ALLEGIANT BANCORP INC/MO/
Form 10-Q
May 15, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 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 MARCH 31, 2003

Commission file number 000-10849

ALLEGIANT BANCORP, INC.

(Exact name of registrant as specified in its charter)

MISSOURI	43-1262037
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

10401 CLAYTON ROAD
ST. LOUIS, MISSOURI 63131

(Address of principal executive offices)
(Zip Code)

(314) 692-8800

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. /X/ Yes / / No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). /X/ Yes / / No

Title of class	Number of shares outstanding as of May 2, 2003
Common stock, $0.01 par value	17,326,835

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALLEGIANT BANCORP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2003 (Unaudited)	Dec
		(Dollars
ASSETS:		
Cash and due from banks	$ 48,016	$
Federal funds sold and other investments	38,270	
Investment securities:		
Available-for-sale (at estimated market value)	389,041	
Held-to-maturity (estimated market value of $12,878, $17,300 and $20,931, respectively)	12,661	
Loans, net of allowance for loan losses of $18,730, $19,567 and $17,530, respectively	1,645,443	1
Loans held for sale	25,874	
Premises and equipment	44,170	
Accrued interest and other assets	69,835	
Cost in excess of fair value of net assets acquired	54,168	
Total assets	$2,327,478	$2
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Deposits:		
Non-interest bearing	$ 197,306	$
Interest bearing	1,315,660	1
Certificates of deposit over $100,000	208,797	
Total deposits	1,721,763	1
Short-term borrowings	78,558	
Federal Home Loan Bank advances	302,895	
Guaranteed preferred beneficial interests in subordinated debentures	57,250	
Accrued expenses and other liabilities	12,904	
Total liabilities	2,173,370	2
Shareholders' equity:		
Common Stock, $0.01 par value - authorized 30,000,000 shares; issued 16,220,542 shares, 16,146,804 shares and 15,541,085 shares, respectively	162	
Capital surplus	121,363	
Retained earnings	49,219	
Accumulated other comprehensive income (loss)	1,264	
Treasury stock, at cost, 974,150 shares	(17,900)	
Total shareholders' equity	154,108	
Total liabilities and shareholders' equity	$2,327,478	$2

See Notes to Condensed Consolidated Financial Statements.

ALLEGIANT BANCORP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended March 31,	
	(In thousands, except share and pe share data)	
	2003	2002
Interest income:		
Interest and fees on loans	$ 25,671	$ 25,107
Investment securities	4,121	5,071
Federal funds sold and overnight investments	49	56
Total interest income	29,841	30,234
Interest expense:		
Deposits	8,805	10,646
Short-term borrowings	1,230	648
Federal Home Loan Bank advances	2,093	2,466
Guaranteed preferred beneficial interests in subordinated debentures	1,372	1,372
Total interest expense	13,500	15,132
Net interest income	16,341	15,102
Provision for loan losses	1,660	1,500
Net interest income after provision for loan losses	14,681	13,602
Non-interest income:		
Service charges on deposits	1,685	1,627
Net gain on sale of securities	1,723	10
Other income	3,613	2,425
Total non-interest income	7,021	4,062
Non-interest expense:		
Salaries and employee benefits	7,127	5,604
Occupancy and furniture and equipment	1,922	1,628
Other operating expenses	4,437	3,461
Total non-interest expense	13,486	10,693
Income before income taxes	8,216	6,971
Provision for income taxes	2,663	2,023
Net income	$ 5,553	$ 4,948

Per share data:		
Earnings per share:		
Basic	$ 0.34	$ 0.32
Diluted	0.34	0.32
Weighted average common shares outstanding:		
Basic	16,186,628	15,380,960
Diluted	16,509,453	15,675,429

See Notes to Condensed Consolidated Financial Statements.

ALLEGIANT BANCORP, INC.
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income Gain (Loss)	Treasury Stock
				(In thousands)	
Balance December 31, 2002	$ 161	$ 119,933	$ 44,614	$ 2,534	$ -
Net income	-	-	5,553	-	-
Change in net unrealized losses on available-for-sale securities, net of tax	-	-	-	(1,270)	-
Comprehensive income	-	-	-	-	-
Issuance of common stock	1	840	-	-	-
Amortization of restricted stock	-	590	-	-	-
Repurchase of common stock	-	-	-	-	(17,900)
Dividends ($0.07 per share)	-	-	(948)	-	-
Balance March 31, 2003	$ 162	$ 121,363	$ 49,219	$ 1,264	$ (17,900)

See Notes to Condensed Consolidated Financial Statements.

ALLEGIANT BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Three Months E March 31,	
	2003	
	(In thousand	
OPERATING ACTIVITIES:		
Net income	$ 5,553	$
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,767	
Provision for loan losses	1,660	
Net gain on sale of fixed assets	(17)	
Net realized gains on securities available-for-sale	(1,723)	
Other changes in assets and liabilities:		
Accrued interest receivable and other assets	2,522	
Accrued expenses and other liabilities	2,114	
Cash provided by (used in) operating activities	11,876	
INVESTING ACTIVITIES:		
Adjustment to cash received in acquisition of branches	-	
Decrease in cash and cash equivalents resulting from sale of divested subsidiary	(14,870)	
Proceeds from maturities of securities held-to-maturity	1,041	
Proceeds from maturities of securities available-for-sale	104,061	
Proceeds from sales of securities available-for-sale	93,614	
Purchase of investment securities available-for-sale	(194,163)	
Loans made to customers, net of repayments	8,278	
Purchase of bank-owned life insurance	(441)	
Additions to premises and equipment	(1,037)	
Cash used in investing activities	(3,517)	
FINANCING ACTIVITIES:		
Net increase (decrease) in deposits	47,600	
Net increase (decrease) in short-term borrowings	(16,337)	
Repayment of long-term debt	(360)	
Proceeds from issuance of common stock	841	
Payment of dividends	(948)	
Cash provided by (used in) financing activities	30,796	
Net increase (decrease) in cash and cash equivalents	39,155	
Cash and cash equivalents, beginning of period	47,131	
Cash and cash equivalents, end of period	$ 86,286	$

See Notes to Condensed Consolidated Financial Statements.

ALLEGIANT BANCORP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Basis of Presentation

The accompanying condensed consolidated financial statements include the accounts of Allegiant Bancorp, Inc. and its subsidiaries. The terms "Allegiant," "company," "we," "our," and "corporation" as used in this report refer to Allegiant Bancorp, Inc. and its subsidiaries as a consolidated entity, except where it is made clear that it means only Allegiant. Also, sometimes we refer to our principal bank subsidiary, Allegiant Bank as the "bank."

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003.

The balance sheet at December 31, 2002 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2002.

Comprehensive Income

During the first quarter of 2003 and 2002, total comprehensive income amounted to $4.3 million and $4.5 million, respectively.

Acquisitions and Divestitures

On March 31, 2003, we sold Bank of Ste. Genevieve, one of our two subsidiary banks, to First Banks, Inc. Bank of Ste. Genevieve operates two branches located outside of the St. Louis metropolitan area and had total assets of approximately $114.6 million at the time of the sale. First Banks acquired Bank of Ste. Genevieve in exchange for transferring to us 974,150 shares of our common stock held by First Banks. The net assets of Bank of Ste. Genevieve as of the closing were approximately $17.9 million which approximated the value of consideration we received. As a result, we did not recognize any gain or loss as a result of the transaction. First Banks held approximately 7.4% of our outstanding common stock prior to the sale and held approximately 1.5% of our common stock upon completion of the sale.

On March 19, 2003, we entered into a Purchase and Assumption Agreement with Heartland Bank, a federal savings association. Under the

purchase agreement, we will acquire Heartland's bank branch located at 4435 Chippewa, Saint Louis, Missouri. In addition to the branch facility, we will assume approximately $24.6 million in related deposit liabilities. Pursuant to the terms of the agreement, we will pay a purchase price equal to the dollar amount of Heartland's assets acquired as of the closing date of the transaction less a deposit premium equal to 5.05% of all assumed deposits. We expect to close the transaction in the third quarter of 2003.

On October 1, 2002, we completed the acquisition of Investment Counselors, Incorporated, a privately held investment advisory firm located in St. Louis, Missouri. Under the terms of the agreement, we exchanged 194,610 shares of our common stock for all of the common shares of Investment Counselors. We recorded goodwill and other identifiable intangibles of $2.7 million and $0.5 million, respectively. The other identifiable intangibles are being amortized over an estimated average life of approximately 14 years. This acquisition was consistent with our strategy of focusing on the growth of non-interest income and has allowed us to offer a more comprehensive selection of wealth management products and services. At March 31, 2003, Investment Counselors' assets under management totaled $325.4 million.

Recently Issued Accounting Standards

In November 2002, the Financial Accounting Standards Board (FASB) issued Interpretation No. 45, Guarantor's Accounting and Disclosure for Guarantees, Including Indirect Guarantees of Indebtedness of Others (FIN 45). FIN 45 requires certain guarantees to be recorded at fair value and applies to contracts or indemnification agreements that contingently require the guarantor to make payments to the guaranteed party based on changes related to an underlying asset, liability or equity security of the guaranteed party. The recognition requirements of FIN 45 are to be applied prospectively to guarantees issued or modified subsequent to December 31, 2002. FIN 45 also expands the disclosures to be made by guarantors, effective as of December 31, 2002, to include the nature of the guarantee, the maximum potential amount of future payments that the guarantor could be required to make under the guarantee, and the current amount of the liability, if any, for the guarantor's obligation under the guarantee.

At March 31, 2003, the maximum amount of future payments that the company could potentially be required to make under guarantees for standby letters of credit was $19.6 million. Standby letters of credit are conditional commitments issued by our banks to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support contractual obligations of our customers. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements, the likelihood of the counterparties drawing on such financial instruments and the present creditworthiness of such counterparties.

In December 2002, the FASB issued SFAS No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure, which provides transition guidance from accounting under APB Opinion No. 25, Accounting for Stock Issued to Employees, to SFAS No. 123, Accounting for Stock-Based

Compensation, which provides for a fair value method of accounting, if a company elects. We have elected to continue to account for stock-based employee compensation under APB Opinion No. 25. Accordingly, no stock option based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of the grant. The following table illustrates the effect on net income and earnings per share if the company applied the fair value recognition provisions of SFAS No. 123 to stock option based employee compensation.

	Three Months Ended March 31,	
	2003	2002
	(In thousands, except per share d	
Net income, as reported	$ 5,553	$ 4,94
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(280)	(24
Pro forma net income	$ 5,273	$ 4,70
Earnings per share:		
Basic - as reported	$ 0.34	$ 0.3
Basic - pro forma	0.33	0.3
Diluted - as reported	0.34	0.3
Diluted - pro forma	0.32	0.3

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

This report includes forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to risks, uncertainties and assumptions, including, among other things:

- the results of our efforts to implement our business strategy, including Project 2004;
- adverse changes in the bank's loan portfolio and the resulting credit risk-related losses and expenses;
- our ability to manage our growth, including the successful expansion of the customer support, administrative infrastructure and internal management systems necessary to manage that growth;
- our ability to attract core deposits;

- adverse changes in the economy of our market area that could increase credit-related losses and expenses;
- adverse changes in real estate market conditions that could negatively affect credit risk;
- the consequences of continued bank acquisitions and mergers in our market area, resulting in fewer but much larger and financially stronger competitors, which could increase competition for financial services to our detriment;
- fluctuations in interest rates and market prices, which could negatively affect net interest margins, asset valuations and expense expectations;
- changes in regulatory requirements of federal and state agencies applicable to bank holding companies and our present and future bank subsidiaries;
- changes in accounting principles;
- general economic conditions; and
- other risks and uncertainties detailed from time to time in our filings with the Securities and Exchange Commission.

We undertake no obligation to publicly update or otherwise revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the events discussed in any forward-looking statements in this report might not occur.

The profitability of our operations depends on our net interest income, provision for loan losses, non-interest income and non-interest expense. Net interest income is the difference between the income we receive on our loan and investment portfolios and our cost of funds, which consists of interest paid on deposits and borrowings. The provision for loan losses reflects the cost of credit risk in our loan portfolio. Non-interest income consists primarily of service charges on deposit accounts and fees for ancillary banking services and, to a lesser extent, revenues generated from our mortgage banking, securities brokerage, insurance brokerage and wealth management operations. Non-interest expense includes salaries and employee benefits as well as occupancy, data processing, marketing, professional fees, insurance and other expenses. Under recently adopted accounting rules, we will be required to periodically evaluate the carrying values of our goodwill balances to determine whether the values have been impaired. If we determine that there has been an impairment, we will recognize a charge to our earnings, which could be material.

Our net interest income depends on the amounts and yields of interest earning assets compared to the amounts and rates on interest bearing liabilities. Net interest income is sensitive to changes in market rates of interest and our asset/liability management procedures in managing those changes. The provision for loan losses is dependent on increases in the loan portfolio, management's assessment of the collectibility of the

loan portfolio and loss experience, as well as economic and market factors.

OVERVIEW

We are the largest publicly held bank holding company headquartered in the St. Louis metropolitan area. Our principal subsidiary, Allegiant Bank, offers full-service banking and personal trust services to individuals, businesses and municipalities in our market area. These services include commercial real estate, commercial business and consumer loans, checking, savings and time deposit accounts, wealth management and other fiduciary services, as well as other financial services, including mortgage banking, securities brokerage and insurance products. As of March 31, 2003, we reported, on a consolidated basis, total assets of $2.3 billion, loans of $1.7 billion and shareholders' equity of $154.1 million.

Our primary goal has been to expand our branch network in the St. Louis market while increasing our earnings per share. Since our inception in 1989, we have grown through a combination of internal growth and acquisitions. We have sought to maximize our internal growth opportunities by positioning Allegiant as one of the leading St. Louis community banks.

We have supplemented our internal growth with several acquisitions within our market area. Since 2000, we have completed a number of significant acquisitions, including: Equality Bancorp, Inc., a community-based thrift holding company with total assets of approximately $300.4 million, in November 2000; Southside Bancshares Corp., a community-based bank holding company with total assets of approximately $804.9 million, in September 2001; and five branches from Guardian Savings Bank with total deposits of $109.3 million, in December 2001. Additionally, in order to diversify our operations and sources of income, in October 2002, we acquired Investment Counselors, Incorporated, an investment advisory firm with approximately $331.9 million of assets under management.

Consistent with our focus on establishing and maintaining a strong presence in the most attractive areas in the St. Louis market, on March 31, 2003, we sold Bank of Ste. Genevieve, one of our two subsidiary banks, to First Banks, Inc. Bank of Ste. Genevieve operates two branches located outside of the St. Louis metropolitan area and had total assets of $114.6 million at the time of the sale. First Banks acquired Bank of Ste. Genevieve in exchange for transferring to us 974,150 shares of our common stock held by First Banks. The net assets of Bank of Ste. Genevieve as of the closing were approximately $17.9 million, which approximated the value of consideration we received. As a result, we did not recognize any gain or loss as a result of the transaction. First Banks held approximately 7.4% of our outstanding common stock prior to the sale and held approximately 1.5% of our common stock upon completion of the sale.

In order to improve the profitability of our banking operations, over the past several years we have reduced the number of residential mortgages that we hold in our portfolio and have increased the amount of higher yielding commercial loans. Since the beginning of 1998, and in part as a result of opportunities that resulted from the consolidation of the St. Louis banking market, we have hired 23 commercial lending professionals, including a senior credit officer, who average more than 15 years of commercial lending experience in the St. Louis metropolitan area. As these local loan officers have joined our banking team, we have benefited from

their existing customer relationships, as well as their local banking expertise. In addition, we have implemented a company-wide cost control initiative intended to enhance efficiencies throughout our organization that we refer to as "Project 2004" and we consolidated our banking operations into one primary subsidiary, Allegiant Bank, during 2002. These steps taken since the beginning of 1998 have improved our efficiency, return on average assets, return on average equity and earnings per share. Commercial business loans generally involve a higher degree of risk than our other types of loans.

The St. Louis metropolitan area is the 18th largest metropolitan market in the United States with a population of approximately 2.5 million. The St. Louis area is home to 15 Fortune 1000 companies, including Anheuser-Busch Companies, Inc., Emerson Electric Co. and The May Department Stores Company. Over the past several years, a number of financial institutions in our market area have been acquired by larger regional or national out-of-town financial institutions. These acquisitions have included: Marshall & Ilsley Corporation's 2002 acquisition of Mississippi Valley Bancshares, Inc., Firstar Corporation's (now operating as U.S. Bancorp) 1999 acquisition of Mercantile Bancorporation Inc., Union Planters Corporation's 1998 acquisition of Magna Group, Inc. and NationsBank Corporation's (now operating as Bank of America Corporation) 1997 acquisition of Boatmen's Bancshares, Inc. We believe we have capitalized on opportunities created by this market consolidation and have built a strong, customer-friendly, community-focused banking franchise.

We focus on serving customers with banking needs that no longer can be adequately served by smaller local institutions but who still desire the personalized service that larger, out-of-state institutions do not effectively provide. Our community banking focus and streamlined management and decision-making procedures allow us to respond quickly to the needs of our individual and business customers and to tailor products and services to meet their needs.

We seek to effectively meet the convenience and needs of customers through our extensive branch network that provides our customers at least one branch located within a 20-minute drive from all principal sectors of the St. Louis metropolitan area. Our 37 branches and 59 ATMs throughout the St. Louis metropolitan area also serve to increase recognition of the Allegiant name. In addition, we have sought to further enhance our name recognition by serving as the official bank of the St. Louis Rams football team since July 2000.

Project 2004

In August 2002, we announced the launch of Project 2004. The mission of Project 2004 is to improve our operating platform by leveraging our acquisition expertise internally. We are approaching this project as if we had acquired our own operations and have evaluated our systems and strategies in order to enhance our delivery of products and services to customers, to improve operating efficiencies and to provide increased revenue. Based on our evaluations, we have undertaken improvement initiatives, several of which have been completed.

Of our major initiatives, we expect to realize increases in incremental revenue, beginning in the second half of 2003, at a rate of more

than $750,000 annually from improvements in our retail banking sales training, measurement and tracking, and of up to $1.0 million annually from the implementation of a specialized marketing plan for our 11 smallest branches by deposit size. Our new sales measurement and tracking systems will improve management's ability to identify products and practices that are most profitable to us and focus our sales efforts on those products and practices. Our new training will improve our employees' ability to offer products to new and existing customers and to implement our most profitable practices. Our specialized marketing plan includes mail programs and special promotions directed to current and prospective customers in an effort to increase deposits at our smaller branches.

In addition, in the first half of 2003 we will implement a new fee structure, operating procedures and electronic processing systems from which we expect to realize improvements in operating efficiencies and incremental revenue at a rate of up to $1.0 million annually. Operating efficiencies we expect to achieve include more efficient branch staffing, implementation of an automated credit scoring system for consumer lending and streamlining a variety of backroom functions such as loan document imaging. We expect to achieve increases in incremental revenue through fees on new customer services, including an overdraft protection program for electronic transactions. However, we cannot assure you that we will be able to realize all of the estimated revenues or efficiencies from our Project 2004 initiatives.

RESULTS OF OPERATIONS

Net income for the three months ended March 31, 2003 was $5.6 million, a 12.2% increase over the $4.9 million earned in the first quarter of 2002. Basic and diluted earnings per share increased 6.3% to $0.34 for the first quarter of 2003 compared to $0.32 for the first quarter of 2002. The annualized return on average assets was 0.92% for both the first quarter of 2003 and 2002. The return on average equity on an annualized basis was 13.10% for the first quarter of 2003 compared to 13.95% for the first quarter of 2002.

As a result of recent accounting pronouncements, we discontinued the amortization of goodwill in 2002 and will periodically determine whether the carrying value of our goodwill is impaired. As required by these pronouncements, we continue to amortize core deposit premiums and other identifiable intangibles as a non-cash charge that increases our operating expenses. Intangible asset amortization included as an operating expense totaled $279,000 and $271,000 for the three-month periods ended March 31, 2003 and 2002, respectively.

Total assets at March 31, 2003 were $2.3 billion, an increase of $169.8 million, or 8%, from March 31, 2002, due largely to a $214.9 million, or 15%, increase in loans. Total loans increased to $1.7 billion and total deposits increased to $1.7 billion at March 31, 2003, reflecting a 15% and 5% increase from March 31, 2002, respectively. Consistent with our focus on establishing and maintaining a strong presence in the most attractive areas in the St. Louis market, in March 2003, we sold Bank of Ste. Genevieve, one of our two subsidiary banks, to First Banks, Inc. Bank of Ste. Genevieve operates two branches located outside of the St. Louis metropolitan area and had total assets of $114.6 million at the time of the sale.

At March 31, 2003, shareholders' equity totaled $154.1 million, an increase of 7% from March 31, 2002. On April 14, 2003 we completed a secondary public offering and issued 2.1 million shares of common stock at a public offering price of $16.50 per share. Net proceeds from the offering totaled $31.9 million. We contributed substantially all of the net proceeds to Allegiant Bank to strengthen the bank's capital position, to support the bank's anticipated loan growth and for other general corporate purposes. The bank has used a portion of the capital contributed to temporarily reduce short-term indebtedness, which may be reborrowed, if necessary, to fund loan growth. We will use the remaining proceeds that are not contributed to the bank for general corporate and working capital purposes.

Net Interest Income. Net interest income for the three months ended March 31, 2003 was $16.3 million, an 8% increase compared to the $15.1 million reported for the first quarter of 2002. The increase in net interest income was primarily attributable to a $247.4 million, or 13%, increase in average earning assets, due largely to a $228.6 million, or 15%, increase in average loans, as loan growth in our market remained strong. As a result of lower prevailing market rates, interest income decreased $393,000 from the first quarter of 2002 which was more than offset by a $1.6 million decrease in interest expense. The decrease in interest expense was the result of a 66 basis point decline in the average interest rate paid on interest bearing liabilities partially offset by a $211.3 million increase in average interest bearing liabilities.

Interest expense on deposits decreased $1.8 million from the first quarter of 2002. This decrease reflected a 66 basis point decline in the average rate paid on deposits from 2.91% in the first quarter of 2002 to 2.25% for the comparable period in 2003 which was partially offset by average deposit growth of 6.9%.

Interest expense on other interest bearing liabilities increased $209,000 in the first quarter of 2003 compared to the first quarter of 2002 as average short and long-term borrowings increased $109.1 million during the period, respectively. The average rate paid on short-term borrowings decreased 75 basis points while the rate paid on long-term borrowings decreased 21 basis points in the first quarter of 2003 compared to the first quarter of 2002.

The net interest margin in the first quarter of 2003 was 3.00% compared to 3.13% and 3.05% during the first and fourth quarters of 2002, respectively. The margin was negatively impacted as we reinvested the proceeds of certain securities transactions into temporary short-term investments. We expect our net interest margin to improve over the balance of the year, in view of our expectation that we should be able to re-invest these short-term investments into higher yielding loans and securities and that a portion of our deposits and borrowings will reprice at lower market rates. The net interest spread was 2.80% in the first quarter of 2003 compared to 2.90% in the first quarter of 2002 as the earning assets yield declined 77 basis points while the overall interest rate paid on interest bearing liabilities decreased 67 basis points.

The following table sets forth the condensed average balance sheets for the quarterly periods reported. Also shown is the average yield on each category of interest earning assets and the average rate paid on interest bearing liabilities for each of the periods reported.

DISTRIBUTION OF AVERAGE ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY AND INTERE

	Three Months Ended March			
	2003			
	Average Balance	Int. earned/ Paid	Yield/ Rate	Average Balance
	(Dollars in thousands)			
Assets:				
Interest earning assets:				
Loans(1) (2)	$ 1,709,113	$ 25,671	6.09%	$ 1,480,52
Taxable investment securities	442,407	3,745	3.43	427,29
Non-taxable investment securities(3)	36,257	376	4.21	35,78
Federal funds sold and other investments	17,757	49	1.12	14,52
Total interest earning assets	2,205,534	29,841	5.49	1,958,12
Non-interest earning assets:				
Cash and due from banks	45,892			41,76
Premises and equipment	47,811			48,10
Other assets	129,032			126,01
Allowance for loan losses	(19,360)			(18,70
Total assets	$ 2,408,909			$ 2,155,29
Liabilities and shareholders' equity:				
Interest bearing liabilities:				
Money market and NOW accounts	$ 428,753	$ 1,227	1.16%	$ 417,69
Savings deposits	226,123	845	1.52	203,56
Certificates of deposit	578,159	4,013	2.81	594,61
Certificates of deposit over $100,000	210,837	1,405	2.70	181,97
IRA certificates	83,075	922	4.50	87,24
Brokered deposits	60,335	393	2.64	
Total interest bearing deposits	1,587,282	8,805	2.25	1,485,08
Federal funds purchased, repurchase agreements and other short-term borrowings	218,085	1,230	2.29	86,57
Other borrowings	173,032	2,093	4.91	195,43
Guaranteed preferred beneficial interest in subordinated debentures	57,250	1,372	9.72	57,25
Total interest bearing liabilities	2,035,649	13,500	2.69	1,824,34
Non-interest bearing liabilities and equity:				
Demand deposits	190,771			171,62
Other liabilities	12,955			17,47
Shareholders' equity	169,534			141,85
Total liabilities and shareholders'				

equity.....	$ 2,408,909			$ 2,155,29
Net interest income.....		$ 16,341		
Net interest spread.....			2.80%	
Net interest margin.....			3.00	