (File No. 001-31566).
- \*\*\*\* Filed as exhibits to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 29, 2004 (File No. 001-31566).
- \*\*\*\*\* Filed as exhibits to the Company's Proxy Statement for the 2003 Annual Meeting of Stockholders filed with the Securities and Exchange Commission on June 4, 2003 (File No. 001-31566).
- \*\*\*\*\* Filed as an exhibit to the Company's December 31, 2007 Annual Report to Stockholders on Form 10-K filed with the Securities and Exchange Commission on February 29, 2008 (File No. 001-31566).
- \*\*\*\*\* Filed as an exhibit to the Company's Proxy Statement for the 2008 Annual Meeting of Stockholders filed with the Securities and Exchange Commission on March 14, 2008 (File No. 001-31566).

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**PROVIDENT FINANCIAL SERVICES, INC.**

Date: November 10, 2008

By: /s/ Paul M. Pantozzi  
Paul M. Pantozzi  
Chairman and Chief Executive Officer  
(Principal Executive Officer)

Date: November 10, 2008

By: /s/ Linda A. Niro  
Linda A. Niro  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)

Date: November 10, 2008

By: /s/ Thomas M. Lyons  
Thomas M. Lyons  
First Vice President and Chief Accounting Officer  
(Principal Accounting Officer)