FIRST COMMUNITY BANCSHARES INC /NV/
Form 10-Q
May 11, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarter ended March 31, 2009
Commission file number 000-19297
FIRST COMMUNITY BANCSHARES, INC.
(Exact name of registrant as specified in its charter)

Nevada	**55-0694814**
(State or other jurisdiction of incorporation)	(IRS Employer Identification No.)
P.O. Box 989 **Bluefield, Virginia**	**24605-0989**
(Address of principal executive offices)	(Zip Code)

(276) 326-9000
(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 the to such filing requirements for the past 90 days.
Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes o No o

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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o	Smaller reporting company o
		(Do not check if a 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 o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.
Class Common Stock, $1.00 Par Value; 11,596,249 shares outstanding as of May 4, 2009

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PART I. ITEM 1. Financial Statements

FIRST COMMUNITY BANCSHARES, INC.
CONSOLIDATED BALANCE SHEETS

(Dollars in Thousands, Except Per Share Data)	**March 31, 2009 (Unaudited)**	**December 31, 2008***
Assets		
Cash and due from banks	$ 32,758	$ 39,310
Interest-bearing balances with banks	68,202	7,129
Total cash and cash equivalents	100,960	46,439
Securities available-for-sale	549,664	520,723
Securities held-to-maturity	8,471	8,670
Loans held for sale	1,445	1,024
Loans held for investment, net of unearned income	1,276,790	1,298,159
Less allowance for loan losses	16,555	15,978
Net loans held for investment	1,260,235	1,282,181
Premises and equipment	54,893	55,024
Other real estate owned	3,114	1,326
Interest receivable	8,848	10,084
Goodwill and other intangible assets	89,338	89,612
Other assets	122,173	118,231
Total Assets	$ 2,199,141	$ 2,133,314
Liabilities		
Deposits:		
Noninterest-bearing	$ 207,947	$ 199,712
Interest-bearing	1,375,497	1,304,046
Total Deposits	1,583,444	1,503,758
Interest, taxes and other liabilities	28,293	27,423
Securities sold under agreements to repurchase	153,824	165,914
FHLB borrowings and other indebtedness	215,870	215,877
Total Liabilities	1,981,431	1,912,972
Stockholders Equity		
Preferred stock, par value undesignated; 1,000,000 shares authorized; 41,500 issued at March 31, 2009, and December 31, 2008	40,471	40,419
Common stock, $1 par value; 25,000,000 shares authorized; 12,051,234 shares issued at March 31, 2009, and December 31, 2008, including 454,985 and 483,785 shares in treasury, respectively	12,051	12,051
Additional paid-in capital	127,992	128,526

Retained earnings	118,021	107,231
Treasury stock, at cost	(14,453)	(15,368)
Accumulated other comprehensive loss	(66,372)	(52,517)
Total Stockholders Equity	217,710	220,342
Total Liabilities and Stockholders Equity	$ 2,199,141	$ 2,133,314

* Derived from audited financial statements.

See Notes to Consolidated Financial Statements.

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FIRST COMMUNITY BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(Dollars in Thousands, Except Per Share Data)	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Interest Income		
Interest and fees on loans held for investment	$ 19,984	$ 21,237
Interest on securities-taxable	5,164	6,067
Interest on securities-nontaxable	1,676	2,063
Interest on deposits in banks	39	180
Total interest income	26,863	29,547
Interest Expense		
Interest on deposits	7,567	8,741
Interest on borrowings	2,863	4,446
Total interest expense	10,430	13,187
Net interest income	16,433	16,360
Provision for loan losses	2,087	323
Net interest income after provision for loan losses	14,346	16,037
Noninterest Income		
Wealth management income	984	899
Service charges on deposit accounts	3,157	3,099
Other service charges, commissions and fees	1,178	1,121
Insurance commissions	2,317	1,344
Total other-than-temporary impairment losses	(209)	
Portion of loss recognized in other comprehensive income		
Net impairment losses recognized in earnings	(209)	
Gain on sale of securities	411	1,820
Other operating income	586	858
Total noninterest income	8,424	9,141
Noninterest Expense		
Salaries and employee benefits	7,866	7,790
Occupancy expense of bank premises	1,603	1,164
Furniture and equipment expense	938	901
Intangible amortization	245	160
Prepayment penalty on FHLB advance		1,647
Other operating expense	4,542	4,621
Total noninterest expense	15,194	16,283
Income before income taxes	7,576	8,895

Income tax expense		2,346		2,583
Net income		5,230		6,312
Dividends on preferred stock		571		
Net income available to common shareholders	$	4,659	$	6,312
Basic earnings per common share	$	0.40	$	0.57
Diluted earnings per common share	$	0.40	$	0.57
Dividends declared per common share	$		$	0.28
Weighted average basic shares outstanding		11,567,769		11,029,931
Weighted average diluted shares outstanding		11,616,568		11,107,610

See Notes to Consolidated Financial Statements.

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FIRST COMMUNITY BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Three Months Ended March 31,	
	2009	**2008**
(In Thousands)		
Operating activities:		
Net Income	$ 5,230	$ 6,312
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	2,087	323
Depreciation and amortization of premises and equipment	1,096	889
Intangible amortization	245	160
Net investment amortization and accretion	193	(340)
Net gain on the sale of assets	(439)	(1,781)
Mortgage loans originated for sale	(8,481)	(13,280)
Proceeds from sales of mortgage loans	8,083	12,058
Gain on sales of loans	(23)	(83)
Deferred income tax benefit	(317)	(149)
Decrease in interest receivable	1,235	2,723
Other operating activities, net	1,194	3,543
Net cash provided by operating activities	10,103	10,375
Investing activities:		
Proceeds from sales of securities available-for-sale	46,394	30,797
Proceeds from maturities and calls of securities available-for-sale	10,346	37,723
Proceeds from maturities and calls of securities held-to-maturity	200	
Purchase of securities available-for-sale	(97,018)	(14,118)
Net decrease in loans held for investment	18,065	45,809
Proceeds from the redemption of FHLB stock	324	
Proceeds from sales of equipment	7	
Purchase of premises and equipment	(971)	(1,952)
Net cash provided by (used in) investing activities	(22,653)	98,259
Financing activities:		
Net increase (decrease) in demand and savings deposits	27,482	(2,662)
Net increase (decrease) in time deposits	52,204	(31,828)
Net decrease in federal funds purchased		(18,500)
Net (decrease) increase in securities sold under agreement to repurchase	(12,090)	573
Net decrease in FHLB and other borrowings	(7)	(26,674)
Proceeds from the exercise of stock options		66
Excess tax benefit from stock-based compensation		10
Acquisition of treasury stock		(2,168)
Preferred dividends paid	(518)	
Common dividends paid		(3,082)

Net cash (used in) provided by financing activities	67,071	(84,265)
Increase in cash and cash equivalents	54,521	24,369
Cash and cash equivalents at beginning of period	46,439	52,746
Cash and cash equivalents at end of period	$ 100,960	$ 77,115
Supplemental information Noncash items		
Transfer of loans to other real estate	$ 2,030	$ 282
Cumulative effect adjustment of FAS 115-2, net of tax	$ 6,131	$

See Notes to Consolidated Financial Statements.

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FIRST COMMUNITY BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (Unaudited)

(Dollars in Thousands)	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
Balance January 1, 2008	$	$ 11,499	$ 108,825	$ 117,670	$ (13,613)	$ (7,283)	$ 217,098
Cumulative effect of change in accounting principle				(813)			(813)
Comprehensive income:							
Net income				6,312			6,312
Other comprehensive loss, net of tax:							
Unrealized loss on securities available for sale						(7,280)	(7,280)
Reclassification adjustment for gains realized in net income						(534)	(534)
Unrealized loss on cash flow hedge						(950)	(950)
Comprehensive loss				6,312		(8,764)	(2,452)
Common dividends declared				(3,082)			(3,082)
Acquisition of 67,300 treasury shares					(2,168)		(2,168)
Acquisition of GreenPoint Insurance - 7,728 shares issued			22		245		267
Equity-based compensation expense			52				52
Tax benefit from exercise of stock options			10				10
Option exercises - 41,470 shares			(13)		79		66
Balance March 31, 2008	$	$ 11,499	$ 108,896	$ 120,087	$ (15,457)	$ (16,047)	$ 208,978
Balance January 1, 2009	$ 40,419	$ 12,051	$ 128,526	$ 107,231	$ (15,368)	$ (52,517)	$ 220,342
				6,131			6,131

Cumulative effect of change in accounting principle							
Comprehensive income:							
Net income				5,230			5,230
Other comprehensive loss, net of tax:							
Unrealized loss on securities available-for-sale						(13,863)	(13,863)
Reclassification adjustment for gains realized in net income						(140)	(140)
Unrealized gain on cash flow hedge						148	148
Comprehensive loss				5,230		(13,855)	(8,625)
Preferred dividend, net	52		(38)	(571)			(557)
Equity-based compensation expense			40				40
Retirement plan contribution - 28,800 shares issued			(536)		915		379
Balance March 31, 2009	$ 40,471	$ 12,051	$ 127,992	$ 118,021	$ (14,453)	$ (66,372)	$ 217,710

See Notes to Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. General

Unaudited Consolidated Financial Statements

The accompanying unaudited consolidated financial statements of First Community Bancshares, Inc. and subsidiaries (First Community or the Company) have been prepared in accordance with United States generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments, including normal recurring accruals, necessary for a fair presentation have been made. These results are not necessarily indicative of the results of consolidated operations that might be expected for the full calendar year.

The consolidated balance sheet as of December 31, 2008, has been derived from the audited consolidated financial statements included in the Company s 2008 Annual Report on Form 10-K. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) have been omitted in accordance with standards for the preparation of interim consolidated financial statements. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s 2008 Annual Report on Form 10-K.

A more complete and detailed description of First Community s significant accounting policies is included within Footnote 1 of Item 8, Financial Statements and Supplementary Data in the Company s Annual Report on Form 10-K for December 31, 2008. Further discussion of the Company s application of critical accounting policies is included within the Application of Critical Accounting Policies section of Part I, Item 2, Management s Discussion and Analysis of Financial Condition and Results of Operations, included herein.

The Company operates within two business segments, banking and insurance services. Insurance services are comprised of agencies which sell property and casualty and life and health insurance policies and arrangements. All other operations, including commercial and consumer banking, lending activities, and wealth management are included within the banking segment.

Earnings Per Share

Basic earnings per share is determined by dividing net income available to common shareholders by the weighted average number of shares outstanding. Diluted earnings per share is determined by dividing net income available to common shareholders by the weighted average shares outstanding increased by the dilutive effect of stock options, warrants and contingently issuable shares. Basic and diluted net income per common share calculations follow:

	For the three months ended March 31,	
(Amounts in Thousands, Except Share and Per Share Data)	**2009**	**2008**
Net income available to common shareholders	$ 4,659	$ 6,312
Weighted average shares outstanding	11,567,769	11,029,931
Dilutive shares for stock options	6,332	57,040
Contingently issuable shares	42,467	20,639
Common stock warrants		
Weighted average dilutive shares outstanding	11,616,568	11,107,610
Basic earnings per share	$ 0.40	$ 0.57
Diluted earnings per share	$ 0.40	$ 0.57

For the three months ended March 31, 2009, options and warrants to purchase 391,104 shares of common stock were outstanding but were not included in the computation of diluted earnings per common share because their effect would be anti-dilutive. This compares to options to purchase 10,000 shares of common stock outstanding but not included in

the computation of diluted earnings per common share because their effect would be anti-dilutive for the three months ended March 31, 2008.

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Recent Accounting Pronouncements

In April 2009, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments. The FSP requires a public entity to provide disclosures about fair value of financial instruments in interim financial information. The FSP will be effective for interim and annual financial periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. The Company adopted the provisions of FSP FAS 107-1 and APB 28-1 effective January 1, 2009.

In April 2009, the FASB issued FSP FAS 115-2, FAS 124-2 and EITF 99-20-2, Recognition and Presentation of Other-Than-Temporary-Impairment. The FSP (i) changes existing guidance for determining whether an impairment is other than temporary to debt securities and (ii) replaces the existing requirement that the entity s management assert it has both the intent and ability to hold an impaired debt security until recovery with a requirement that management assert: (a) it does not have the intent to sell the debt security; and (b) it is more likely than not that it will not have to sell the debt security before recovery of its cost basis. Under the FSP, declines in the fair value of held-to-maturity and available-for-sale debt securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of impairment related to other factors is recognized in other comprehensive income. The Company adopted the provisions of FSP FAS 115-2, FAS 124-2 and EITF 99-20-2-1 effective January 1, 2009, and made a cumulative effect credit adjustment in retained earnings of approximately $6.13 million.

In April 2009, the FASB issued FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly. The FSP affirms the objective of fair value when a market is not active, clarifies and includes additional factors for determining whether there has been a significant decrease in market activity, eliminates the presumption that all transactions are distressed unless proven otherwise, and requires an entity to disclose a change in valuation technique. The Company adopted the provisions of FSP FAS 157-4 effective January 1, 2009, which did not have a material impact on the Company s financial condition or results of operations.

In May 2008, the FASB issued Statement No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS 162). This statement establishes a framework for selecting accounting principles to be used in preparing financial statements that are presented in conformity with US GAAP. SFAS 162 is effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board Auditing amendments to AU Section 411, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles, and is not expected to have an impact on the Company s consolidated financial statements.

In March 2008, the FASB issued Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (SFAS 161). This statement requires enhanced disclosures about an entity s derivative and hedging activities in order to improve the transparency of financial reporting. Entities are required to provide enhanced disclosures 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. The Company adopted SFAS 161 effective January 1, 2009, and the enhanced disclosures are included in Note 11 Derivatives and Hedging Activities.

In December 2007, the FASB revised Statement No. 141, Business Combinations (SFAS 141R). This statement requires an acquirer to recognize the assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree at the acquisition date, measured at their fair values as of that date. This statement recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase. This statement also defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquiree achieves control. Additionally this statement determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. In connection with its January 1, 2009, adoption of SFAS 141R, the Company has expensed costs associated with recently announced transactions.

Note 2. Mergers, Acquisitions, and Branching Activity

On April 2, 2009, the Company signed a definitive agreement providing for the acquisition of TriStone Community Bank (TriStone), a $152.42 million state-chartered commercial bank headquartered in Winston-Salem, North Carolina. The definitive agreement provides for the exchange of .5262 shares of the Company s common stock for each outstanding share of TriStone common stock. TriStone will be merged with and into the Company s wholly-owned national bank subsidiary, First Community Bank, N. A. The transaction is subject to regulatory approvals and approval by the stockholders of TriStone, and is expected to close in the third quarter of 2009.

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On November 14, 2008, the Company completed the acquisition of Coddle Creek Financial Corp. (Coddle Creek), based in Mooresville, North Carolina. Coddle Creek had three full service locations in Mooresville, Cornelius, and Huntersville, North Carolina. At acquisition, Coddle Creek had total assets of approximately $158.66 million, loans of approximately $136.99 million, and deposits of approximately $137.06 million. Under the terms of the merger agreement, shares of Coddle Creek were exchanged for .9046 shares of the Company s common stock and $19.60 in cash, for a total purchase price of approximately $32.29 million. As a result of the acquisition and purchase price allocation, approximately $14.41 million in goodwill was recorded, which represents the excess purchase price over the fair market value of the net assets acquired and identified intangibles.

Since January 1, 2008, GreenPoint Insurance Group, Inc., the Company s wholly-owned insurance agency subsidiary, has acquired a total of five agencies, issuing cash consideration of approximately $2.04 million. Acquisition terms in all instances call for additional cash consideration if certain operating performance targets are met. If those targets are met, the value of the consideration ultimately paid will be added to the cost of the acquisitions. Goodwill and other intangibles associated with those acquisitions total approximately $2.04 million.

In May 2008, the Company opened a new branch location in Summersville, West Virginia.

Note 3. Investment Securities

As of March 31, 2009, and December 31, 2008, the amortized cost and estimated fair value of available-for-sale securities were as follows:

	March 31, 2009			
	Amortized Cost	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
(In Thousands)				
U.S. Government agency securities	$ 53,425	$ 702	$	$ 54,127
States and political subdivisions	141,536	2,296	(2,209)	141,623
Trust-preferred securities	148,882		(99,409)	49,473
Mortgage-backed securities	303,431	7,149	(11,989)	298,591
Equities	7,005	376	(1,531)	5,850
Total	$ 654,279	$ 10,523	$ (115,138)	$ 549,664

	December 31, 2008			
	Amortized Cost	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
U.S. Government agency securities	$ 53,425	$ 1,393	$	$ 54,818
States and political subdivisions	163,042	864	(4,487)	159,419
Trust-preferred securities	148,760		(82,707)	66,053
Mortgage-backed securities	230,488	4,649	(1,659)	233,478
Equities	7,979	357	(1,381)	6,955
Total	$ 603,694	$ 7,263	$ (90,234)	$ 520,723

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As of March 31, 2009, and December 31, 2008, the amortized cost and estimated fair value of held-to-maturity securities were as follows:

	March 31, 2009			
	Amortized Cost	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
(In Thousands)				
States and political subdivisions	$ 8,471	$ 149	$	$ 8,620
Total	$ 8,471	$ 149	$	$ 8,620

	December 31, 2008			
	Amortized Cost	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
States and political subdivisions	$ 8,670	$ 133	$ (1)	$ 8,802
Total	$ 8,670	$ 133	$ (1)	$ 8,802

The following table reflects those investments in an unrealized loss position at March 31, 2009, and December 31, 2008. The Company has the intent and ability to hold until maturity or recovery any security in a continuous unrealized loss position for 12 or more months.

	March 31, 2009					
	Less than 12 Months		**12 Months or longer**		**Total**	
Description of Securities	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
(In Thousands)						
U. S. Government agency securities	$	$	$	$	$	$
States and political subdivisions	43,135	(1,194)	11,225	(1,015)	54,360	(2,209)
Trust-preferred securities			49,473	(99,409)	49,473	(99,409)
Mortgage-backed securities	24,705	(330)	16,558	(11,659)	41,263	(11,989)
Equity securities	2,059	(1,245)	2,153	(286)	4,212	(1,531)
Total	$ 69,899	$ (2,769)	$ 79,409	$ (112,369)	$ 149,308	$ (115,138)

	December 31, 2008					
	Less than 12 Months		**12 Months or longer**		**Total**	
Description of Securities	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U. S. Government agency securities	$	$	$	$	$	$
States and political subdivisions	86,344	(2,949)	16,413	(1,539)	102,757	(4,488)
Trust-preferred securities			60,260	(82,707)	60,260	(82,707)
Mortgage-backed securities	48,440	(1,658)	43	(1)	48,483	(1,659)

Equity securities	2,167	(1,161)	2,201	(220)	4,368	(1,381)
Total	$ 136,951	$ (5,768)	$ 78,917	$ (84,467)	$ 215,868	$ (90,235)

Included in available-for-sale securities is a portfolio of trust-preferred securities with a total fair value of approximately $49.47 million as of March 31, 2009. That portfolio is comprised of single-issue securities and pooled trust-preferred securities. The single-issue securities had a total fair value of approximately $26.77 million as of March 31, 2009, compared with their adjusted cost basis of approximately $55.52 million.

At March 31, 2009, the total fair value of the pooled trust-preferred securities was approximately $22.71 million, compared with an adjusted cost basis of approximately $93.37 million. The collateral underlying these securities is comprised of 86% of bank trust-preferred securities and subordinated debt issuances of over 500 banks nationwide. The remaining collateral is from insurance companies and real estate investment trusts. During 2008 and 2009, these securities experienced credit rating

downgrades and certain of these securities are on negative watch. As of December 31, 2008, the Company recorded pre-tax other-than-temporary impairment charges of $15.46 million on one of its pooled trust preferred securities which demonstrated a probable adverse change in cash flow. Recent modeling of the expected cash flows from the pooled trust-preferred securities, at present, does not suggest any of the remaining securities will incur credit losses under any of the scenarios modeled due to the existence of other subordinate classes within the pools and on current projections for deferrals and defaults of underlying collateral.

The Company made a cumulative effect adjustment of $6.13 million, $10.22 million pre-tax, as of January 1, 2009, to recognize the portion of non-credit losses associated with a non-agency mortgage-backed security for which the Company recognized a pre-tax other-than-temporary impairment charge of $14.47 million as of December 31, 2008. The Company determined that only $4.25 million of the original impairment charge was due to probable credit losses. The amount due to probable credit losses was determined using customized default and prepayment scenarios.

At March 31, 2009, the combined depreciation in value of the 193 individual securities in an unrealized loss position was approximately 26.36% of the combined reported value of the aggregate securities portfolio. At December 31, 2008, the combined depreciation in value of the 310 individual securities in an unrealized loss position was approximately 17.04% of the combined reported value of the aggregate securities portfolio. Management does not believe any individual unrealized loss as of March 31, 2009, represents other-than-temporary impairment. The Company intends to hold these securities until recovery or maturity and it is more likely than not that it will not sell these securities before recovery. For the quarter ended March 31, 2009, the Company recognized impairment of $209 thousand on certain of its equity securities holdings.

The amortized cost and estimated fair value of available-for-sale securities by contractual maturity, at March 31, 2009, are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	**Fair Value**
	(Dollars in Thousands)	
Due within one year	$ 1,378	$ 1,399
Due after one year but within five years	5,222	5,330
Due after five years within ten years	75,311	76,792
Due after ten years	261,932	161,702
	343,843	245,223
Mortgage-backed securities	303,431	298,591
Equity securities	7,005	5,850
Total	$ 654,279	$ 549,664

The amortized cost and estimated fair value of held-to-maturity securities by contractual maturity, at March 31, 2009, are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	**Fair Value**
	(Dollars in Thousands)	
Due within one year	$ 551	$ 556
Due after one year but within five years	4,116	4,197
Due after five years within ten years	3,804	3,867
Due after ten years		

Total	$ 8,471	$ 8,620

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Note 4. Loans

Loans, net of unearned income, consist of the following:

	March 31, 2009		December 31, 2008	
(Dollars in Thousands)	**Amount**	**Percent**	**Amount**	**Percent**
Loans held for investment:				
Commercial, financial, and agricultural	$ 81,880	6.41%	$ 85,034	6.55%
Real estate commercial	405,549	31.76%	407,638	31.40%
Real estate construction	124,320	9.74%	130,610	10.06%
Real estate residential	597,372	46.79%	602,573	46.42%
Consumer	62,353	4.88%	66,258	5.10%
Other	5,316	0.42%	6,046	0.47%
Total	$ 1,276,790	100.00%	$ 1,298,159	100.00%
Loans held for sale	$ 1,445		$ 1,024	

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and financial guarantees. These instruments involve, to varying degrees, elements of credit and interest rate risk beyond the amount recognized on the balance sheet. The contractual amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments. The Company s exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit and financial guarantees written is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is not a violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer s creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management s credit evaluation of the counterparties. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit and written financial guarantees are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. To the extent deemed necessary, collateral of varying types and amounts is held to secure customer performance under certain of those letters of credit outstanding.

Financial instruments whose contract amounts represent credit risk are commitments to extend credit (including availability of lines of credit) of $157.81 million and standby letters of credit and financial guarantees written of $2.49 million at March 31, 2009. Additionally, the Company had gross notional amount of outstanding commitments to lend related to secondary market mortgage loans of $11.28 million at March 31, 2009.

Note 5. Allowance for Loan Losses

The allowance for loan losses is maintained at a level sufficient to absorb probable loan losses inherent in the loan portfolio. The allowance is increased by charges to earnings in the form of provision for loan losses and recoveries of prior loan charge-offs, and decreased by loans charged off. The provision is calculated to bring the allowance to a level which, according to a systematic process of measurement, reflects the amount management estimates is needed

to absorb probable losses within the portfolio.

Management performs periodic assessments to determine the appropriate level of allowance. Differences between actual loan loss experience and estimates are reflected through adjustments that are made by either increasing or decreasing the loss provision based upon current measurement criteria. Commercial, consumer and mortgage loan portfolios are evaluated separately for purposes of determining the allowance. The specific components of the allowance include allocations to individual commercial credits and allocations to the remaining non-homogeneous and homogeneous pools of loans.

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Management s allocations are based on judgment of qualitative and quantitative factors about both macro and micro economic conditions reflected within the portfolio of loans and the economy as a whole. Factors considered in this evaluation include, but are not necessarily limited to, probable losses from loan and other credit arrangements, general economic conditions, changes in credit concentrations or pledged collateral, historical loan loss experience, and trends in portfolio volume, maturities, composition, delinquencies, and non-accruals. While management has allocated the allowance for loan losses to various portfolio segments, the entire allowance is available for use against any type of loan loss deemed appropriate by management.

The following table details the Company s allowance for loan loss activity for the three-month periods ended March 31, 2009 and 2008.

	For the Three Months Ended March 31,	
	2009	**2008**
(In Thousands)		
Beginning balance	$ 15,978	$ 12,833
Provision for loan losses	2,087	323
Charge-offs	(1,730)	(966)
Recoveries	220	672
Ending balance	$ 16,555	$ 12,862

Note 6. Deposits

The following is a summary of interest-bearing deposits by type as of March 31, 2009, and December 31, 2008.

(In Thousands)	**March 31, 2009**	**December 31, 2008**
Interest-bearing demand deposits	$ 194,934	$ 185,117
Savings and money market deposits	319,007	309,577
Certificates of deposit	861,556	809,352
Total	$ 1,375,497	$ 1,304,046

Note 7. Borrowings

The following schedule details the Company s Federal Home Loan Bank (FHLB) borrowings and other indebtedness at March 31, 2009, and December 31, 2008.

	March 31, 2009	December 31, 2008
(In Thousands)		
FHLB borrowings	$ 200,000	$ 200,000
Subordinated debt	15,464	15,464
Other long-term debt	406	413
Total	$ 215,870	$ 215,877

FHLB borrowings include $200.00 million in convertible and callable advances at March 31, 2009. The weighted average interest rate of advances was 2.95% and 3.70% at March 31, 2009, and December 31, 2008, respectively. The Company has entered into a derivative interest rate swap instrument where it receives LIBOR-based variable interest payments and pays fixed interest payments. The notional amount of the derivative swap is $50.00 million and effectively fixes a portion of the FHLB borrowings at approximately 4.34%. After considering the effect of the interest rate swap, the effective weighted average interest rate of all FHLB borrowings was 3.79% at March 31, 2009. The fair value of the interest rate swap was a liability of $3.08 million at March 31, 2009.

At March 31, 2009, the FHLB advances have approximate contractual maturities between eight and twelve years. The scheduled maturities of the advances are as follows:

	Amount
(In Thousands)	
2009	$
2010	
2011	
2012	
2013	
2014 and thereafter	200,000
Total	$ 200,000

The callable advances may be redeemed at quarterly intervals after various lockout periods. These call options may substantially shorten the lives of these instruments. If these advances are called, the debt may be paid in full, converted to another FHLB credit product, or converted to a fixed or adjustable rate advance. Prepayment of the advances may result in substantial penalties based upon the differential between contractual note rates and current advance rates for similar maturities. Advances from the FHLB are secured by stock in the FHLB of Atlanta, qualifying loans, mortgage-backed securities, and certain other securities.

Also included in other indebtedness is $15.46 million of junior subordinated debentures (the Debentures) issued by the Company in October 2003 to an unconsolidated trust subsidiary, FCBI Capital Trust (the Trust), with an interest rate of three-month LIBOR plus 2.95%. The Trust was able to purchase the Debentures through the issuance of trust preferred securities which had substantially identical terms as the Debentures. The Debentures mature on October 8, 2033, and are currently callable.

The Company has committed to irrevocably and unconditionally guarantee the following payments or distributions with respect to the preferred securities to the holders thereof to the extent that the Trust has not made such payments or distributions: (i) accrued and unpaid distributions, (ii) the redemption price, and (iii) upon a dissolution or

termination of the trust, the lesser of the liquidation amount and all accrued and unpaid distributions and the amount of assets of the trust remaining available for distribution, in each case to the extent the Trust has funds available.

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Note 8. Commitments and Contingencies

In the normal course of business, the Company is a defendant in various legal actions and asserted claims. While the Company and its legal counsel are unable to assess the ultimate outcome of each of these matters with certainty, the resolution of these actions, singly or in the aggregate, should not have a material adverse effect on the financial condition, results of operations or cash flows of the Company.

Note 9. Segment Information

The Company operates in two segments: Community Banking and Insurance Services. The Community Banking segment includes both commercial and consumer lending and deposit services. This segment provides customers with such products as commercial loans, real estate loans, business financing and consumer loans. This segment also provides customers with several choices of deposit products including demand deposit accounts, savings accounts and certificates of deposit. In addition, the Community Banking segment provides wealth management services to a broad range of customers. The Insurance Services segment is a full-service insurance agency providing commercial and personal lines of insurance.

The following table sets forth information about the reportable operating segments and reconciliation of this information to the consolidated financial statements at and for the three periods ended March 31, 2009.

(In Thousands)	For the Three Months Ended March 31, 2009			
	Community Banking	**Insurance Services**	**Parent/ Elimination**	**Total**
Net interest income	$ 16,492	$ (18)	$ (41)	$ 16,433
Provision for loan losses	2,087			2,087
Noninterest income	6,124	2,344	(44)	8,424
Noninterest expense	13,582	1,638	(26)	15,194
Income before income taxes	6,947	688	(59)	7,576
Provision for income taxes	1,932	203	211	2,346
Net income	$ 5,015	$ 485	$ (270)	$ 5,230
End of period goodwill and other intangibles	$ 78,657	$ 10,681	$	89,338
End of period assets	$ 2,170,694	$ 11,698	$ 16,749	2,199,141

(In Thousands)	For the Three Months Ended March 31, 2008			
	Community Banking	**Insurance Services**	**Parent/ Elimination**	**Total**
Net interest income	$ 16,635	$ (6)	$ (269)	$ 16,360
Provision for loan losses	323			323
Noninterest income	7,994	1,344	(197)	9,141
Noninterest expense	15,792	1,046	(555)	16,283
Income before income taxes	8,514	292	89	8,895
Provision for income taxes	2,432	86	65	2,583
Net income	$ 6,082	$ 206	$ 24	$ 6,312

End of period goodwill and other intangibles	$	62,352	$	8,887	$		71,239
End of period assets	$	2,045,941	$	8,900	$	10,272	2,065,113

Note 10. Fair Value Disclosures

Effective January 1, 2008, the Company adopted the provisions of SFAS No. 157, Fair Value Measurements, (SFAS 157) for financial assets and financial liabilities. In accordance with FASB Staff Position No. 157-2, Effective Date of FASB Statement No. 157, the Company delayed application of SFAS 157 for non-financial assets and non-financial liabilities until January 1, 2009. SFAS 157, as amended, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements.

SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal, or most advantageous, market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact, and (iv) willing to transact.

SFAS 157 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1 Inputs	Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
Level 2 Inputs	Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, such as interest rates, volatilities, prepayment speeds, and credit risks, or inputs that are derived principally from or corroborated by market data by correlation or other means.
Level 3 Inputs	Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity s own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of the Company s financial assets and financial liabilities carried at fair value. In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon third party models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality, the Company s creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company s valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company s valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Securities Available-for-Sale: Securities classified as available-for-sale are reported at fair value utilizing Level 1, Level 2, and Level 3 inputs. Securities are classified as Level 1 within the valuation hierarchy when quoted prices are available in an active market. This includes securities, such as U.S. Treasuries, whose value is based on quoted market prices in active markets for identical assets.

Securities are classified as Level 2 within the valuation hierarchy when the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond s terms and conditions, among other things.

Securities are classified as Level 3 within the valuation hierarchy in certain cases when there is limited activity or less transparency to the valuation inputs. These securities include certain pooled trust preferred securities. In the absence

of observable or corroborated market data, internally developed estimates that incorporate market-based assumptions are used when such information is available.

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Fair value models may be required when trading activity has declined significantly or does not exist, prices are not current or pricing variations are significant. The Company s fair value from third party models utilize modeling software that uses market participant data and knowledge of the structures of each individual security to develop cash flows specific to each security. The fair values of the securities are determined by using the cash flows developed by the fair value model and applying appropriate market observable discount rates. The discount rates are developed by determining credit spreads above a benchmark rate, such as LIBOR, and adding premiums for illiquidity developed based on a comparison of initial issuance spread to LIBOR versus a financial sector curve for recently issued debt to LIBOR. Specific securities that have increased uncertainty regarding the receipt of cash flows are discounted at higher rates due to the addition of a deal specific credit premium. Finally, internal fair value model pricing and external pricing observations are combined by assigning weights to each pricing observation. Pricing is reviewed for reasonableness based on the direction of the specific markets and the general economic indicators.

Other Assets and Associated Liabilities: Securities held for trading purposes are recorded at fair value and included in other assets on the consolidated balance sheets. Securities held for trading purposes include assets related to employee deferred compensation plans. The assets associated with these plans are generally invested in equities and classified as Level 1. Deferred compensation liabilities, also classified as Level 1, are carried at the fair value of the obligation to the employee, which corresponds to the fair value of the invested assets.

Derivatives: Derivatives are reported at fair value utilizing Level 2 inputs. The Company obtains dealer quotations based on observable data to value its derivatives.

Impaired Loans: Certain impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 3 inputs based on customized discounting criteria.

Other Real Estate Owned. The fair value of the Company s other real estate owned is determined using current and prior appraisals, estimates of costs to sell, and proprietary adjustments. Accordingly, other real estate owned is stated at a Level 3 fair value.

The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis as of March 31, 2009, and December 31, 2008, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

(In Thousands)	**March 31, 2009**			
	Fair Value Measurements Using			**Total**
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Available-for-sale securities	$5,706	$521,253	$22,705	$549,664
Other assets	2,269			2,269
Derivative assets		57		57
Other liabilities	2,269			2,269
Derivative liabilities		3,085		3,085

(In Thousands)	**December 31, 2008**			
	Fair Value Measurements Using			**Total**
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Available-for-sale securities	$6,811	$485,845	$28,067	$520,723
Other assets	2,637			2,637
Derivative assets		39		39
Other liabilities	2,637			2,637
Derivative liabilities		3,343		3,343

The following table shows a reconciliation of the beginning and ending balances for fair valued assets measured on a recurring basis using significant unobservable inputs. There were no financial assets or liabilities stated at Level 3 at March 31, 2008.

(In Thousands)	**Available-for-Sale Securities**
Beginning balance January 1, 2009	$ 28,067
Total gains or loss (realized/unrealized)	
Included in earnings	
Included in other comprehensive income	(7,508)
Paydowns and maturities	(33)
Transfers into Level 3	2,179
Ending balance March 31, 2009	$ 22,705

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances, for example, when there is evidence of impairment. Items subjected to nonrecurring fair value adjustments at March 31, 2009, and December 31, 2008, are as follows:

(In Thousands)	**March 31, 2009**			
	Fair Value Measurements Using			**Total**
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Impaired loans	$	$	$4,923	$4,923
Other real estate owned			3,114	3,114

(In Thousands)	**December 31. 2008**			
	Fair Value Measurements Using			**Total**
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Impaired loans	$	$	$5,980	$5,980

Certain non-financial assets and non-financial liabilities measured at fair value on a recurring basis include reporting units measured at fair value in the first step of a goodwill impairment test. Certain non-financial assets measured at fair value on a non-recurring basis include non-financial assets and non-financial liabilities measured at fair value in the second step of a goodwill impairment test, as well as intangible assets and other non-financial long-lived assets measured at fair value for impairment assessment.

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Fair Value of Financial Instruments

Fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practical to estimate the value is based upon the characteristics of the instruments and relevant market information. Financial instruments include cash, evidence of ownership in an entity, or contracts that convey or impose on an entity that contractual right or obligation to either receive or deliver cash for another financial instrument. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price if one exists.

	March 31, 2009		December 31, 2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(Amounts in Thousands)			
Assets				
Cash and cash equivalents	$ 100,960	$ 100,960	$ 46,439	$ 46,439
Investment Securities	558,135	558,284	529,393	529,525
Loans held for sale	1,445	1,458	1,024	1,026
Loans held for investment	1,260,235	1,255,995	1,282,181	1,276,479
Derivative financial assets	57	57	39	39
Deferred compensation assets	2,269	2,269	2,637	2,637
Liabilities				
Demand deposits	207,947	207,947	199,712	199,712
Interest-bearing demand deposits	194,934	194,934	185,117	185,117
Savings deposits	319,007	319,007	309,577	309,577
Time deposits	861,556	876,545	809,352	824,068
Securities sold under agreements to repurchase	153,824	165,340	165,914	177,454
FHLB and other indebtedness	215,870	236,836	215,877	242,223
Derivative financial liabilities	3,085	3,085	3,343	3,343
Deferred compensation liabilities	2,269	2,269	2,637	2,637

The following summary presents the methodologies and assumptions used to estimate the fair value of the Company s financial instruments presented below. The information used to determine fair value is highly subjective and judgmental in nature and, therefore, the results may not be precise. Subjective factors include, among other things, estimates of cash flows, risk characteristics, credit quality, and interest rates, all of which are subject to change. Since the fair value is estimated as of the balance sheet date, the amounts that will actually be realized or paid upon settlement or maturity on these various instruments could be significantly different.

Financial Instruments with Book Value Equal to Fair Value: The book values of cash and due from banks and federal funds sold and purchased are considered to be equal to fair value as a result of the short-term nature of these items.

Investment Securities and Deferred Compensation Assets and Liabilities: Fair values are determined in the same manner as described above.

Loans: The estimated fair value of loans held for investment is measured based upon discounted future cash flows using current rates for similar loans, applying a discount for illiquidity. Loans held for sale are recorded at lower of cost or estimated fair value. The fair value of loans held for sale is determined based upon the market sales price of similar loans.

Derivative Financial Instruments: The estimated fair value of derivative financial instruments is based upon the current market price for similar instruments.

Deposits and Securities Sold Under Agreements to Repurchase: Deposits without a stated maturity, including demand, interest-bearing demand, and savings accounts, are reported at their carrying value in accordance with SFAS 107. No value has been assigned to the franchise value of these deposits. For other types of deposits and repurchase

agreements with fixed maturities and rates, fair value has been estimated by discounting future cash flows based on interest rates currently being offered on instruments with similar characteristics and maturities.

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Other Indebtedness: Fair value has been estimated based on interest rates currently available to the Company for borrowings with similar characteristics and maturities.

Commitments to Extend Credit, Standby Letters of Credit, and Financial Guarantees: The amount of off-balance sheet commitments to extend credit, standby letters of credit, and financial guarantees is considered equal to fair value. Because of the uncertainty involved in attempting to assess the likelihood and timing of commitments being drawn upon, coupled with the lack of an established market and the wide diversity of fee structures, the Company does not believe it is meaningful to provide an estimate of fair value that differs from the given value of the commitment.

Note 11. Derivatives and Hedging Activities

The Company, through its mortgage banking and risk management operations, is party to various derivative instruments that are used for asset and liability management and customers financing needs. Derivative assets and liabilities are recorded at fair value on the balance sheet.

The primary derivatives that the Company uses are interest rate swaps and interest rate lock commitments (IRLCs). Generally, these instruments help the Company manage exposure to market risk and meet customer financing needs. Market risk represents the possibility that economic value or net interest income will be adversely affected by fluctuations in external factors, such as interest rates, market-driven loan rates and prices or other economic factors.

The following table presents the aggregate contractual, or notional, amounts of derivative financial instruments as of the dates indicated:

(In Thousands)	**March 31, 2009**	**December 31, 2008**	**March 31, 2008**
Interest rate swap	$ 50,000	$ 50,000	$ 50,000
IRLC s	11,300	10,500	13,200

As of March 31, 2009, December 31, 2008 and March 31, 2008, the fair values of the Company s derivatives were as follows:

	Asset Derivatives					
	March 31, 2009		**December 31, 2008**		**March 31, 2008**	
(In Thousands)	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Derivatives designated as hedges						
Interest rate swap	Other assets	$	Other assets	$	Other assets	$
Total		$		$		$
Derivatives not designated as hedges						
IRLC s	Other assets	$ 57	Other assets	$ 39	Other assets	$ 52
Total		$ 57		$ 39		$ 52
Total derivatives		$ 57		$ 39		$ 52

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	Liability Derivatives					
	March 31, 2009		December 31, 2008		March 31, 2008	
(In Thousands)	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Derivatives designated as hedges						
Interest rate swap	Other liabilities	$ 3,081	Other liabilities	$ 3,327	Other liabilities	$ 2,903
Total		$ 3,081		$ 3,327		$ 2,903
Derivatives not designated as hedges						
IRLC s	Other liabilities	$ 4	Other liabilities	$ 16	Other liabilities	$ 14
Total		$ 4		$ 16		$ 14
Total derivatives		$ 3,085		$ 3,343		$ 2,917

Interest Rate Swaps. The Company uses interest rate swap contracts to modify its exposure to interest rate risk. The Company currently employs a cash flow hedging strategy to effectively convert certain floating-rate liabilities into fixed-rate instruments. The interest rate swap is accounted for under the short-cut method in SFAS 133. Changes in fair value of the interest rate swap are reported as a component of other comprehensive income. The Company does not currently employ fair value hedging strategies.

Interest Rate Lock Commitments. In the normal course of business, the Company sells originated mortgage loans into the secondary mortgage loan market. During the period of loan origination and prior to the sale of the loans in the secondary market, the Company has exposure to movements in interest rates associated with mortgage loans that are in the mortgage pipeline. A pipeline loan is one on which the potential borrower has set the interest rate for the loan by entering into an interest rate lock commitment (IRLC). Once a mortgage loan is closed and funded, it is included within loans held for sale and awaits sale and delivery into the secondary market. During the term of an IRLC, the Company has the risk that interest rates will change from the rate quoted to the borrower.

The Company s balance of mortgage loans held for sale is subject to changes in fair value, due to fluctuations in interest rates from the loan closing date through the date of sale of the loan into the secondary market. Typically, the fair value of the warehouse declines in value when interest rates increase and rises in value when interest rates decrease.

Effect of Derivatives and Hedging Activities on the Income Statement

For the quarters ended March 31, 2009 and 2008, the Company has determined there was no amount of ineffectiveness on cash flow hedges. The following table details gains and losses recognized in income on non-designated hedging instruments under SFAS 133 for the quarters ended March 31, 2009 and 2008.

Derivatives not designated as hedging instruments under	Location of Gain/(Loss)	Amount of Gain/(Loss) Recognized in Income on Derivative

SFAS 133	Recognized in Income on Derivative		Quarter ended March 31, 2009		Quarter ended March 31, 2008
		(Amounts in Thousands)			
IRLC s	Other income	$	30	$	30
Total		$	30	$	30

Counterparty Credit Risk. Like other financial instruments, derivatives contain an element of credit risk. Credit risk is the possibility that the Company will incur a loss because a counterparty, which may be a bank, a broker-dealer or a customer, fails to meet its contractual obligations. This risk is measured as the expected positive replacement value of contracts. All derivative contracts may be executed only with exchanges or counterparties approved by the Company s Asset and Liability Management Committee. The Company reviews its counterparty risk regularly and has determined that, as of March 31, 2009, there is no significant counterparty credit risk.

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PART I. ITEM 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis is provided to address information about the Company financial condition and results of operations. This discussion and analysis should be read in conjunction with the Company s 2008 Annual Report on Form 10-K and the other financial information included in this report.

The Company is a multi-state financial holding company headquartered in Bluefield, Virginia, with total assets of $2.20 billion at March 31, 2009. Through its community bank subsidiary, First Community Bank, N. A. (the Bank), the Company provides financial, trust and investment advisory services to individuals and commercial customers through more than fifty locations in Virginia, West Virginia, North Carolina, South Carolina, and Tennessee. The Company is also the parent of GreenPoint Insurance Group, Inc., a North Carolina-based full-service insurance agency offering commercial and personal lines (GreenPoint). The Bank is the parent of Investment Planning Consultants, Inc. (IPC), a registered investment advisory firm that offers wealth management and investment advice. The Company s common stock is traded on the NASDAQ Global Select Market under the symbol, FCBC .

FORWARD-LOOKING STATEMENTS

The Company may from time to time make written or oral forward-looking statements , including statements contained in its filings with the SEC (including this Quarterly Report on Form 10-Q and the Exhibits hereto and thereto), in its reports to stockholders and in other communications which are made in good faith by the Company pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include, among others, statements with respect to the Company s beliefs, plans, objectives, goals, guidelines, expectations, anticipations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors (many of which are beyond the Company s control). The words may, could, should, would, believe, anticipate, estimate, expect, intend, plan, expressions are intended to identify forward-looking statements. The following factors, among others, could cause the Company s financial performance to differ materially from that expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System; inflation, interest rate, market and monetary fluctuations; the timely development of competitive new products and services of the Company and the acceptance of these products and services by new and existing customers; the willingness of customers to substitute competitors products and services for the Company s products and services and vice versa; the impact of changes in financial services laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes; the effect of acquisitions, including, without limitation, the failure to achieve the expected revenue growth and/or expense savings from such acquisitions; the growth and profitability of the Company s non-interest or fee income being less than expected; unanticipated regulatory or judicial proceedings; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company. These factors are described in greater detail in Item 1A. Risk Factors, in the Company s 2008 Annual Report on Form 10-K.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Company s consolidated financial statements are prepared in accordance with GAAP and conform to general practices within the banking industry. The Company s financial position and results of operations are affected by management s application of accounting policies, including judgments made to arrive at the carrying value of assets and liabilities and amounts reported for revenues, expenses and related disclosures. Different assumptions in the application of these policies could result in material changes in the Company s consolidated financial position and consolidated results of operations.

Estimates, assumptions, and judgments are necessary principally when assets and liabilities are required to be recorded at estimated fair value, when a decline in the value of an asset carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded based upon the probability of occurrence of a future event. Carrying assets and liabilities at fair value

inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by third party sources, when available. When third party information is not available, valuation adjustments are estimated by management primarily through the use of internal modeling techniques and appraisal estimates.

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The Company s accounting policies are fundamental to understanding Management s Discussion and Analysis of Financial Condition and Results of Operation. The disclosures presented in the Notes to the Consolidated Financial Statements and in Management s Discussion and Analysis provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has identified the accounting for and valuation of investment securities, the determination of the allowance for loan losses, accounting for acquisitions and intangible assets, and accounting for income taxes as the four accounting areas that require the most subjective or complex judgments. The identified critical accounting policies are described in detail in the Company s 2008 Annual Report on Form 10-K.

COMPANY OVERVIEW

The Company is a financial holding company which operates within the five-state region of Virginia, West Virginia, North Carolina, South Carolina, and Tennessee. The Company operates through the Bank, Investment Planning Consultants, and GreenPoint to offer a wide range of financial services. The Company reported total assets of $2.20 billion at March 31, 2009.

The Company funds its lending activities primarily through the retail deposit operations of its branch banking network. Retail and wholesale repurchase agreements and borrowings from the Federal Home Loan Bank (FHLB) provide additional funding as needed. The Company invests its funds primarily in loans to retail and commercial customers. In addition to loans, the Company invests a portion of its funds in various debt securities, including those of United States agencies, state and political subdivisions, and certain corporate notes and debt instruments. The Company also maintains overnight interest-bearing balances with the FHLB and correspondent banks. The difference between interest earned on assets and interest paid on liabilities is the Company s primary source of earnings. Net interest income is supplemented by fees for services, commissions on sales, and various deposit service charges.

The Company also conducts asset management activities through the Bank s Trust and Financial Services Division (Trust Division) and its registered investment advisory firm, IPC. The Bank s Trust Division and IPC manage assets with an aggregate market value of $791 million. These assets are not assets of the Company, but are managed under various fee-based arrangements as fiduciary or agent.

RECENT MARKET DEVELOPMENTS

The global and U.S. economies continue to experience significantly reduced business activity as a result of recessionary economic conditions and disruptions in the financial system during the past eighteen months. Dramatic declines in the housing market during the past eighteen months, with falling home prices and increasing foreclosures and unemployment, have resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities and major commercial and investment banks. These write-downs, initially of mortgage-backed securities but spreading to credit default swaps, other derivative securities, and to loan portfolios, have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. Further adverse effects could have an adverse impact on the Company and its business.

MERGERS, ACQUISITIONS AND BRANCHING ACTIVITY

On April 2, 2009, the Company signed a definitive agreement providing for the acquisition of TriStone Community Bank (TriStone) a $152.42 million state-chartered commercial bank headquartered in Winston-Salem, North Carolina. The definitive agreement provides for the exchange of .5262 shares of the Company s common stock for each outstanding share of TriStone common stock. TriStone will be merged with and into the Bank. The transaction is subject to regulatory approvals and approval by the stockholders of TriStone, and is expected to close in the third quarter of 2009.

On November 14, 2008, the Company completed the acquisition of Coddle Creek Financial Corp. (Coddle Creek), based in Mooresville, North Carolina. Coddle Creek had three full service locations in Mooresville, Cornelius, and Huntersville, North Carolina. At acquisition, Coddle Creek had total assets of approximately $158.66 million, loans of approximately $136.99 million, and deposits of approximately $137.06 million. Under the terms of the merger agreement, shares of Coddle Creek were exchanged for .9046 shares of the Company s common stock and $19.60 in cash, for a total purchase price of approximately $32.29 million. As a result of the acquisition and purchase price allocation, approximately $14.41 million in goodwill was recorded, which represents the excess purchase price over

the fair market value of the net assets acquired and identified intangibles.

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Since January 1, 2008, GreenPoint has acquired a total of five agencies, issuing cash consideration of approximately $2.04 million. Acquisition terms in all instances call for additional cash consideration if certain operating performance targets are met. If those targets are met, the value of the consideration ultimately paid will be added to the cost of the acquisitions. Goodwill and other intangibles associated with GreenPoint s acquisitions total approximately $2.04 million.

The Company opened a new branch location in Summersville, West Virginia, in May 2008.

RESULTS OF OPERATIONS

Overview

Net income available to common shareholders for the three months ended March 31, 2009, was $4.66 million, or $0.40 per basic and diluted share, compared with $6.31 million, or $0.57 per basic and diluted share, for the three months ended March 31, 2008, a decrease of $1.65 million, or 26.19%. Return on average assets was 0.87% for the three months ended March 31, 2009, compared with 1.21% for the same period in 2008. Return on average common equity for the three months ended March 31, 2009, was 10.61% compared with 11.66% for the three months ended March 31, 2008. The main reason for the decrease in net income was increased provisions for loan losses.

Net Interest Income (See Table I)

Net interest income, the largest contributor to earnings, was $16.43 million for the three months ended March 31, 2009, compared with $16.36 million for the corresponding period in 2008, an increase of $73 thousand, or 0.45%. Tax-equivalent net interest income totaled $17.35 million for the three months ended March 31, 2009, a decrease of $142 thousand from $17.49 million for the first quarter of 2008. The decrease in tax-equivalent net interest income was due primarily to decreases in loan and investment yields as a result of the precipitous declines in benchmark interest rates, including the New York Prime Rate, since late 2007.

Compared with the first quarter of 2008, average earning assets increased $24.15 million while interest-bearing liabilities increased $93.30 million during the three months ended March 31, 2009. The changes include the impact of the Coddle Creek acquisition in November 2008. The yield on average earning assets decreased by 65 basis points to 5.97% from 6.62% between the three months ended March 31, 2009 and 2008, respectively. Total cost of interest-bearing liabilities decreased 79 basis points between the first quarters of 2008 and 2009, which resulted in a net interest rate spread that was 14 basis points higher at 3.53% for the first quarter of 2008 compared with 3.39% for the same period last year. The Company s tax-equivalent net interest margin of 3.73% for the three months ended March 31, 2009, decreased five basis points from 3.78% for the same period of 2008.

The rate earned on loans decreased 81 basis points to 6.28% from 7.09% for the three months ended March 31, 2009 and 2008, respectively. The effect of the cuts in the target federal funds rate by the Federal Open Market Committee and the associated decline in the Prime rate had a profound impact on loan yields throughout 2008 and 2009, resulting in a net decrease of $1.26 million, or 5.93%, in tax-equivalent loan interest income for the first quarter of 2009 compared with the first quarter of 2008.

During the three months ended March 31, 2009, the tax-equivalent yield on available-for-sale securities increased 17 basis points to 5.98%, while the average balance decreased by $109.98 million, or 17.64%, compared with the same period in 2008. The decline in average balance was due to declines in the fair value of available-for-sale securities. The average balance of the held-to-maturity securities portfolio continued to decline as securities matured or were called and were not replaced.

Compared with the first quarter of 2008, average interest-bearing balances with banks increased to $73.63 million during the first quarter of 2008, as the yield decreased 299 basis points to 0.21% during the same period. Interest-bearing balances with banks is comprised largely of excess liquidity bearing overnight market rates. The rate earned on these overnight balances during the first quarter of 2008 decreased along with decreases in short-term benchmark interest rates. The Company maintained a strong liquidity position in the first quarter to balance the risks associated with the fed funds market and general economic conditions.

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Compared with the same period in 2008, the average balances of interest-bearing demand deposits increased $28.04 million, or 17.29%, while the average rate paid during the first quarter of 2009 decreased by two basis points. During the three months ended March 31, 2009, the average balances of savings deposits decreased $14.50 million, or 4.43%, while the average rate paid decreased 98 basis points compared to the same period in 2008. Average time deposits increased $185.38 million, or 27.56%, while the average rate paid on time deposits decreased 106 basis points from 4.29% in the first quarter of 2008 to 3.23% in the first quarter of 2009. The level of average non-interest-bearing demand deposits decreased $13.66 million, or 6.41%, to $199.31 million during the quarter ended March 31, 2009, compared with the corresponding period of the prior year. The overall increase in the level of average deposits reflects the addition of Coddle Creek. Movements within the deposit types reflect customers seeking yield enhancement within FDIC insured products.

Retail repurchase agreements, which consist of collateralized retail deposits and commercial treasury accounts, decreased $43.11 million, or 28.82%, to $106.47 million for the first quarter of 2009, while the rate decreased 126 basis points to 1.49% during the same period. The decrease in average balance can be largely attributed to the customers converting retail repurchase agreements to certificates of deposit. There were no fed funds purchased on average during the first quarter of 2009, compared with $1.82 million in the same period in 2008. Wholesale repurchase agreements remained unchanged at $50.00 million, while the rate increased 34 basis points between the two periods. The average balance of FHLB borrowings and other long-term debt decreased by $60.69 million, or 21.95%, in the first quarter of 2009 to $215.81 million, while the rate paid on those borrowings decreased 58 basis points.

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Table I

AVERAGE BALANCE SHEETS AND NET INTEREST INCOME ANALYSIS

	Three Months Ended March 31, 2009			Three Months Ended March 31, 2008		
	Average Balance	Interest (1)	Yield/ Rate (1)	Average Balance	Interest (1)	Yield/ Rate (1)
	(Dollars in Thousands)					
ASSETS						
Earning Assets						
Loans (2)	$ 1,292,179	$ 19,997	6.28%	$ 1,205,481	$ 21,258	7.09%
Securities available for sale	513,300	7,571	5.98%	623,275	8,998	5.81%
Securities held to maturity	8,473	172	8.23%	12,075	242	8.06%
Interest-bearing deposits	73,628	39	0.21%	22,602	180	3.20%
Total Earning Assets	1,887,580	27,779	5.97%	1,863,433	30,678	6.62%
Other assets	290,182			227,964		
TOTAL ASSETS	$ 2,177,762			$ 2,091,397		
LIABILITIES						
Interest-bearing deposits:						
Demand deposits	$ 190,215	$ 79	0.17%	$ 162,175	$ 76	0.19%
Savings deposits	312,563	656	0.85%	327,061	1,487	1.83%
Time deposits	858,020	6,832	3.23%	672,645	7,178	4.29%
Total interest-bearing deposits	1,360,798	7,567	2.26%	1,161,881	8,741	3.03%
Borrowings:						
Federal funds purchased				1,819	18	3.98%
Retail repurchase agreements	106,469	390	1.49%	149,581	1,022	2.75%
Wholesale repurchase agreements	50,000	510	4.14%	50,000	473	3.80%
FHLB borrowings and other indebtedness	215,813	1,963	3.69%	276,503	2,933	4.27%
Total borrowings	372,282	2,863	3.12%	477,903	4,446	3.74%
Total interest-bearing liabilities	1,733,080	10,430	2.44%	1,639,784	13,187	3.23%
Non-interestbearing demand deposits	199,311			212,972		
Other liabilities	25,718			20,962		
Stockholders Equity	219,653			217,679		
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 2,177,762			$ 2,091,397		
Net Interest Income, Tax Equivalent		$ 17,349			$ 17,491	
Net Interest Rate Spread (3)			3.53%			3.39%

Net Interest Margin (4)	3.73%	3.78%

(1) Fully Taxable Equivalent (FTE) at the rate of 35%. The FTE basis adjusts for the tax benefits of income on certain tax-exempt loans and investments using the federal statutory rate of 35% for each period presented. The Company believes this measure to be the preferred industry measurement of net interest income and provides relevant comparison between taxable and non-taxable amounts.

(2) Non-accrual loans are included in average balances outstanding but with no related interest income during the period of non-accrual.

(3) Represents the difference between the

yield on earning assets and cost of funds.

(4) Represents tax equivalent net interest income divided by average interest-earning assets.

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The following table summarizes the changes in tax-equivalent interest earned and paid resulting from changes in the volume of earning assets and paying liabilities and changes in their interest rates. The changes in interest due to both rate and volume have been allocated to the volume and rate columns in proportion to dollar amounts.

	Three Months Ended March 31, 2009 Compared to 2008 $ Increase/(Decrease) due to		
(In Thousands)	**Volume**	**Rate**	**Total**
Interest Earned On:			
Loans (1)	$ 2,100	$ (3,361)	$ (1,261)
Securities available-for-sale (1)	(1,722)	295	(1,427)
Securities held-to-maturity (1)	(75)	5	(70)
Interest-bearing deposits with other banks	136	(277)	(141)
Total interest-earning assets	439	(3,338)	(2,899)
Interest Paid On:			
Demand deposits	8	(5)	3
Savings deposits	(64)	(767)	(831)
Time deposits	1,675	(2,021)	(346)
Fed funds purchased	(9)	(9)	(18)
Retail repurchase agreements	(244)	(388)	(632)
Wholesale repurchase agreements		37	37
FHLB borrowings and other long-term debt	(600)	(370)	(970)
Total interest-bearing liabilities	766	(3,523)	(2,757)
Change in net interest income, tax-equivalent	$ (327)	$ 185	$ (142)

(1) Fully taxable equivalent using a rate of 35%.

Provision and Allowance for Loan Losses

There was significant disruption and volatility in the financial and capital markets during 2008 and the first three months of 2009. Turmoil in the mortgage market adversely impacted both domestic and global markets, resulting in a credit and liquidity crisis. The disruption has been exacerbated by significant declines in valuations within the real estate and housing markets. Decreases in real estate values could adversely affect the value of property used as collateral for loans, including loans originated by the Company. Adverse changes in the economy may have a negative effect on the ability of the Company s borrowers to make timely loan payments, which would have an adverse impact on the Company s earnings. A further increase in loan delinquencies could adversely impact loan loss experience, causing potential increases in the provision and allowance for loan losses.

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The allowance for loan losses was $16.56 million at March 31, 2009, $15.98 million at December 31, 2008 and $12.86 million at March 31, 2008. The Company s allowance for loan loss activity for the quarters ended March 31, 2009 and 2008, is as follows:

	For the Three Months Ended March 31,	
(In Thousands)	**2009**	**2008**
Allowance for loan losses		
Beginning balance	$ 15,978	$ 12,833
Provision for loan losses	2,087	323
Charge-offs	(1,730)	(966)
Recoveries	220	672
Net charge-offs	(1,510)	(294)
Ending balance	$ 16,555	$ 12,862

The total allowance for loan losses to loans held for investment ratio was 1.30% at March 31, 2009, compared with 1.24% at December 31, 2008, and 1.09% at March 31, 2008. Management considers the allowance adequate based upon its analysis of the portfolio as of March 31, 2009. However, no assurances can be made that future adjustments to the allowance for loan losses will not be necessary as a result of increases in non-performing loans and other factors.

Throughout the first quarter of 2009, the Company incurred net charge-offs of $1.51 million compared with $294 thousand in 2008. Annualized net charge-offs for the first quarter of 2009 were 0.47%. The Company made provisions for loan losses of $2.09 million for the first quarter of 2009 compared to $323 thousand in 2008. The increase in loan loss provision is primarily attributable to rising loss factors as net charge-offs were higher than in 2008. Qualitative risk factors were also higher, reflective of the higher risk of inherent loan losses due to rising unemployment, recessionary pressures, and devaluation of various categories of collateral.

Noninterest Income

Noninterest income consists of all revenues that are not included in interest and fee income related to earning assets. Noninterest income for the first quarter of 2009 was $8.42 million compared with $9.14 million in the same period of 2008, a decrease of $717 thousand, or 7.84%. Wealth management revenues increased $85 thousand, or 9.45%, to $984 thousand for the three months ended March 31, 2009, compared with the same period in 2008. IPC added several large accounts during 2008. Service charges on deposit accounts increased $58 thousand, or 1.87%, to $3.16 million for the three months ended March 31, 2009, compared with the same period in 2008. The increase is smaller than recent quarters increases due to lower consumer spending and a generally higher rate of savings. Other service charges, commissions, and fees increased $57 thousand, or 5.08%, to $1.18 million for the three months ended March 31, 2009, compared with the same period in 2008. Insurance commissions for the first quarter of 2009 were $2.32 million, an increase of $973 thousand, or 41.99%, over 2008. Increased insurance commissions reflect revenue increases associated with agency acquisitions made by GreenPoint throughout 2008. Other operating income was $586 thousand for the three months ended March 31, 2009, a decrease of $272 thousand, or 46.42%, compared with the same period in 2008. Other operating income was down due largely to decreases in dividends on FHLB stock. At March 31, 2009, the Company recognized $209 thousand of other-than-temporary impairment on several smaller equity security holdings. During the first quarter of 2009, securities gains of $411 thousand were realized, compared with a gain of $1.82 million in the comparable period in 2008.

Noninterest Expense

Noninterest expense totaled $15.19 million for the quarter ended March 31, 2009, a decrease of $1.09 million, or 6.69%, from the same period in 2008. Salaries and benefits for the first quarter of 2009 increased $76 thousand, or

0.98%, compared to the same period in 2008. Salaries and benefits at GreenPoint increased $438 thousand over the prior first quarter, a result of new agency acquisitions, and salaries and benefits at the new branches from Coddle Creek were $341 thousand. Decreases in general bank staffing levels and benefits largely offset the increases. Occupancy and furniture and fixtures expenses increased between the comparable periods with the addition of GreenPoint and the Coddle Creek branches. Other non- interest expense totaled $4.54 million for the first quarter of 2009, a decrease of $79 thousand, or 1.71%, from $4.62 million for the first quarter of 2008.

Over the course of the last two quarters, the FDIC has announced increases in deposit insurance premiums, as well as proposals to levy special assessments. The Company expects the increased deposit insurance premiums will add approximately $400 thousand in quarterly expense and the FDIC s proposed special assessment could approximate $3.20 million, depending on the final special assessment level determined by the FDIC.

Income Tax Expense

Income tax expense is comprised of federal and state current and deferred income taxes on pre-tax earnings of the Company. Income taxes as a percentage of pre-tax income may vary significantly from statutory rates due to items of income and expense which are excluded, by law, from the calculation of taxable income. These items are commonly referred to as permanent differences. The most significant permanent differences for the Company include income on state and municipal securities which are exempt from federal income tax, certain dividend payments which are deductible by the Company, and tax credits generated by investments in low income housing and historic rehabilitations.

For the first quarter of 2009, income taxes were $2.35 million compared with $2.58 million for the first quarter of 2008. For the quarters ended March 31, 2009 and 2008, the effective tax rates were 30.97% and 28.44%, respectively. The increase in the effective tax rate is due largely to decreases in tax-free municipal security income.

FINANCIAL CONDITION

Total assets at March 31, 2009, increased $65.91 million, or 3.09%, to $2.20 billion from December 31, 2008. The increase reflects net increases in the securities portfolio, continued loan payoffs, and higher levels of customer deposits as a result of deposit campaigns and a general movement of funds into FDIC insured products.

Securities

Available-for-sale securities were $549.66 million at March 31, 2009, compared with $520.72 million at December 31, 2008, an increase of $28.94 million, or 5.56%. Held-to-maturity securities declined to $8.47 million at March 31, 2009, compared with $8.67 million at December 31, 2008.

Available-for-sale and held-to-maturity securities are reviewed quarterly for possible other-than-temporary impairment. This review includes an analysis of the facts and circumstances of each individual investment such as the length of time the fair value has been below cost, timing and amount of contractual cash flows, the expectation for that security s performance, the creditworthiness of the issuer and the Company s intent and ability to hold the security to recovery or maturity. The portion of a decline in value associated with probable credit losses, if any, would be recorded as a loss within noninterest income in the Consolidated Statements of Income. The Company does not believe any unrealized loss remaining in the investment portfolio, individually or in the aggregate, as of March 31, 2009, represents other-than-temporary impairment. The Company intends to hold these securities until recovery or maturity and it is more likely than not that it will not sell these securities before recovery.

Included in available-for-sale securities is a portfolio of trust-preferred securities with a total market value of approximately $49.47 million as of March 31, 2009. That portfolio is comprised of single-issue securities and pooled trust-preferred securities. The single-issue securities had a total market value of approximately $26.77 million as of March 31, 2009, compared with their adjusted cost basis of approximately $55.52 million.

At March 31, 2009, the total market value of the pooled trust-preferred securities was approximately $22.71 million, compared with an adjusted cost basis of approximately $93.37 million. The collateral underlying these securities is comprised of 86% of bank trust-preferred securities and subordinated debt issuances of over 500 banks nationwide. The remaining collateral is from insurance companies and real estate investment trusts. The securities carry variable rate structures that float at a prescribed margin over 3-month LIBOR. During 2008 and 2009, these securities experienced credit rating downgrades, and certain of these securities are on negative watch. As of December 31, 2008, the Company recorded pre-tax other-than-temporary impairment charges of $15.46 million for one of its pooled trust preferred securities with demonstrated a probable adverse change in cash flow. Recent modeling of the expected cash flows from the pooled trust-preferred securities, at present, does not suggest any of the remaining securities will have an adverse cash flow effect under any of the scenarios modeled due to the existence of other subordinate classes within the pools.

The Company made a cumulative effect adjustment of $6.13 million as of January 1, 2009, to recognize the portion of non-credit losses associated with a non-agency mortgage-backed security for which the Company recognized a pre-tax

other-than-temporary impairment charge of $14.47 million as of December 31, 2008. The Company determined that only $4.25 million of the original impairment charge was due to probable credit losses.

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The following table provides details regarding the type and credit ratings within the securities portfolios as of March 31, 2009. In the case of multiple ratings, the lower rating was utilized.

	Par Value	Fair Value	Amortized Cost	Unrealized Gains/(Losses) Recognized in OCL	Cumulative OTTI
			(Amounts in Thousands)		
Available for sale					
Agency securities	$ 53,435	$ 54,127	$ 53,425	$ 702	$
Agency mortgage-backed securities	273,870	282,075	275,257	6,818	
Non-Agency mortgage-backed securities:					
AAA	7,250	5,786	7,206	(1,420)	
B	25,000	10,730	20,968	(10,238)	4,252
Total	32,250	16,516	28,174	(11,658)	4,252
Municipals:					
AAA	5,955	6,043	5,956	87	
AA	54,230	54,739	54,261	478	
A	46,282	46,394	46,284	110	
BBB	30,005	28,788	29,106	(318)	
Not rated	5,920	5,659	5,929	(270)	
Total	142,392	141,623	141,536	87	
Single issuer bank trust preferred securities:					
AA	10,300	4,171	10,064	(5,893)	
A	17,130	8,852	16,750	(7,898)	
BB	29,125	13,745	28,703	(14,958)	
Total	56,555	26,768	55,517	(28,749)	
Pooled trust preferred securities:					
A	20,000	935	20,000	(19,065)	15,456
CCC	88,659	21,770	73,367	(51,597)	
Total	108,659	22,705	93,367	(70,662)	15,456
Equity securities		5,850	7,006	(1,156)	209
Total	$ 667,161	$ 549,664	$ 654,282	$ (104,618)	$ 19,917
Held to maturity					
Municipals:					
AA	$ 3,680	$ 3,727	$ 3,665	$	$
A	3,670	3,566	3,491		
BBB	1,395	1,327	1,315		
Total	$ 8,745	$ 8,620	$ 8,471	$	$

The Company closely monitors this portfolio due to the substantial market discounts. The market discounts reflect the credit market disruption in bank subordinated debt instruments and the possibility of future negative credit events within the banking sector, which could affect collateral within certain of the pooled and single-issue securities. Monitoring for other-than-temporary impairment (OTI) is dependent on the aforementioned assumptions regarding future credit events and the general strength of the banking industry as it deals with credit losses in the current recessionary real estate market. Acceleration of bank losses and the possibility of unforeseen bank failures could result in changes in the Company s outlook for these securities and possible future OTI. Accordingly, there can be no assurance that continued deterioration of credit portfolios within certain of those banks will not lead to unanticipated deferrals of interest payments and defaults beyond those assumed in the Company s impairment testing. At present, cash flow modeling indicates varying ability to absorb additional deferrals and defaults before incurring breaks in interest or principal for the various pools.

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Loan Portfolio

Loans Held for Sale: The $1.45 million balance of loans held for sale at March 31, 2009, represents mortgage loans that are sold to investors on a best efforts basis. Accordingly, the Company does not retain the interest rate risk involved in the commitment. The gross notional amount of outstanding commitments at March 31, 2009, was $11.28 million on 71 loans.

Loans Held for Investment: Total loans held for investment were $1.28 billion at March 31, 2009, representing a decline of $21.37 million from December 31, 2008, and an increase of $97.29 million from March 31, 2008. The average loan to deposit ratio decreased to 82.83% for the first quarter of 2009, compared with 86.01% for the fourth quarter of 2008 and 87.68% for the first quarter of 2008. Year-to-date average loans of $1.29 billion increased $86.70 million when compared to 2008.

Over the course of the last three years, the Company has taken measures to enhance its commercial underwriting standards. The more stringent underwriting has led to improved credit quality, and coupled with a reduced complement of commercial loan officers, has resulted in decreases in the loan portfolio. The Company also continues to realize net payoffs in the area of consumer finance, as it competes with credit card lenders and captive automobile finance companies.

The held for investment loan portfolio continues to be diversified among loan types and industry segments. The following table presents the various loan categories and changes in composition as of March 31, 2009, December 31, 2008, and March 31, 2008.

	March 31 , 2009		December 31, 2008		March 31 , 2008	
(Dollars in Thousands)	**Amount**	**Percent**	**Amount**	**Percent**	**Amount**	**Percent**
Loans Held for Investment						
Commercial and agricultural	$ 81,880	6.41%	$ 85,034	6.55%	$ 88,532	7.51%
Commercial real estate	405,549	31.76%	407,638	31.40%	376,087	31.89%
Residential real estate	597,372	46.79%	602,573	46.42%	488,860	41.45%
Construction	124,320	9.74%	130,610	10.06%	151,242	12.82%
Consumer	62,353	4.88%	66,258	5.10%	69,377	5.88%
Other	5,316	0.42%	6,046	0.47%	5,406	0.46%
Total	$ 1,276,790	100.00%	$ 1,298,159	100.00%	$ 1,179,504	100.01%
Loans Held for Sale	$ 1,445		$ 1,024		$ 2,116	

Non-Performing Assets

Non-performing assets include loans on non-accrual status, loans contractually past due 90 days or more and still accruing interest, and other real estate owned (OREO). Non-performing assets were $13.74 million at March 31, 2009, $14.09 million at December 31, 2008, and $3.54 million at March 31, 2008. The percentage of non-performing assets to total loans and OREO was 1.07% at March 31, 2009, 1.08% at December 31, 2008, and 0.30% at March 31, 2008. The following schedule details non-performing assets by category at the close of each of the quarters ended March 31, 2009 and 2008, and December 31, 2008.

(In Thousands)	**March 31, 2009**	**December 31, 2008**	**March 31, 2008**
Non-accrual	$ 10,628	$ 12,763	$ 3,137
Ninety days past due and accruing			
Other real estate owned	3,114	1,326	400

Total non-performing assets	$ 13,742	$ 14,089	$ 3,537

Ongoing activity within the classification and categories of non-performing loans includes collections on delinquencies, foreclosures and movements into or out of the non-performing classification as a result of changing customer business conditions. OREO was $3.11 million at March 31, 2009, and is carried at the lesser of estimated net realizable value or cost.

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Deposits and Other Borrowings

Total deposits increased by $79.69 million, or 5.30%, during the first three months of 2009. Non interest-bearing demand deposits increased $8.24 million to $207.95 million at March 31, 2009, compared with $199.71 million at December 31, 2008. Interest-bearing demand deposits increased $9.82 million to $194.93 million at March 31, 2009. Savings increased $9.43 million, or 3.05%, and time deposits increased $52.20 million, or 6.45%, during the first three months of 2009. The Company s increase in deposits is likely due to increasing customer household savings and a desire for FDIC insured deposit products.

Securities sold under repurchase agreements decreased $12.09 million, or 7.29%, in the first quarter 2009 to $153.82 million. There were no federal funds purchased outstanding at March 31, 2009, as the Company maintained strong liquidity through the first quarter.

Stockholders Equity

Total stockholders equity decreased $2.63 million, or 1.19%, from $220.34 million at December 31, 2008, to $217.71 million at March 31, 2009, as the Company experienced increases in other comprehensive losses associated with the Company s investment portfolio. The change in equity was the result of net earnings of $5.23 million, less preferred dividends of $571 thousand, the cumulative effect adjustment of $6.13 million, and other comprehensive loss of $13.86 million.

During the first quarter, the Company common stock traded at a level below its book value per share, and as a result, the Company performed a level one goodwill evaluation for each of its segments. The results of the level one evaluation did not provide evidence of impairment of goodwill in either of the Company s segments.

Risk-Based Capital

Risk-based capital guidelines promulgated by federal banking agencies weight balance sheet assets and off-balance sheet commitments based on inherent risks associated with the respective asset types. At March 31, 2009, the Company s total capital to risk-weighted assets ratio was 12.64% compared with 12.91% at December 31, 2008. The Company s Tier 1 capital to risk-weighted assets ratio was 11.70% at March 31, 2009, compared with 11.92% at December 31, 2008. The Company s Tier 1 leverage ratio at March 31, 2009, was 9.77% compared with 9.75% at December 31, 2008. All of the Company s regulatory capital ratios exceed the current well-capitalized levels. Regulatory capital ratios declined from December 31, 2008, primarily because of the treatment of collateralized mortgage obligations and collateralized debt obligations when rated below investment grade.

PART I. ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Liquidity and Capital Resources

At March 31, 2009, the Company maintained liquidity in the form of cash and cash equivalent balances of $100.96 million, unpledged securities available-for-sale of $183.90 million, and total FHLB credit availability of approximately $143.9 million. Cash and cash equivalents as well as advances from the FHLB are immediately available for satisfaction of deposit withdrawals, customer credit needs and operations of the Company. Investment securities available-for-sale represents a secondary level of liquidity available for conversion to liquid funds in the event of extraordinary needs. The Company also maintains approved lines of credit with correspondent banks as backup liquidity sources.

The Company maintains a liquidity policy as a means to manage liquidity and the associated risk. The policy includes a Liquidity Contingency Plan (the Liquidity Plan) that is designed as a tool for the Company to detect liquidity issues promptly in order to protect depositors, creditors and shareholders. The Liquidity Plan includes monitoring various internal and external indicators such as changes in core deposits and changes in market conditions. It provides for timely responses to a wide variety of funding scenarios ranging from changes in loan demand to a decline in the Company s quarterly earnings to a decline in the market price of the Company s stock. The Liquidity Plan calls for specific responses designed to meet a wide range of liquidity needs based upon assessments on a recurring basis by the Company and its Board of Directors.

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Interest Rate Risk and Asset/Liability Management

The Company s profitability is dependent to a large extent upon its net interest income, which is the difference between its interest income on interest-earning assets, such as loans and securities, and its interest expense on interest-bearing liabilities, such as deposits and borrowings. The Company, like other financial institutions, is subject to interest rate risk to the degree that interest-earning assets reprice differently than interest-bearing liabilities. The Company manages its mix of assets and liabilities with the goals of limiting its exposure to interest rate risk, ensuring adequate liquidity, and coordinating its sources and uses of funds while maintaining an acceptable level of net interest income given the current interest rate environment.

The Company s primary component of operational revenue, net interest income, is subject to variation as a result of changes in interest rate environments in conjunction with unbalanced repricing opportunities on earning assets and interest-bearing liabilities. Interest rate risk has four primary components: repricing risk, basis risk, yield curve risk and option risk. Repricing risk occurs when earning assets and paying liabilities reprice at differing times as interest rates change. Basis risk occurs when the underlying rates on the assets and liabilities the institution holds change at different levels or in varying degrees. Yield curve risk is the risk of adverse consequences as a result of unequal changes in the spread between two or more rates for different maturities for the same instrument. Lastly, option risk is due to embedded options, often put or call options, given or sold to holders of financial instruments.

In order to mitigate the effect of changes in the general level of interest rates, the Company manages repricing opportunities and thus, its interest rate sensitivity. The Company seeks to control its interest rate risk exposure to insulate net interest income and net earnings from fluctuations in the general level of interest rates. To measure its exposure to interest rate risk, quarterly simulations of net interest income are performed using financial models that project net interest income through a range of possible interest rate environments including rising, declining, most likely and flat rate scenarios. The simulation model used by the Company captures all earning assets, interest-bearing liabilities and off-balance sheet financial instruments and combines the various factors affecting rate sensitivity into an earnings outlook. The results of these simulations indicate the existence and severity of interest rate risk in each of those rate environments based upon the current balance sheet position, assumptions as to changes in the volume and mix of interest-earning assets and interest-paying liabilities and the Company s estimate of yields to be attained in those future rate environments and rates that will be paid on various deposit instruments and borrowings. These assumptions are inherently uncertain and, as a result, the model cannot precisely predict the impact of fluctuations in interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude, and frequency of interest rate changes, as well as changes in market conditions and the Company s strategies. However, the earnings simulation model is currently the best tool available to the Company for managing interest rate risk.

Specific strategies for management of interest rate risk have included shortening the amortized maturity of new fixed-rate loans, increasing the volume of adjustable-rate loans to reduce the average maturity of the Company s interest-earning assets, and monitoring the term and structure of liabilities to maintain a balanced mix of maturity and repricing structures to mitigate potential exposure. At March 31, 2009, net interest income modeling shows the Company to be in a relatively neutral position. Additionally, structure in the Company s assets and liabilities creates a situation where net interest income decreases in a sustained increasing rate environment.

The Company has established policy limits for tolerance of interest rate risk that allow for no more than a 10% reduction in projected net interest income for the next twelve months based on a comparison of net interest income simulations in various interest rate scenarios. In addition, the policy addresses exposure limits to changes in the economic value of equity according to predefined policy guidelines. The most recent simulation indicates that current exposure to interest rate risk is within the Company s defined policy limits.

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The following table summarizes the projected impact on the next twelve months net interest income and the economic value of equity as of March 31, 2009, and December 31, 2008, of immediate and sustained rate shocks in the interest rate environments of plus and minus 100 and 200 basis points from the base simulation, assuming no remedial measures are effected. As of March 31, 2009, the Federal Open Market Committee set a target range for federal funds of 0 to 25 basis points, rendering a complete downward shock of 200 basis points not realistic and not meaningful. In the downward rate shocks presented, benchmark interest rates are dropped with floors near 0%.

The economic value of equity is a measure which reflects the impact of changing rates on the underlying values of the Company s assets and liabilities in various rate scenarios. The scenarios illustrate the potential estimated impact of instantaneous rate shocks on the underlying value of equity. The economic value of the equity is based on the present value of all the future cash flows under the different rate scenarios.

Rate Sensitivity Analysis

(Dollars in Thousands)	**March 31, 2009**			
Increase (Decrease) in Interest Rates (Basis Points)	**Change in Net Interest Income**	**% Change**	**Change in Econcomic Value of Equity**	**% Change**
200	$(370)	(0.6)	$ 11,911	5.0
100	(575)	(0.9)	15,508	6.5
(100)	176	0.3	(26,274)	(11.0)

	December 31, 2008			
Increase (Decrease) in Interest Rates (Basis Points)	**Change in Net Interest Income**	**% Change**	**Change in Econcomic Value of Equity**	**% Change**
200	$1,479	2.3	$ (8,040)	(3.7)
100	1,493	2.3	719	0.3
(100)	1,874	2.9	(21,443)	(9.9)

PART I. ITEM 4. Controls and Procedures

Disclosure Controls and Procedures

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company s management, including the Company s Chief Executive Officer (CEO) along with the Company s Chief Financial Officer (CFO), of the effectiveness of the Company s disclosure controls and procedures pursuant to the Securities Exchange Act of 1934 (Exchange Act) Rule 13a-15(b). Based on that evaluation, the Company s CEO along with the Company s CFO concluded that the Company s disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company s periodic SEC filings.

The Company s management, including the CEO and CFO, does not expect that the Company s disclosure controls and internal controls will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls.

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Changes in Internal Control Over Financial Reporting

There have not been any changes in the Company s internal controls over financial reporting during the quarter ended March 31, 2009, that have materially affected, or are reasonably likely to materially affect, the Company s internal controls over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

The Company is currently a defendant in various legal actions and asserted claims in the normal course of business. Although the Company and legal counsel are unable to assess the ultimate outcome of each of these matters with certainty, they are of the belief that the resolution of these actions should not have a material adverse affect on the financial position, results of operations, or cash flows of the Company.

ITEM 1A. Risk Factors

There were no material changes to the risk factors as presented in the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Not Applicable

(b) Not Applicable

(c) Issuer Purchases of Equity Securities

There were no open market purchases by the Company of its equity securities during the three months ended March 31, 2009. The maximum number of shares that may yet be purchased under a publicly announced plan at March 31, 2009, was 645,015 shares. The Company s stock repurchase plan allows for the purchase and retention of up to 1,100,000 shares. The plan has no expiration date and remains open. The Company held 454,985 shares in treasury at March 31, 2009.

ITEM 3. Defaults Upon Senior Securities

Not Applicable

ITEM 4. Submission of Matters to a Vote of Security Holders

Not Applicable

ITEM 5. Other Information

Not Applicable

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ITEM 6. Exhibits

(a) Exhibits

hibit No.	Exhibit
	Agreement and Plan of Merger dated July 31, 2008, among First Community Bancshares, Inc. and Coddle Creek Financial Corp. (21)
	Articles of Incorporation of First Community Bancshares, Inc., as amended. (1)
)	Certificate of Designation Series A Preferred Stock (22)
i)	Bylaws of First Community Bancshares, Inc., as amended. (17)
	Specimen stock certificate of First Community Bancshares, Inc. (3)
	Indenture Agreement dated September 25, 2003. (11)
	Amended and Restated Declaration of Trust of FCBI Capital Trust dated September 25, 2003. (11)
	Preferred Securities Guarantee Agreement dated September 25, 2003. (11)
	Form of Certificate for the Series A Preferred Stock (22)
	Warrant to purchase 176,546 shares of common stock of First Community Bancshares, Inc (22)
1	First Community Bancshares, Inc. 1999 Stock Option Contracts (2) and Plan. (4)
1.1	Amendment to First Community Bancshares, Inc. 1999 Stock Option Plan. (11)
2	First Community Bancshares, Inc. 2001 Non-Qualified Directors Stock Option Plan. (5)
3	Employment Agreement dated December 16, 2008, between First Community Bancshares, Inc. and John M. Mendez. (6)
4	First Community Bancshares, Inc. 2000 Executive Retention Plan, as amended. (24)
5	First Community Bancshares, Inc. Split Dollar Plan and Agreement. (2)
6	First Community Bancshares, Inc. 2001 Directors Supplemental Retirement Plan. (2)
6.1	First Community Bancshares, Inc. 2001 Directors Supplemental Retirement Plan. Second Amendment (B.W. Harvey, Sr. October 19, 2004). (14)
7	First Community Bancshares, Inc. Wrap Plan. (7)
8	Reserved.
9	Form of Indemnification Agreement between First Community Bancshares, Inc., its Directors and Certain Executive Officers. (9)

10 Form of Indemnification Agreement between First Community Bank, N. A, its Directors and Certain Executive Officers. (9)

11 Reserved.

12 First Community Bancshares, Inc. 2004 Omnibus Stock Option Plan (10) and Award Agreement. (13)

13 Reserved.

14 First Community Bancshares, Inc. Directors Deferred Compensation Plan. (7)

15 First Community Bancshares, Inc. Deferred Compensation and Supplemental Bonus Plan For Key Employees. (15)

16 Employment Agreement dated November 30, 2006, between First Community Bank, N. A. and Ronald L. Campbell. (19)

17 Employment Agreement dated September 28, 2007, between GreenPoint Insurance Group, Inc. and Shawn C. Cummings. (20)

18 Securities Purchase Agreement by and between the United States Department of the Treasury and First Community Bancshares, I
dated November 21, 2008. (22)

19 Employment Agreement dated December 16, 2008, between First Community Bancshares, Inc. and David D. Brown. (23)

1* Rule 13a-14(a)/a5d-14(a) Certification of Chief Executive Officer.

2* Rule 13a-14(a)/a5d-14(a) Certification of Chief Financial Officer.

Certification of Chief Executive Officer and Chief Financial Officer Section 1350.

* Furnished herewith.

(1) Incorporated by reference from the Quarterly Report on Form 10-Q for the period ended June 30, 2005, filed on August 5, 2005.

(2) Incorporated by reference from the Quarterly Report on Form 10-Q for the period ended June 30, 2002, filed on August 14, 2002.

(3) Incorporated by reference from the Annual Report on Form 10-K for the period ended December 31, 2002, filed on March 25, 2003, as amended on March 31, 2003.

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(4) Incorporated by reference from the Annual Report on Form 10-K for the period ended December 31, 1999, filed on March 30, 2000, as amended April 13, 2000.

(5) The option agreements entered into pursuant to the 1999 Stock Option Plan and the 2001 Non-Qualified Directors Stock Option Plan are incorporated by reference from the Quarterly Report on Form 10-Q for the period ended June 30, 2002, filed on August 14, 2002.

(6) Incorporated by reference from Exhibit 10.1 of the Current Report on Form 8-K dated and filed December 16, 2008. The Registrant has entered into substantially identical agreements with Robert L. Buzzo and E. Stephen Lilly, with the only differences being with respect to title and salary.

(7) Incorporated by reference from the Current Report on Form 8-K dated August 22, 2006, and filed August 23, 2006.

(8) Reserved.

(9) Form of indemnification agreement entered into by the Company and by First Community Bank, N. A. with their respective directors and certain

officers of each including, for the Registrant and Bank: John M. Mendez, Robert L. Schumacher, Robert L. Buzzo, E. Stephen Lilly, David D. Brown, and Gary R. Mills. Incorporated by reference from the Annual Report on Form 10-K for the period ended December 31, 2003, filed on March 15, 2004, and amended on May 19, 2004.

(10) Incorporated by reference from the 2004 First Community Bancshares, Inc. Definitive Proxy filed on March 19, 2004.

(11) Incorporated by reference from the Quarterly Report on Form 10-Q for the period ended September 30, 2003, filed on November 10, 2003.

(12) Incorporated by reference from the Quarterly %">

loans held for investment, net	1.70%	1.18%	0.20%	0.05%	0.13%
Non-accrual and 90 days or more past due loans as a percentage of total assets	1.42%	0.96%	0.16%	0.04%	0.08%
Non-performing assets as a percentage of total assets	1.99%	1.20%	0.16%	0.04%	0.08%

(1) Includes $1.4 million of non-performing loans at June 30, 2008.

The Bank assesses loans individually and identifies impairment when the accrual of interest has been discontinued, loans have been restructured or management has serious doubts about the future collectibility of principal and interest, even though the loans are currently performing. Factors considered in determining impairment include, but are not limited to, expected future cash flows, the financial condition of the borrower and current economic conditions. The Bank measures each impaired loan based on the fair value of its collateral and charges off those loans or portions of loans deemed uncollectible.

During fiscal year ended June 30, 2008, 32 loans for $10.5 million were modified from their original terms, were re-underwritten at current market interest rates and were identified in our asset quality reports as restructured loans. As of June 30, 2008, these restructured loans were classified as follows: six are classified as pass ($2.3 million); 13 are classified as special mention and remain on accrual status ($4.0 million); eight are classified as substandard and remain on accrual status ($2.8 million); and five are classified as substandard on non-accrual status ($1.4 million).

The following table shows the restructured loans by type, net of specific allowances, at June 30, 2008:

	June 30, 2008		
(In Thousands)	Recorded Investment	Allowance For Loan Losses	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 1,900	$ (545)	$ 1,355
Without a related allowance	9,101	-	9,101
Total single-family loans	11,001	(545)	10,456
Other loans:			
Without a related allowance	28	-	28
Total other loans	28	-	28
Total restructured loans	$ 11,029	$ (545)	$ 10,484

As of June 30, 2008, total non-performing assets were $32.5 million, or 1.99% of total assets, which was primarily comprised of 52 single-family loans originated for investment ($15.4 million), 12 construction loans originated for investment ($4.7 million), 12 single-family loans repurchased from, or unable to sell to investors ($1.9 million) and 45 real estate owned properties ($9.4 million). Compared to June 30, 2007, total non-performing assets increased $12.8 million, or 65%, primarily due to the weakness in the California real estate market and increases in interest rates on mortgages.

Foregone interest income, which would have been recorded for the fiscal year June 30, 2008 had the impaired loans been current in accordance with their original terms, amounted to $1.9 million and was not included in the results of operations for the fiscal year June 30, 2008.

Foreclosed Real Estate. Real estate acquired by the Bank as a result of foreclosure or by deed-in-lieu of foreclosure is classified as real estate owned until it is sold. When a property is acquired, it is recorded at the lower of its cost, which is the unpaid principal balance of the related loan plus foreclosure costs or its market value less the cost of sale. Subsequent declines in value are charged to operations. At June 30, 2008, the Bank had $9.4 million in real estate owned, comprised of 30 single-family properties, one multi-family property and 14 undeveloped lots. The 14 undeveloped lots are located in Coachella, California.

Asset Classification. The OTS has adopted various regulations regarding the problem assets of savings institutions. The regulations require that each institution review and classify its assets on a regular basis. In addition, in connection with examinations of institutions, OTS examiners have the authority to identify problem assets and, if appropriate, require them to be classified. There are three classifications for problem assets: substandard, doubtful and loss. Substandard assets have one or more defined weaknesses and are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Doubtful assets have the weaknesses of substandard assets with the additional characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss. An asset classified as a loss is considered uncollectible and of such little value that continuance as an asset of the institution is not warranted. If an asset or portion thereof is classified as loss, the institution establishes a specific loss allowance for the full amount or for the portion of the asset classified as loss. All or a portion of general allowances for loan losses established to cover probable losses related to assets classified substandard or doubtful may be included in determining an institution's regulatory capital, while specific valuation allowances for loan losses generally do not qualify as regulatory capital. Assets that do not currently expose the institution to sufficient risk to warrant

classification in one of the aforementioned categories but possess weaknesses are designated as special mention and are monitored by the Bank.

The aggregate amounts of the Bank's classified assets, including assets designated as special mention, were as follows at the dates indicated:

	At June 30,	
	2008	2007
(Dollars In Thousands)		
Special mention assets	$ 29,467	$ 13,299
Substandard assets	29,781	18,990
Total classified loans	59,248	32,289
Real estate owned, net	9,355	3,804
Total classified assets	$ 68,603	$ 36,093
Total classified assets as a percentage of total assets	4.20%	2.19%

The Bank's classified assets increased $32.5 million, or 90%, to $68.6 million at June 30, 2008 from $36.1 million at June 30, 2007. This increase was primarily attributable to the decline in real estate market values, increases in mortgage interest rates and a slower economy. As of June 30, 2008, special mention assets were comprised of 33 single-family loans ($11.8 million), two construction loans ($8.1 million), six multi-family loans ($8.0 million), two commercial real estate loans ($1.4 million), one consumer loan ($20,000), one commercial business loan ($100,000) and one land loan ($28,000); substandard assets were comprised of 79 single-family loans ($23.6 million), 12 construction loans ($4.7 million), two land loans ($575,000), one commercial real estate loan ($572,000) and one multi-family loan ($367,000). These classified assets are primarily located in Southern California.

As set forth below, assets classified as special mention and substandard as of June 30, 2008 were comprised of 143 loans totaling $59.2 million.

(Dollars In Thousands)	Number of Loans	Special Mention	Substandard	Total
Mortgage loans:				
Single-family	112	$ 11,772	$ 23,552	$ 35,324
Multi-family	7	8,026	367	8,393
Commercial real estate	3	1,388	572	1,960
Construction	14	8,133	4,715	12,848
Commercial business loans	3	100	-	100
Consumer loans	1	20	-	20
Other loans	3	28	575	603
Total	143	$ 29,467	$ 29,781	$ 59,248

Not all of the Bank's classified assets are delinquent or non-performing. In determining whether the Bank's assets expose the Bank to sufficient risk to warrant classification, the Bank may consider various factors, including the payment history of the borrower, the loan-to-value ratio, and the debt coverage ratio of the property securing the loan. After consideration of these factors, the Bank may determine that the asset in question, though not currently delinquent, presents a risk of loss that requires it to be classified or designated as special mention. In addition, the Bank's loans held for investment may include commercial and multi-family real estate loans with a balance exceeding the current market value of the collateral which are not classified because they are performing and have borrowers who have sufficient resources to support the repayment of the loan.

The Bank's market area continues to experience difficult economic conditions. The Bank anticipates that delinquent loans and net charge-offs will continue to occur during the rest of calendar 2008 and well into 2009.

Allowance for Loan Losses. The allowance for loan losses is maintained to cover losses inherent in the loans held for investment. In originating loans, the Bank recognizes that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the collateral securing the loan. The responsibility for the review of the Bank's assets and the determination of the adequacy of the allowance lies with the Internal Asset Review Committee ("IAR Committee"). The Bank adjusts its allowance for loan losses by charging or crediting its provision for loan losses against the Bank's operations.

The Bank has established a methodology for the determination of the provision for loan losses. The methodology is set forth in a formal policy and takes into consideration the need for an overall allowance for loan losses as well as specific allowances that are tied to individual loans. The Bank's methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance and specific allowance for identified problem loans.

The formula allowance is calculated by applying loss factors to the loans held for investment. The loss factors are applied according to loan program type and loan classification. The loss factors for each program type and loan classification are established based on an evaluation of the historical loss experience, prevailing market conditions, concentration in loan types and other relevant factors. Homogeneous loans, such as residential mortgage, home equity and consumer installment loans are considered on a pooled loan basis. A factor is assigned to each pool based upon expected charge-offs for one year. The factors for larger, less homogeneous loans, such as construction, multi-family and commercial real estate loans, are based upon loss experience tracked over business cycles considered appropriate for the loan type.

Specific valuation allowances are established to absorb losses on loans for which full collectibility may not be reasonably assured as prescribed in SFAS No. 114, "Accounting by Creditors for Impairment of A Loan," (as amended by SFAS No. 118). The amount of the specific allowance is based on the estimated value of the collateral securing the loan and other analyses pertinent to each situation. Estimates of identifiable losses are reviewed continually and, generally, a provision for losses is charged against operations on a monthly basis as necessary to maintain the allowance at an appropriate level. Management presents the minutes of the IAR Committee to the Bank's Board of Directors on a quarterly basis, which summarizes the actions of the Committee.

The IAR Committee meets quarterly to review and monitor conditions in the portfolio and to determine the appropriate allowance for loan losses. To the extent that any of these conditions are apparent by identifiable problem credits or portfolio segments as of the evaluation date, the IAR Committee's estimate of the effect of such conditions may be reflected as a specific allowance applicable to such credits or portfolio segments. Where any of these conditions is not apparent by specifically identifiable problem credits or portfolio segments as of the evaluation date, the IAR Committee's evaluation of the probable loss related to such condition is reflected in the general allowance. The intent of the Committee is to reduce the differences between estimated and actual losses. Pooled loan factors are adjusted to reflect current estimates of charge-offs for the subsequent 12 months. Loss activity is reviewed for non-pooled loans and the loss factors adjusted, if necessary. By assessing the probable estimated losses inherent in the loans held for investment on a quarterly basis, the Bank is able to adjust specific and inherent loss estimates based upon the most recent information that has become available.

At June 30, 2008, the Bank had an allowance for loan losses of $19.9 million, or 1.43% of gross loans held for investment, compared to an allowance for loan losses at June 30, 2007 of $14.8 million, or 1.09% of gross loans held for investment. A $13.1 million provision for loan losses was recorded in fiscal 2008, compared to $5.1 million in fiscal 2007. The Bank's current business strategy of expanding its investment in multi-family, commercial real estate, construction and commercial business loans, as well as rising delinquencies and defaults in single-family mortgage loans, may lead to increased levels of charge-offs. Although management believes the best information available is used to make such determinations, future adjustments to the allowance for loan losses may be necessary and results of

operations could be significantly and adversely affected if circumstances differ substantially from the assumptions used in making the determinations.

As a result of the decline in real estate values and the significant losses experienced by many financial institutions, there has been a higher level of scrutiny by regulatory authorities of the loan portfolio of financial institutions undertaken as a part of the examinations of such institutions. While the Bank believes that it has established its

existing allowance for loan losses in accordance with accounting principles generally accepted in the United States of America, there can be no assurance that regulators, in reviewing the Bank's loan portfolio, will not recommend that the Bank significantly increase its allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that substantial increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect the Bank's financial condition and results of operations.

During the course of fiscal year 2008, the Bank implemented more conservative underwriting standards commensurate with the deteriorating real estate market conditions. At June 30, 2008, the Bank requires verified documentation of income and assets, has limited the maximum loan-to-value to the lower of 90% of the appraised value or purchase price of the property, requires borrower paid or lender paid mortgage insurance when the loan-to-value ratio exceeds 75%, eliminated cash-out refinance programs, and limits the loan-to-value on non-owner occupied transactions to the lower of 65% of the appraised value or purchase price of the property.

The following table sets forth an analysis of the Bank's allowance for loan losses for the periods indicated. Where specific loan loss reserves have been established, any differences between the loss allowances and the amount of loss realized has been charged or credited to current operations.

	Year Ended June 30,				
	2008	2007	2006	2005	2004
(Dollars In Thousands)					
Allowance at beginning of period	$ 14,845	$ 10,307	$ 9,215	$ 7,614	$ 7,218
Provision for loan losses	13,108	5,078	1,134	1,641	819
Recoveries:					
Mortgage Loans:					
Single-family	188	-	-	-	-
Construction	32	-	-	-	-
Consumer loans	3	1	2	2	1
Total recoveries	223	1	2	2	1
Charge-offs:					
Mortgage loans:					
Single-family	(6,028)	(535)	-	-	-
Multi-family	(335)	-	-	-	-
Construction	(1,911)	-	-	-	-
Commercial business loans	-	-	(41)	(32)	(415)
Consumer loans	(4)	(6)	(3)	(10)	(9)
Total charge-offs	(8,278)	(541)	(44)	(42)	(424)
Net charge-offs	(8,055)	(540)	(42)	(40)	(423)
Allowance at end of period	$ 19,898	$ 14,845	$ 10,307	$ 9,215	$ 7,614
Allowance for loan losses as a percentage of gross loans held for investment	1.43%	1.09%	0.81%	0.81%	0.87%
Net charge-offs as a percentage of average loans receivable, net, during the period	0.58%	0.04%	-	-	0.05%
Allowance for loan losses as a percentage of					

non-performing loans at the end of the period	85.79%	93.32%	407.71%	1,561.86%	701.75%

The following table sets forth the breakdown of the allowance for loan losses by loan category at the periods indicated. Management believes that the allowance can be allocated by category only on an approximate basis. The allocation of the allowance is based upon an asset classification matrix. The allocation of the allowance to each category is not necessarily indicative of future losses and does not restrict the use of the allowance to absorb losses in any other categories.

	At June 30,							
	2008		2007		2006		2005	
(Dollars In Thousands)	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans
Mortgage loans:								
Single-family	$ 8,779	58.16 %	$ 2,893	59.72 %	$ 2,382	61.22 %	$ 1,924	65.63%
Multi-family	5,100	28.75	4,255	23.83	2,819	16.16	1,936	9.68
Commercial real estate	3,627	9.79	4,000	10.65	3,476	9.39	3,663	9.90
Construction	1,926	2.37	2,973	4.36	788	11.03	426	12.62
Commercial business loans	343	0.62	449	0.73	525	0.95	1,040	1.24
Consumer loans	16	0.04	14	0.04	16	0.05	16	0.06
Other loans	107	0.27	261	0.67	301	1.20	210	0.87
Total allowance for loan losses	$ 19,898	100.00 %	$ 14,845	100.00 %	$ 10,307	100.00 %	$ 9,215	100.00%

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Investment Securities Activities

Federally chartered savings institutions are permitted under federal and state laws to invest in various types of liquid assets, including U.S. Treasury obligations, securities of various federal agencies and government sponsored enterprises and of state and municipal governments, deposits at the FHLB, certificates of deposit of federally insured institutions, certain bankers' acceptances, mortgage-backed securities and federal funds. Subject to various restrictions, federally chartered savings institutions may also invest a portion of their assets in commercial paper and corporate debt securities. Savings institutions such as the Bank are also required to maintain an investment in FHLB – San Francisco stock.

The investment policy of the Bank, established by the Board of Directors and implemented by the Bank's Asset-Liability Committee ("ALCO"), seeks to provide and maintain adequate liquidity, complement the Bank's lending activities, and generate a favorable return on investments without incurring undue interest rate risk or credit risk. Investments are made based on certain considerations, such as yield, credit quality, maturity, liquidity and marketability. The Bank also considers the effect that the proposed investment would have on the Bank's risk-based capital requirements and interest rate risk sensitivity.

At June 30, 2008, the Bank's investment securities portfolio was $153.1 million, which primarily consisted of federal agency and government sponsored enterprise obligations. The Bank's investment securities portfolio was classified as available for sale.

The following table sets forth the composition of the Bank's investment portfolio at the dates indicated.

	At June 30,								
	2008			2007			2006		
	Amortized Cost	Estimated Fair Value	Percent	Amortized Cost	Estimated Fair Value	Percent	Amortized Cost	Estimated Fair Value	Percent
(Dollars In Thousands)									
Held to maturity securities:									
U.S. government sponsored enterprise debt securities	$ -	$ -	- %	$ 19,000	$ 18,836	12.50%	$ 51,028	$ 49,911	28.35%
U.S. government agency MBS (1)	-	-	-	1	1	-	3	3	-
Total held to	-	-	-	19,001	18,837	12.50	51,031	49,914	28.35

maturity									
Available for sale securities:									
U.S. government sponsored enterprise debt securities	5,250	5,111	3.34	9,849	9,683	6.43	21,846	21,264	12.08
U.S. government agency MBS	90,960	90,938	59.39	57,555	57,539	38.18	38,143	37,365	21.22
U.S. government sponsored enterprise MBS	53,847	54,254	35.44	58,861	59,066	39.20	61,455	61,249	34.79
Private issue CMO (2)	2,275	2,225	1.45	4,627	4,641	3.08	5,557	5,412	3.07
Freddie Mac common stock	6	98	0.06	6	364	0.24	6	342	0.19
Fannie Mae common stock	1	8	0.01	1	26	0.02	1	19	0.01
Other common stock	118	468	0.31	118	523	0.35	118	507	0.29
Total available for sale	152,457	153,102	100.00	131,017	131,842	87.50	127,126	126,158	71.65
Total investment securities	$ 152,457	$ 153,102	100.00%	$ 150,018	$ 150,679	100.00%	$ 178,157	$ 176,072	100.00%

(1) Mortgage-backed securities ("MBS")
(2) Collateralized mortgage obligations ("CMO")

As of June 30, 2008, the Corporation held investments in a continuous unrealized loss position totaling $473,000, consisting of the following:

(In Thousands)	Unrealized Holding Losses Less Than 12 Months		Unrealized Holding Losses 12 Months or More		Unrealized Holding Losses Total	
Description of Securities	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. government sponsored enterprise debt securities:						
Fannie Mae	$ 1,940	$ 60	$ -	$ -	$ 1,940	$ 60
FHLB	3,171	79	-	-	3,171	79
U.S. government agency MBS:						
GNMA	47,048	269	-	-	47,048	269
U.S. government sponsored enterprise MBS:						
Freddie Mac	8,770	15	-	-	8,770	15
Private issue CMO:						
Other institutions	1,836	49	389	1	2,225	50
Total	$ 62,765	$ 472	$ 389	$ 1	$ 63,154	$ 473

As of June 30, 2008, the unrealized holding losses relate to a total of 15 investment securities, which consist of 11 adjustable-rate MBS (primarily U.S. government agency MBS), two adjustable-rate private issue CMO and two fixed-rate government sponsored enterprise debt obligations, ranging from a de minimus percentage to 3.1% of cost. Of these unrealized losses in investment securities, only one has been in an unrealized position for more than 12 months. Such unrealized holding losses are the result of fluctuations in interest rates during fiscal 2008 and are not the result of credit or principal risk. Based on the nature of the investments, the Bank’s ability and intent to hold the investments until recovery, and other considerations discussed above, management concluded that such unrealized losses were not other than temporary as of June 30, 2008.

The following table sets forth the outstanding balance, maturity and weighted average yield of the investment securities at June 30, 2008:

	Due in One Year or Less		Due After One to Five Years		Due After Five to Ten Years		Due After Ten Years		No Stated Maturity		Total	
(Dollars in Thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale securities:												
U.S. government sponsored enterprise debt securities	$ -	- %	$ -	- %	$ 5,111	4.00%	$ -	- %	$ -	- %	$ 5,111	4.00%
U.S. government agency MBS	-	-	-	-	-	-	90,938	5.09%	-	-	90,938	5.09%
U.S. government sponsored enterprise MBS	-	-	-	-	-	-	54,254	5.38%	-	-	54,254	5.38%
Private issue CMO	-	-	-	-	-	-	2,225	4.77%	-	-	2,225	4.77%
Freddie Mac common stock	-	-	-	-	-	-	-	-	98	-	98	-
Fannie Mae common stock	-	-	-	-	-	-	-	-	8	-	8	-
Other common stock	-	-	-	-	-	-	-	-	468	-	468	-
Total available for sale	-	- %	-	- %	5,111	4.00%	147,417	5.19%	574	- %	153,102	5.13%
Total investment securities	$ -	- %	$ -	- %	$ 5,111	4.00%	$ 147,417	5.19%	$ 574	- %	$ 153,102	5.13%

Deposit Activities and Other Sources of Funds

General. Deposits, the proceeds from loan sales and loan repayments are the major sources of the Bank's funds for lending and other investment purposes. Scheduled loan repayments are a relatively stable source of funds, while deposit inflows and outflows are influenced significantly by general interest rates and money market conditions. Loan sales are also influenced significantly by general interest rates. Borrowings through the FHLB – San Francisco and repurchase agreements may be used to compensate for declines in the availability of funds from other sources.

Deposit Accounts. Substantially all of the Bank's depositors are residents of the State of California. Deposits are attracted from within the Bank's market area by offering a broad selection of deposit instruments, including checking, savings, money market and time deposits. Deposit account terms vary, differentiated by the minimum balance required, the time periods that the funds must remain on deposit and the interest rate, among other factors. In determining the terms of its deposit accounts, the Bank considers current interest rates, profitability to the Bank, interest rate risk characteristics, competition and its customer's preferences and concerns. Generally, the Bank's deposit rates are commensurate with the median rates of its competitors within a given market. The Bank may occasionally pay above-market interest rates to attract or retain deposits when less expensive sources of funds are not available. The Bank may also pay above-market interest rates in specific markets in order to increase the deposit base of a particular office or group of offices. Currently, the Bank does not accept brokered deposits. The Bank reviews its deposit composition and pricing on a weekly basis.

The Bank generally offers time deposits for terms not exceeding five years. As illustrated in the following table, time deposits represented 66% of the Bank's deposit portfolio at June 30, 2008, compared to 65% at June 30, 2007. At June 30, 2008, the Bank has a single depositor with an aggregate balance of $100.3 million in time deposits and the Bank does not know the likelihood of renewal by the depositor. The Bank attempts to reduce the overall cost of its deposit portfolio and to increase its franchise value by emphasizing transaction accounts which are subject to a heightened degree of competition (see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" beginning on page 50 of this Form 10-K).

The following table sets forth information concerning the Bank's weighted-average interest rate of deposits at June 30, 2008.

Weighted Average Interest Rate	Term	Deposit Account Type	Minimum Amount	Balance (In Thousands)	Percentage of Total Deposits
		Transaction accounts:			
0.00%	N/A	Checking accounts – non interest-bearing	$ -	$ 48,056	4.74%
0.63	N/A	Checking accounts – interest-bearing	-	122,065	12.05
1.61	N/A	Savings accounts	10	144,883	14.31
1.93	N/A	Money market accounts	-	33,675	3.33
		Time deposits:			
3.11	12 to 36 months	Fixed-term, variable rate	1,000	1,271	0.13
0.83	30 days or less	Fixed-term, fixed rate	1,000	23	-
2.02	31 to 90 days	Fixed-term, fixed rate	1,000	4,832	0.48

1.98	91 to 180 days	Fixed-term, fixed rate	1,000	125,904	12.44
3.95	181 to 365 days	Fixed-term, fixed rate	1,000	256,043	25.29
4.91	Over 1 to 2 years	Fixed-term, fixed rate	1,000	155,850	15.39
4.98	Over 2 to 3 years	Fixed-term, fixed rate	1,000	91,129	9.00
4.13	Over 3 to 5 years	Fixed-term, fixed rate	1,000	28,607	2.83
0.40	Over 5 years	Fixed-term, fixed rate	1,000	72	0.01
2.95%				$ 1,012,410	100.00%

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The following table indicates the aggregate dollar amount of the Bank's time deposits with balances of $100,000 or more differentiated by time remaining until maturity as of June 30, 2008.

Maturity Period (In Thousands)	Amount
Three months or less	$ 134,559
Over three to six months	86,389
Over six to twelve months	108,355
Over twelve months	33,960
Total	$ 363,263

Deposit Flows. The following table sets forth the balances (inclusive of interest credited) and changes in the dollar amount of deposits in the various types of accounts offered by the Bank at and between the dates indicated.

	At June 30, 2008			2007		
(Dollars in Thousands)	Amount	Percent of Total	Increase (Decrease)	Amount	Percent of Total	Increase (Decrease)
Checking accounts – non interest-bearing	$ 48,056	4.75%	$ 2,944	$ 45,112	4.51%	$ (5,379)
Checking accounts – interest-bearing	122,065	12.06	(523)	122,588	12.24	(8,677)
Savings accounts	144,883	14.31	(8,153)	153,036	15.28	(28,770)
Money market accounts	33,675	3.32	1,621	32,054	3.20	798
Time deposits:						
Fixed-term, fixed rate which mature:						
Within one year	589,027	58.18	155,735	433,292	43.27	128,533
Over one to two years	59,440	5.87	(103,125)	162,565	16.23	33,824
Over two to five years	13,935	1.38	(37,448)	51,383	5.13	(39,826)
Over five years	58	0.01	58	-	-	-
Fixed-term, variable rate	1,271	0.12	(96)	1,367	0.14	(385)
Total	$ 1,012,410	100.00%	$ 11,013	$ 1,001,397	100.00%	$ 80,118

Time Deposits by Rates. The following table sets forth the aggregate balance of time deposits categorized by interest rates at the dates indicated.

	At June 30, 2008	2007	2006
(In Thousands)			
Below 1.00%	$ 118	$ 49	$ 151
1.00 to 1.99%	51,088	-	384
2.00 to 2.99%	155,100	8,808	31,707
3.00 to 3.99%	88,723	81,052	175,831
4.00 to 4.99%	153,575	119,862	278,574
5.00 to 5.99%	215,127	438,836	39,814

Total	$ 663,731	$ 648,607	$ 526,461

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Time Deposits by Maturities. The following table sets forth the aggregate dollar amount of time deposits at June 30, 2008 differentiated by interest rates and maturity.

(In Thousands)	One Year or Less	Over One to Two Years	Over Two to Three Years	Over Three to Four Years	After Four Years	Total
Below 1.00%	$ 47	$ 10	$ -	$ 2	$ 59	$ 118
1.00 to 1.99%	51,088	-	-	-	-	51,088
2.00 to 2.99%	146,052	8,853	195	-	-	155,100
3.00 to 3.99%	72,173	6,487	6,047	885	3,131	88,723
4.00 to 4.99%	145,562	4,144	778	1,543	1,548	153,575
5.00 to 5.99%	174,462	40,665	-	-	-	215,127
Total	$ 589,384	$ 60,159	$ 7,020	$ 2,430	$ 4,738	$ 663,731

Deposit Activity. The following table sets forth the deposit activity of the Bank at and for the periods indicated.

	At or For the Year Ended June 30,		
(In Thousands)	2008	2007	2006
Beginning balance	$ 1,001,397	$ 921,279	$ 923,670
Net (withdrawals) deposits before interest credited	(23,563)	48,895	(24,522)
Interest credited	34,576	31,223	22,131
Net increase (decrease) in deposits	11,013	80,118	(2,391)
Ending balance	$ 1,012,410	$ 1,001,397	$ 921,279

Borrowings. The FHLB – San Francisco functions as a central reserve bank providing credit for member financial institutions. As a member, the Bank is required to own capital stock in the FHLB – San Francisco and is authorized to apply for advances using such stock and certain of its mortgage loans and other assets (principally investment securities) as collateral, provided certain creditworthiness standards have been met. Advances are made pursuant to several different credit programs. Each credit program has its own interest rate, maturity, terms and conditions. Depending on the program, limitations on the amount of advances are based on the financial condition of the member institution and the adequacy of collateral pledged to secure the credit. The Bank utilizes advances from the FHLB – San Francisco as an alternative to deposits to supplement its supply of lendable funds, to meet deposit withdrawal requirements and to help manage interest rate risk. The FHLB – San Francisco has, from time to time, served as the Bank's primary borrowing source. As of June 30, 2008, the FHLB – San Francisco borrowing capacity is limited to 50% of total assets. Advances from the FHLB – San Francisco are typically secured by the Bank's single-family residential mortgages, multi-family and commercial real estate loans. Total mortgage loans pledged to the FHLB – San Francisco were $899.3 million at June 30, 2008 as compared to $875.2 million at June 30, 2007. In

addition, the Bank pledged investment securities totaling $26.4 million at June 30, 2008 as compared to $24.9 million at June 30, 2007 to collateralize its FHLB – San Francisco advances under the Securities-Backed Credit ("SBC") facility. At June 30, 2008, the Bank had $479.3 million of borrowings from the FHLB – San Francisco with a weighted-average rate of 3.81%, $13.0 million was under the SBC facility. Such borrowings mature between 2008 and 2021 with a weighted maturity of 23 months. As of June 30, 2008 and 2007, the remaining borrowing facility was $352.7 million and $370.9 million, respectively, with remaining collateral of $439.9 million and $391.9 million, respectively.

In addition, the Bank has a borrowing arrangement in the form of a federal funds facility with its correspondent bank in the amount of $25.0 million. As of June 30, 2008 and 2007, the Bank had no outstanding correspondent bank advances.

The following table sets forth certain information regarding borrowings by the Bank at the dates and for the periods indicated:

	At or For the Year Ended June 30,		
(Dollars In Thousands)	2008	2007	2006
Balance outstanding at the end of period:			
FHLB – San Francisco advances	$ 479,335	$ 502,774	$ 546,211
Correspondent bank advances	$ -	$ -	$ -
Weighted average rate at the end of period:			
FHLB – San Francisco advances	3.81%	4.55%	4.53%
Correspondent bank advances	-	-	-
Maximum amount of borrowings outstanding at any month end:			
FHLB – San Francisco advances	$ 499,744	$ 689,443	$ 572,342
Correspondent bank advances	$ -	$ 1,000	$ -
Average short-term borrowings during the period (1) With respect to:			
FHLB – San Francisco advances	$ 188,390	$ 281,267	$ 121,950
Correspondent bank advances	$ 143	$ 168	$ 205
Weighted average short-term borrowing rate during the period (1) With respect to:			
FHLB – San Francisco advances	3.76%	4.89%	4.11%
Correspondent bank advances	5.36%	5.34%	3.46%

(1) Borrowings with a remaining term of 12 months or less.

As a member of the FHLB – San Francisco, the Bank is required to maintain a minimum investment in FHLB – San Francisco stock. The Bank held the required investment of $30.0 million and an excess investment of $2.1 million at June 30, 2008, as compared to the required investment of $32.2 million and an excess investment of $11.7 million at June 30, 2007. Any excess may be redeemed at par by the Bank or returned by FHLB – San Francisco.

Subsidiary Activities

Federal savings institutions generally may invest up to 3% of their assets in service corporations, provided that at least one-half of any amount in excess of 1% is used primarily for community, inner-city and community development projects. The Bank's investment in its service corporations did not exceed these limits at June 30, 2008.

The Bank has three wholly owned subsidiaries; Provident Financial Corp ("PFC"), Profed Mortgage, Inc., and First Service Corporation. PFC's current activities include: (i) acting as trustee for the Bank's real estate transactions and (ii) holding real estate for investment, if any. Profed Mortgage, Inc., which formerly conducted the Bank's mortgage banking activities, and First Service Corporation are currently inactive. At June 30, 2008, the Bank's investment in its

subsidiaries was $305,000.

REGULATION

The following is a brief description of certain laws and regulations which are applicable to the Corporation and the Bank. The description of these laws and regulations, as well as descriptions of laws and regulations contained elsewhere herein, does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.

Legislation is introduced from time to time in the United States Congress that may affect the Corporation's and the Bank's operations. In addition, the regulations governing the Corporation and the Bank may be amended from time to time by the OTS. Any such legislation or regulatory changes could adversely affect the Corporation and the Bank and no prediction can be made as to whether any such changes may occur.

General

The Bank, as a federally chartered savings institution, is subject to extensive regulation, examination and supervision by the OTS, as its primary federal regulator, and the FDIC, as its insurer of deposits. The Bank is a member of the FHLB System and its deposits are insured up to applicable limits by the FDIC. The Bank must file reports with the OTS and the FDIC concerning its activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with, or acquisitions of, other financial institutions. There are periodic examinations by the OTS to evaluate the Bank's safety and soundness and compliance with various regulatory requirements. Under certain circumstances, the FDIC may also examine the Bank. This regulatory structure is intended primarily for the protection of the insurance fund and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such policies, whether by the OTS, the FDIC or Congress, could have a material adverse impact on the Corporation and the Bank and their operations. The Corporation, as a savings and loan holding company, is required to file certain reports with, is subject to examination by, and otherwise must comply with the rules and regulations of the OTS. The Corporation is also subject to the rules and regulations of the Securities and Exchange Commission ("SEC") under the federal securities laws. See "Savings and Loan Holding Company Regulations" on page 36.

Federal Regulation of Savings Institutions

Office of Thrift Supervision. The OTS has extensive authority over the operations of savings institutions. As part of this authority, the Bank is required to file periodic reports with the OTS and is subject to periodic examinations by the OTS and the FDIC. The OTS also has extensive enforcement authority over all savings institutions and their holding companies, including the Bank and the Corporation. This enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease-and-desist or removal orders and initiate injunctive actions. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inaction may provide the basis for enforcement action, including misleading or untimely reports filed with the OTS. Except under certain circumstances, public disclosure of final enforcement actions by the OTS is required.

In addition, the investment, lending and branching authority of the Bank is prescribed by federal laws and it is prohibited from engaging in any activities not permitted by these laws. For example, no savings institution may invest in non-investment grade corporate debt securities. In addition, the permissible level of investment by federal institutions in loans secured by non-residential real property may not exceed 400% of total capital, except with the approval of the OTS. Federal savings institutions are also generally authorized to branch nationwide. The Bank is in compliance with the noted restrictions.

All savings institutions are required to pay assessments to the OTS to fund the agency's operations. The general assessments, paid on a semi-annual basis, are determined based on the savings institution's total assets, including consolidated subsidiaries. The Bank's annual OTS assessment for the fiscal year ended June 30, 2008 was $338,000.

Federal law provides that savings institutions are generally subject to the national bank limit on loans to one borrower. A savings institution may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of its unimpaired capital and surplus. An additional amount may be lent, equal to 10% of unimpaired capital and surplus, if secured by specified readily marketable collateral. At June 30, 2008, the Bank's limit on loans to one borrower was $19.5 million. At June 30, 2008, the Bank's single largest loan commitment to a single borrower was $8.5 million in the form of a condominium construction loan located in Southern California. As of June 30, 2008, this loan is classified as special mention since the primary source of loan repayment is the sale of the 65 condominiums, which has been delayed given the current real estate market conditions. The Bank also monitors multiple loans to a single borrower and/or guarantor. At June 30, 2008, one such borrower had a total of $7.5 million of loans outstanding, primarily commercial real estate loans, all of which are performing according to their original terms.

The OTS, as well as the other federal banking agencies, has adopted guidelines establishing safety and soundness standards on such matters as loan underwriting and documentation, asset quality, earnings, internal controls and audit systems, interest rate risk exposure and compensation and other employee benefits. Any institution that fails to comply with these standards must submit a compliance plan.

Federal Home Loan Bank System. The Bank is a member of the FHLB – San Francisco, which is one of 12 regional FHLBs that administer the home financing credit function of member financial institutions. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans or advances to members in accordance with policies and procedures, established by the Board of Directors of the FHLB, which are subject to the oversight of the Federal Housing Finance Board. All advances from the FHLB are required to be fully secured by sufficient collateral as determined by the FHLB. In addition, all long-term advances are required to provide funds for residential home financing. At June 30, 2008, the Bank had $479.3 million of outstanding advances from the FHLB – San Francisco under an available credit facility of $837.1 million, based on 50% of total assets, which is limited to available collateral. See "Business – Deposit Activities and Other Sources of Funds – Borrowings" on page 29.

As a member, the Bank is required to purchase and maintain stock in the FHLB – San Francisco. At June 30, 2008, the Bank had $32.1 million in FHLB – San Francisco stock, which was in compliance with this requirement. In past years, the Bank has received substantial dividends on its FHLB – San Francisco stock. The average dividend yield for fiscal 2008, 2007 and 2006 was 5.65%, 5.35% and 4.78%, respectively. There is no guarantee that the FHLB – San Francisco will maintain its dividend at these levels.

Under federal law, the FHLB is required to provide funds for the resolution of troubled savings institutions and to contribute to low and moderately priced housing programs through direct loans or interest subsidies on advances targeted for community investment and low and moderate income housing projects. These contributions have adversely affected the level of FHLB dividends paid and could continue to do so in the future. These contributions also could have an adverse effect on the value of FHLB stock in the future. A reduction in value of the Bank's FHLB stock may result in a corresponding reduction in the Bank's capital.

Insurance of Accounts and Regulation by the FDIC. The Bank's deposits are insured up to applicable limits by the DIF of the FDIC. The DIF is the successor to the Bank Insurance Fund and the Savings Association Insurance Fund, which were merged effective March 31, 2006. As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of and to require reporting by FDIC insured institutions. It also may prohibit any FDIC insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious risk to the insurance fund. The FDIC also has the authority to initiate enforcement actions against savings institutions, after giving the Office of Thrift Supervision an opportunity to take such action, and may terminate the deposit insurance if it determines that the institution has engaged in unsafe or unsound practices or is in an unsafe or unsound condition.

The FDIC amended its risk-based assessment system for 2007 to implement authority granted by the Federal Deposit Insurance Reform Act of 2005, which was enacted in 2006 ("Reform Act"). Under the revised system, insured institutions are assigned to one of four risk categories based on supervisory evaluations, regulatory capital levels and certain other factors. An institution's assessment rate depends upon the category to which it is assigned.

Risk Category I, which contains those depository institutions that pose the smallest risk, is expected to include more than 90% of all institutions. Unlike the other categories, Risk Category I contains further risk differentiation based on the FDIC's analysis of financial ratios, examination component ratings and other information. Assessment rates are determined by the FDIC and currently range from five to seven basis points for the healthiest institutions (Risk Category I) to 43 basis points of assessable deposits for those that pose the highest risk (Risk Category IV). The FDIC may adjust rates uniformly from one quarter to the next, except that no single adjustment can exceed three basis points. No institution may pay a dividend if in default of the FDIC assessment.

The Reform Act also provided for a one-time credit for eligible institutions based on their assessment base as of December 31, 1996. Subject to certain limitations with respect to institutions that are exhibiting weaknesses, credits can be used to offset assessments until exhausted. The Bank's one-time credit was $695,000 and was exhausted in the quarter ended March 31, 2008. The Reform Act also provided for the possibility that the FDIC may pay dividends to insured institutions once the DIF reserve ratio equals or exceeds 1.35% of estimated insured deposits.

In addition to the assessment for deposit insurance, institutions are required to make payments on bonds issued in the late 1980s by the Financing Corporation to recapitalize a predecessor deposit insurance fund. For the quarter ended March 31, 2008, which is the most recent information available, this payment was established at 1.12 basis points (annualized) of assessable deposits.

The Reform Act provided the FDIC with authority to adjust the DIF ratio to insured deposits within a range of 1.15% and 1.50%, in contrast to the prior statutorily fixed ratio of 1.25%. The ratio, which is viewed by the FDIC as the level that the fund should achieve, was established by the agency at 1.25% for 2008.

The FDIC has authority to increase insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Bank. There can be no prediction as to what insurance assessment rates will be in the future. Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the Office of Thrift Supervision. Management of the Bank is not aware of any practice, condition or violation that might lead to termination of the Bank's deposit insurance.

Prompt Corrective Action. The OTS is required to take certain supervisory actions against undercapitalized savings institutions, the severity of which depends upon the institution's degree of undercapitalization. Generally, an institution is considered to be "undercapitalized" if it has a core capital ratio of less than 4.0% (3.0% or less for institutions with the highest examination rating), a ratio of total capital to risk-weighted assets of less than 8.0%, or a ratio of Tier 1 capital to risk-weighted assets of less than 4.0%. An institution that has a core capital ratio that is less than 3.0%, a total risk-based capital ratio less than 6.0%, and a Tier 1 risk-based capital ratio of less than 3.0% is considered to be "significantly undercapitalized" and an institution that has a tangible capital ratio equal to or less than 2.0% is deemed to be "critically undercapitalized." Subject to a narrow exception, the OTS is required to appoint a receiver or conservator for a savings institution that is "critically undercapitalized." OTS regulations also require that a capital restoration plan be filed with the OTS within 45 days of the date a savings institution receives notice that it is "undercapitalized," "significantly undercapitalized" or "critically undercapitalized." In addition, numerous mandatory supervisory actions become immediately applicable to an undercapitalized institution, including, but not limited to, increased monitoring by regulators and restrictions on growth, capital distributions and expansion. "Significantly undercapitalized" and "critically undercapitalized" institutions are subject to more extensive mandatory regulatory actions. The OTS also could take any one of a number of discretionary supervisory actions, including the issuance of a capital directive and the replacement of senior executive officers and directors.

At June 30, 2008, the Bank was categorized as "well capitalized" under the prompt corrective action regulations of the OTS.

Qualified Thrift Lender Test. All savings institutions, including the Bank, are required to meet a qualified thrift lender ("QTL") test to avoid certain restrictions on their operations. This test requires a savings institution to have at least 65% of its total assets as defined by regulation, in qualified thrift investments on a monthly average for nine out of every 12 months on a rolling basis. As an alternative, the savings institution may maintain 60% of its assets in those assets specified in Section 7701(a)(19) of the Internal Revenue Code ("Code"). Under either test, such assets primarily consist of residential housing related loans and investments.

A savings institution that fails to meet the QTL is subject to certain operating restrictions and may be required to convert to a national bank charter. Recent legislation has expanded the extent to which education loans, credit card loans and small business loans may be considered "qualified thrift investments." As of June 30, 2008, the Bank maintained 83.65% of its portfolio assets in qualified thrift investments and, therefore, met the qualified thrift lender test.

Capital Requirements. The OTS's capital regulations require federal savings institutions to meet three minimum capital standards: a 1.5% tangible capital ratio, a 4% core capital ratio (3% for institutions receiving the highest rating on the CAMELS examination rating system) and an 8% risk-based capital ratio. In addition, the prompt corrective action standards discussed above also establish, in effect, a minimum ratio of 2% tangible capital, 4% core capital (3% for institutions receiving the highest rating on the CAMELS system), 8% risk-based capital, and 4% Tier 1 risk-based capital. The OTS regulations also require that, in meeting the tangible, core and risk-based capital ratios, institutions must generally deduct investments in and loans to subsidiaries engaged in activities as principal that are not permissible for a national bank.

The risk-based capital standard requires federal savings institutions to maintain Tier 1 and total capital (which is defined as core capital and supplementary capital) to risk-weighted assets of at least 4% and 8%, respectively. In determining the amount of risk-weighted assets, all assets, including certain off-balance sheet assets, recourse obligations, residual interests and direct credit substitutes, are multiplied by a risk-weight factor of 0% to 100%, assigned by the OTS capital regulation based on the risks believed inherent in the type of asset. Core capital is defined as common stockholders' equity (including retained earnings), certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries, less intangibles other than certain mortgage servicing rights and credit card relationships. The components of supplementary capital currently include cumulative preferred stock, long-term perpetual preferred stock, mandatory convertible securities, subordinated debt and intermediate preferred stock, the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and up to 45% of unrealized gains on available-for-sale equity securities with readily determinable fair market values. Overall, the amount of supplementary capital included as part of total capital cannot exceed 100% of core capital.

The OTS also has authority to establish individual minimum capital requirements in appropriate cases upon a determination that an institution's capital level is or may become inadequate in light of the particular circumstances. At June 30, 2008, the Bank met each of these capital requirements. For additional information, including the capital levels of the Bank, see Note 10 of the Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K.

Limitations on Capital Distributions. OTS regulations impose various restrictions on savings institutions with respect to their ability to make distributions of capital, which include dividends, stock redemptions or repurchases, cash-out mergers and other transactions charged to the capital account. Generally, savings institutions, such as the Bank, that before and after the proposed distribution are well-capitalized, may make capital distributions during any calendar year up to 100% of net income for the year-to-date plus retained net income for the two preceding years. However, an institution deemed to be in need of more than normal supervision by the OTS may have its dividend authority restricted by the OTS. The Bank may pay dividends to the Corporation in accordance with this general authority.

Savings institutions proposing to make any capital distribution need not submit written notice to the OTS prior to such distribution unless they are a subsidiary of a holding company or would not remain well-capitalized following the distribution. Savings institutions that do not, or would not meet their current minimum capital requirements following a proposed capital distribution or propose to exceed these net income limitations, must obtain OTS approval prior to making such distribution. The OTS may object to the distribution during that 30-day period based on safety and soundness concerns.

Activities of Associations and Their Subsidiaries. When a savings institution establishes or acquires a subsidiary or elects to conduct any new activity through a subsidiary that the association controls, the savings institution must notify the FDIC and the OTS 30 days in advance and provide the information each agency may, by regulation, require. Savings institutions also must conduct the activities of subsidiaries in accordance with existing regulations

and orders.

The OTS may determine that the continuation by a savings institution of its ownership, control of, or its relationship to, the subsidiary constitutes a serious risk to the safety, soundness or stability of the savings institution or is inconsistent with sound banking practices or with the purposes of the Federal Deposit Insurance Act. Based upon that determination, the FDIC or the OTS has the authority to order the savings institution to divest itself of control of the subsidiary. The FDIC also may determine by regulation or order that any specific activity poses a serious threat to the DIF. If so, it may require that no DIF member engage in that activity directly.

Transactions with Affiliates. The Bank's authority to engage in transactions with "affiliates" is limited by OTS regulations and by Sections 23A and 23B of the Federal Reserve Act as implemented by the Federal Reserve Board's Regulation W. The term "affiliates" for these purposes generally means any company that controls or is under common control with an institution. The Corporation and its non-savings institution subsidiaries would be affiliates of the Bank. In general, transactions with affiliates must be on terms that are as favorable to the institution as comparable transactions with non-affiliates. In addition, certain types of transactions are restricted to an aggregate percentage of the institution's capital. Collateral in specified amounts must be provided by affiliates in order to receive loans from an institution. In addition, savings institutions are prohibited from lending to any affiliate that is engaged in activities that are not permissible for bank holding companies and no savings institution may purchase the securities of any affiliate other than a subsidiary. Federally insured savings institutions are subject, with certain exceptions, to certain restrictions on extensions of credit to their parent holding companies or other affiliates, on investments in the stock or other securities of affiliates and on the taking of such stock or securities as collateral from any borrower. In addition, these institutions are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit or the providing of any property or service.

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act") generally prohibits a company from making loans to its executive officers and directors. However, that act contains a specific exception for loans by a depository institution to its executive officers and directors in compliance with federal banking laws. Under such laws, the Bank's authority to extend credit to executive officers, directors and 10% stockholders ("insiders"), as well as entities which such persons control, is limited. The law restricts both the individual and aggregate amount of loans the Bank may make to insiders based, in part, on the Bank's capital position and requires certain Board approval procedures to be followed. Such loans must be made on terms substantially the same as those offered to unaffiliated individuals and not involve more than the normal risk of repayment. There is an exception for loans made pursuant to a benefit or compensation program that is widely available to all employees of the institution and does not give preference to insiders over other employees. There are additional restrictions applicable to loans to executive officers.

Community Reinvestment Act. Under the Community Reinvestment Act, every FDIC-insured institution has a continuing and affirmative obligation consistent with safe and sound banking practices to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The Community Reinvestment Act does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the Community Reinvestment Act. The Community Reinvestment Act requires the OTS, in connection with the examination of the Bank, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications, such as a merger or the establishment of a branch, by the Bank. The OTS may use an unsatisfactory rating as the basis for the denial of an application. Due to the heightened attention being given to the Community Reinvestment Act in the past few years, the Bank may be required to devote additional funds for investment and lending in its local community. The Bank was examined for Community Reinvestment Act compliance and received a rating of satisfactory in its latest examination.

Regulatory and Criminal Enforcement Provisions. The OTS has primary enforcement responsibility over savings institutions and has the authority to bring action against all "institution-affiliated parties," including stockholders,

attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an insured institution. Formal enforcement action may range from the issuance of a capital directive or cease and desist order to removal of officers or directors, receivership, conservatorship or termination of deposit insurance. Civil penalties cover a wide range of violations and can amount to $25,000 per day, or $1.1 million per day in especially egregious cases. The FDIC has the authority to recommend to the Director

of the OTS that an enforcement action be taken with respect to a particular savings institution. If the Director does not take action, the FDIC has authority to take such action under certain circumstances. Federal law also establishes criminal penalties for certain violations.

Environmental Issues Associated with Real Estate Lending. The Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), a federal statute, generally imposes strict liability on all prior and present "owners and operators" of sites containing hazardous waste. However, Congress acted to protect secured creditors by providing that the term "owner and operator" excludes a person whose ownership is limited to protecting its security interest in the site. Since the enactment of the CERCLA, this "secured creditor exemption" has been the subject of judicial interpretations which have left open the possibility that lenders could be liable for cleanup costs on contaminated property that they hold as collateral for a loan.

To the extent that legal uncertainty exists in this area, all creditors, including the Bank, that have made loans secured by properties with potential hazardous waste contamination (such as petroleum contamination) could be subject to liability for cleanup costs, which costs often substantially exceed the value of the collateral property.

Privacy Standards. The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 ("GLBA"), which was enacted in 1999, modernized the financial services industry by establishing a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms and other financial service providers. The Bank is subject to OTS regulations implementing the privacy protection provisions of the GLBA. These regulations require the Bank to disclose its privacy policy, including identifying with whom it shares "non-public personal information," to customers at the time of establishing the customer relationship and annually thereafter.

Anti-Money Laundering and Customer Identification. Congress enacted the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the "USA Patriot Act") on October 26, 2001 in response to the terrorist events of September 11, 2001. The USA Patriot Act gives the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing, and broadened anti-money laundering requirements. In March 2006, Congress re-enacted certain expiring provisions of the USA Patriot Act.

Savings and Loan Holding Company Regulations

General. The Corporation is a unitary savings and loan holding company subject to the regulatory oversight of the OTS. Accordingly, the Corporation is required to register and file reports with the OTS and is subject to regulation and examination by the OTS. In addition, the OTS has enforcement authority over the Corporation and its non-savings institution subsidiaries, which also permits the OTS to restrict or prohibit activities that are determined to present a serious risk to the subsidiary savings institution.

Activities Restrictions. The GLBA provides that no company may acquire control of a savings association after May 4, 1999 unless it engages only in the financial activities permitted for financial holding companies under the law or for multiple savings and loan holding companies as described below. The GLBA also specifies, subject to a grandfather provision, that existing savings and loan holding companies may only engage in such activities. The Corporation qualifies for the grandfathering and is therefore not restricted in terms of its activities. Upon any non-supervisory acquisition by the company of another savings association as a separate subsidiary, the Corporation would become a multiple savings and loan holding company and would be limited to those activities permitted multiple savings and loan holding companies by OTS regulation. OTS has issued an interpretation concluding that multiple savings and loan holding companies may also engage in activities permitted for financial holding companies, including lending, trust services, insurance activities and underwriting, investment banking and real estate investments.

If the Bank fails the OTL test, the Corporation must, within one year of that failure, register as, and will become subject to the restrictions applicable to bank holding companies. See "Federal Regulation of Savings Institutions – Qualified Thrift Lender Test" on page 33 of this Form 10-K.

Mergers and Acquisitions. The Corporation must obtain approval from the OTS before acquiring more than 5% of the voting stock of another savings institution or savings and loan holding company or acquiring such an institution or holding company by merger, consolidation or purchase of its assets. In evaluating an application for the Company to acquire control of a savings institution, the OTS would consider the financial and managerial resources and future prospectus of the Corporation and the target institution, the effect of the acquisition on the risk to the Deposit Insurance Fund, the convenience and the needs of the community and competitive factors.

The OTS may not approve any acquisition that would result in a multiple savings and loan holding company controlling savings institutions in more than one state, subject to two exceptions; (i) the approval of interstate supervisory acquisitions by savings and loan holding companies and (ii) the acquisition of a savings institution in another state if the laws of the states of the target savings institution specifically permit such acquisitions. The states vary in the extent to which they permit interstate savings and loan holding company acquisitions.

Sarbanes-Oxley Act. The Sarbanes-Oxley Act was signed into law on July 30, 2002 in response to public concerns regarding corporate accountability in connection with certain accounting scandals. The stated goals of the Sarbanes-Oxley Act are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. The Sarbanes-Oxley Act generally applies to all companies that file or are required to file periodic reports with the SEC, under the Securities Exchange Act of 1934, including the Corporation.

The Sarbanes-Oxley Act includes very specific additional disclosure requirements and new corporate governance rules, requires the SEC and securities exchanges to adopt extensive additional disclosures, corporate governance and related rules and mandates. The Sarbanes-Oxley Act represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

TAXATION

Federal Taxation

General. The Corporation and the Bank report their income on a fiscal year basis using the accrual method of accounting and will be subject to federal income taxation in the same manner as other corporations with some exceptions, including particularly the Bank’s reserve for bad debts discussed below. The following discussion of tax matters is intended only as a summary and does not purport to be a comprehensive description of the tax rules applicable to the Bank or the Corporation.

Tax Bad Debt Reserves. As a result of legislation enacted in 1996, the reserve method of accounting for bad debt reserves was repealed for tax years beginning after December 31, 1995. Due to such repeal, the Bank is no longer able to calculate its deduction for bad debts using the percentage-of-taxable-income or the experience method. Instead, the Bank will be permitted to deduct as bad debt expense its specific charge-offs during the taxable year. In addition, the legislation required savings institutions to recapture into taxable income, over a six-year period, their post 1987 additions to their bad debt tax reserves. As of the effective date of the legislation, the Bank had no post 1987 additions to its bad debt tax reserves. As of June 30, 2008, the Bank’s total pre-1988 bad debt reserve for tax purposes was approximately $9.0 million. Under current law, a savings institution will not be required to recapture its pre-1988 bad debt reserve unless the Bank makes a “non-dividend distribution” as defined below.

Distributions. To the extent that the Bank makes “non-dividend distributions” to the Corporation that are considered as made from the reserve for losses on qualifying real property loans, to the extent the reserve for such losses exceeds the

amount that would have been allowed under the experience method; or from the supplemental reserve for losses on loans ("Excess Distributions"), then an amount based on the amount distributed will be included in the Bank's taxable income. Non-dividend distributions include distributions in excess of the Bank's current and accumulated earnings and profits, distributions in redemption of stock, and distributions in partial or complete liquidation. However, dividends paid out of the Bank's current or accumulated earnings and profits, as

calculated for federal income tax purposes, will not be considered to result in a distribution from the Bank's bad debt reserve. Thus, any dividends to the Corporation that would reduce amounts appropriated to the Bank's bad debt reserve and deducted for federal income tax purposes would create a tax liability for the Bank. The amount of additional taxable income attributable to an Excess Distribution is an amount that, when reduced by the tax attributable to the income, is equal to the amount of the distribution. Thus, if the Bank makes a "non-dividend distribution," then approximately one and one-half times the amount distributed will be included in taxable income for federal income tax purposes, assuming a 35% corporate income tax rate (exclusive of state and local taxes). See "Limitation on Capital Distributions" on page 34 of this Form 10-K for limits on the payment of dividends by the Bank. The Bank does not intend to pay dividends that would result in a recapture of any portion of its tax bad debt reserve. During fiscal 2008, the Bank declared and paid cash dividends to the Corporation of $12.0 million while the Corporation declared and paid cash dividends to the shareholders of $4.0 million.

Corporate Alternative Minimum Tax. The Internal Revenue Code of 1986 imposes a tax on alternative minimum taxable income ("AMTI") at a rate of 20%. In addition, only 90% of AMTI can be offset by net operating loss carryovers. AMTI is increased by an amount equal to 75% of the amount by which the Bank's adjusted current earnings exceeds its AMTI (determined without regard to this preference and prior to reduction for net operating losses).

Non-Qualified Compensation Tax Benefits. During fiscal 2008, 750 shares of common stock under the Management Recognition Plan ("MRP") were distributed to non-employee members of the Corporation's Board of Directors in accordance with previous awards and consistent with the vesting schedule. There were no options to purchase shares of the Corporation's common stock exercised as non-qualified stock options during fiscal 2008. A $4,000 federal tax benefit from the non-qualified compensation was realized in fiscal 2008.

Other Matters. The Internal Revenue Service has audited the Bank's income tax returns through 1996 and the California Franchise Tax Board has audited the Bank through 1990. The Corporation is currently undergoing a regular review by the Internal Revenue Service for fiscal 2006 and 2007, and as part of that review, a tax adjustment of $348,000 was recorded in fiscal 2008 tax expense for a disallowed tax deduction related to the sale of the commercial building sold in 2006. Management has not been made aware of any other significant issues at this time.

State Taxation

California. The California franchise tax rate applicable to the Bank equals the franchise tax rate applicable to corporations generally, plus an "in lieu" rate of 2%, which is approximately equal to personal property taxes and business license taxes paid by such corporations (but not generally paid by banks or financial corporations such as the Bank). At June 30, 2008, the Corporation's net state tax rate was 7.9%. Bad debt deductions are available in computing California franchise taxes using the specific charge-off method. The Bank and its California subsidiaries file California franchise tax returns on a combined basis. The Corporation will be treated as a general corporation subject to the general corporate tax rate. A $2,000 state tax benefit from the non-qualified compensation was realized in fiscal 2008, as described under the Federal Taxation section.

Delaware. As a Delaware holding company not earning income in Delaware, the Corporation is exempted from Delaware corporate income tax, but is required to file an annual report with and pay an annual franchise tax to the State of Delaware. The Corporation paid the annual franchise tax of $107,000 in fiscal 2008.

EXECUTIVE OFFICERS

The following table sets forth information with respect to the executive officers of the Corporation and the Bank.

		Position	
Name	Age (1)	Corporation	Bank
Craig G. Blunden	60	Chairman, President and Chief Executive Officer	Chairman, President and Chief Executive Officer
Richard L. Gale	57	-	Senior Vice President Provident Bank Mortgage
Kathryn R. Gonzales	50	-	Senior Vice President Retail Banking
Lilian Salter	53	-	Senior Vice President Chief Information Officer
Donavon P. Ternes	48	Chief Operating Officer Chief Financial Officer Corporate Secretary	Executive Vice President Chief Operating Officer Chief Financial Officer Corporate Secretary
David S. Weiant	49	-	Senior Vice President Chief Lending Officer

(1) As of June 30, 2008.

Biographical Information

Set forth below is certain information regarding the executive officers of the Corporation and the Bank. There are no family relationships among or between the executive officers.

Craig G. Blunden has been associated with the Bank since 1974 and has held his current positions at the Bank since 1991 and as President and Chief Executive Officer of the Corporation since its formation in 1996. Mr. Blunden also serves on the City of Riverside Council of Economic Development Advisors and is Immediate Past Chairman of the Board of the Greater Riverside Chamber of Commerce.

Richard L. Gale, who joined the Bank in 1988, has served as President of the Provident Bank Mortgage division since 1989. Mr. Gale has held his current position with the Bank since 1993.

Kathryn R. Gonzales joined the Bank as Senior Vice President of Retail Banking on August 7, 2006. Prior to joining the Bank, Ms. Gonzales was with Bank of America where she was responsible for working with under-performing branches and re-energizing their business development capabilities. Prior to that she was with Arrowhead Central Credit Union where she was responsible for 25 retail branches and oversaw their significant deposit growth. Her experience includes retail branch sales development, branch operations, development of business related products and services, and commercial lending.

Lilian Salter, who joined the Bank in 1993, was general auditor prior to being promoted to Chief Information Officer in 1997. Prior to joining the Bank, Ms. Salter was with Home Federal Bank, San Diego, California for 17 years and held various positions in information systems, auditing and accounting.

Donavon P. Ternes joined the Bank as Senior Vice President and Chief Financial Officer on November 1, 2000 and was appointed Secretary of the Corporation and the Bank in April 2003. Effective January 1, 2008, Mr. Ternes was appointed Executive Vice President and Chief Operating Officer, while continuing to serve as the Chief Financial

Officer and Corporate Secretary of the Bank and the Corporation. Prior to joining the Bank, Mr. Ternes was the President, Chief Executive Officer, Chief Financial Officer and Director of Mission Savings and Loan Association, located in Riverside, California holding those positions for over 11 years.

David S. Weiant joined the Bank as Senior Vice President and Chief Lending Officer on June 29, 2007. Prior to joining the Bank, Mr. Weiant was a Senior Vice President of Professional Business Bank (June 2006 to June 2007) where he was responsible for commercial lending in the Los Angeles and Inland Empire regions of Southern California. Prior to that, Mr. Weiant was Executive Vice President and Regional Manager of Southwest Community Bank (April 2005 to June 2006), Senior Vice President and Regional Manager of Vineyard Bank (2004 – 2005) and Executive Vice President and Branch Administrator of Business Bank of California (2000 – 2004). Mr. Weiant has more than 25 years of experience with financial institutions including the last 11 years in senior management.

Item 1A. Risk Factors

We assume and manage a certain degree of risk in order to conduct our business. In addition to the risk factors described below, other risks and uncertainties not specifically mentioned, or that are currently known to, or deemed by, management to be immaterial also may materially and adversely affect our financial position, results of operation and/or cash flows. Before making an investment decision, you should carefully consider the risks described below together with all of the other information included in this Form 10-K. If any of the circumstances described in the following risk factors actually occur to a significant degree, the value of our common stock could decline, and you could lose all or part of your investment.

Our business is subject to general economic risks that could adversely impact our results of operations and financial condition.

a) Changes in economic conditions, particularly a further economic slowdown in Southern California and Inland Empire could hurt our business.

Our business is directly affected by market conditions, trends in industry and finance, legislative and regulatory changes, and changes in governmental monetary and fiscal policies and inflation, all of which are beyond our control. In 2007, the housing and real estate sectors experienced an economic slowdown that has continued into 2008. Further deterioration in economic conditions and real estate markets, in particular within our primary market area in Southern California, could result in the following consequences, among others, any of which could hurt our business materially:

- loan delinquencies may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decline; and
- collateral for loans made by us, especially real estate, may decline in value, in turn reducing a customer's borrowing capacity and reducing the value of assets and collateral securing our loans.

b) Downturns in the real estate markets in our primary market area could hurt our business.

Our business activities and credit exposure are primarily concentrated in Southern California and the Inland Empire in particular. Our construction and land loan portfolios, our commercial and multi-family loan portfolios and a certain number of our other loans have been affected by the downturn in the residential real estate market. We anticipate that further declines in the real estate markets in our primary market area will hurt our business. As of June 30, 2008, substantially all of our loan portfolio consisted of loans secured by real estate located in Southern California. If real estate values continue to decline the collateral for our loans will provide less security. As a result, our ability to recover on defaulted loans by selling the underlying real estate will be diminished, and we would be more likely to

suffer losses on defaulted loans. The events and conditions described in this risk factor could therefore have a material adverse effect on our business, results of operations and financial condition.

c) We may suffer losses in our loan portfolio despite our underwriting practices.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Although we believe that our underwriting criteria are appropriate for the various kinds of loans we make, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for loan losses.

Our loan portfolio is concentrated in loans with a higher risk of loss.

We originate construction and land loans, commercial real estate and multi-family mortgage loans, commercial business loans, consumer loans, and single-family loans primarily within our market areas. Generally, these types of loans, other than the single-family loans, have a higher risk of loss. We had approximately $573.9 million outstanding in these types of higher risk loans at June 30, 2008, an increase of $41.2 million, or 8%, from $532.7 million at June 30, 2007. These loans have greater credit risk than single-family loans for a number of reasons, including those described below:

Construction and Land loans. This type of lending contains the inherent difficulty in estimating both a property's value at completion of the project and the estimated cost (including interest) of the project. If the estimate of construction costs proves to be inaccurate, we may be required to advance funds beyond the amount originally committed to permit completion of the project. If the estimate of value upon completion proves to be inaccurate, we may be confronted at, or prior to, the maturity of the loan with a project where the value is insufficient to assure full repayment. In addition, speculative construction loans to a builder are often associated with homes that are not pre-sold, and thus pose a greater potential risk than construction loans to individuals on their personal residences. Loans on land under development or held for future construction also poses additional risk because of the lack of income being produced by the property and the potential illiquid nature of the collateral. These risks can be significantly impacted by supply and demand conditions. As a result, this type of lending often involves the disbursement of substantial funds with repayment dependent on the success of the ultimate project and the ability of the borrower to sell or lease the property, rather than the ability of the borrower or guarantor themselves to repay principal and interest. At June 30, 2008, we had $36.6 million or 2.6% of total loans in construction (gross of undisbursed loan funds) and land loans.

Commercial Real Estate and Multi-Family loans. These loans typically involve higher principal amounts than other types of loans, and repayment is dependent upon income generated, or expected to be generated, by the property securing the loan in amounts sufficient to cover operating expenses and debt service, which may be adversely affected by changes in the economy or local market conditions. Commercial real estate and multi-family mortgage loans also expose a lender to greater credit risk than loans secured by residential real estate because the collateral securing these loans typically cannot be sold as easily as residential real estate. In addition, many of our commercial real estate and multi-family loans are not fully amortizing and contain large balloon payments upon maturity. Such balloon payments may require the borrower to either sell or refinance the underlying property in order to make the payment, which may increase the risk of default or non-payment. At June 30, 2008, we had $535.9 million or 38.5% of loans held for investment in commercial real estate and multi-family mortgage loans.

Commercial Business loans. Our commercial business loans are primarily made based on the cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. The borrowers' cash flow may be unpredictable, and collateral securing these loans may fluctuate in value. Most often, this collateral is accounts receivable, inventory, equipment or real estate. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. Other collateral securing loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. At June 30, 2008, we had $8.6 million or 0.6% of total in commercial business loans.

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We are also subject to credit risks in connection with our single-family lending practices.

We are subject to credit risk in connection with our loans held for investment, loans available for sale, receivable from sale of loans, investment securities and in connection with mortgage banking activities, particularly in the sale of loans (counter-party risk).

A substantial majority of our single-family mortgage loans held for investment are adjustable rate loans. Any rise in prevailing market interest rates may result in increased payments for borrowers who have adjustable rate mortgage loans, increasing the possibility of default. Multi-family and commercial real estate loans bear higher credit risk as compared to single-family mortgage loans. These loans are typically secured by properties that are generally greater in amount, more difficult to evaluate and monitor and are susceptible to default as a result of changes in general economic conditions and, therefore, involve a greater degree of risk than single-family mortgage loans. Since payments on loans secured by multi-family and commercial real estate are often dependent on the successful operation and management of the properties, repayment of such loans may be impacted by adverse conditions in the real estate market or the economy. As with single-family mortgage loans, a substantial majority of our multi-family and commercial real estate loans are adjustable rate, and thus are subject to higher payments by the borrower when prevailing market interest rates rise. Our single-family, multi-family and commercial real estate loans are primarily located in Los Angeles, Orange, Riverside, San Bernardino and San Diego Counties.

Recent negative developments in the financial industry and credit markets may continue to adversely impact our financial condition and results of operations.

Negative developments beginning in the latter half of 2007 in the sub-prime mortgage market and the securitization markets for such loans, together with substantially increased oil prices, other commodity prices and other factors, have resulted in uncertainty in the financial markets in general and a related general economic downturn, which have continued in 2008. Many lending institutions, including us, have experienced substantial declines in the performance of their loans, including construction and land loans, single-family loans, multi-family loans, commercial loans and consumer loans. Moreover, competition among depository institutions for deposits and quality loans has increased significantly. In addition, the values of real estate collateral supporting many construction and land, commercial and multi-family and other commercial loans and home mortgages have declined and may continue to decline. Bank and holding company stock prices have been negatively affected, as has the ability of banks and holding companies to raise capital or borrow in the debt markets compared to recent years. These conditions may have a material adverse effect on our financial condition and results of operations. In addition, as a result of the foregoing factors, there is a potential for new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations, including the expected issuance of formal enforcement orders. Negative developments in the financial industry and the impact of new legislation in response to those developments could restrict our business operations, including our ability to originate or sell loans, and adversely impact our results of operations and financial condition.

We may be required to make further increases in our provision for loan losses and to charge off additional loans in the future, which could adversely affect our results of operations.

For the fiscal year June 30, 2008 we recorded a provision for loan losses of $12.1 million compared to $5.1 million for the fiscal year June 30, 2007, which reduced our results of operations for fiscal 2008. We also recorded net loan charge-offs of $8.1 million for the fiscal year ended June 30, 2008 compared to $540,000 for the fiscal year ended June 30, 2007. We are experiencing increasing loan delinquencies and credit losses. Generally, our non-performing loans and assets reflect financial difficulties of individual borrowers resulting from weakness in the Southern California economy. In addition, slowing sales have been a contributing factor to the increase in non-performing loans as well as the increase in delinquencies. At June 30, 2008 our total non-performing loans had increased to $23.2 million compared to $15.9 million at June 30, 2007. In that regard, our portfolio is concentrated in

multi-family and commercial real estate loans and to a lesser degree in construction, commercial business and land loans, all of which are generally perceived to have a higher risk of loss than residential mortgage loans. While construction (gross of undisbursed loan funds) and land loans represented 2.6% of our total loans held for investment at June 30, 2008 they represented 22.8% of our non-performing loans at that date.

Our non-traditional single-family loans include interest-only loans, negative amortization and more than 30-year amortization loans, stated-income loans, low FICO score loans, and may bear higher credit risk. As of June 30, 2008, these loans totaled $707.6 million, comprising 88% of total single-family mortgage loans held for investment and 52% of total loans held for investment. In the case of interest-only loans a borrower's monthly payment is subject to change in the future when the loan converts to a fully-amortizing status. Since the borrower’s monthly payment may increase by a substantial amount even without an increase in prevailing market interest rates, there is no assurance that the borrower will be able to afford the increased monthly payment. In the case of stated income loans a borrower may misrepresent his income or source of income (which we have not verified) in order to obtain the loan. The borrower may not have sufficient income to qualify for the loan amount and may not be able to make the monthly loan payment. In the case of more than 30-year amortization loans the term of the loan requires many more monthly payments from the borrower (ultimately increasing the cost of the home) and subjects the loan to more interest rate cycles, economic cycles and employment cycles which increases the possibility that the borrower is negatively impacted by one of these cycles and is no longer willing or able to meet his monthly payment obligations. We have recently seen a rise in delinquencies in our non-traditional loans held for investment. As of June 30, 2008, 2.24% of such loans, totaling $15.9 million, were in non-accrual status, compared to 1.64% of such loans, totaling $12.0 million, in non-accrual status as of June 30, 2007.

If current trends in the housing and real estate markets continue, we expect that we will continue to experience increased delinquencies and credit losses. Moreover, if a recession occurs we expect that it would negatively impact economic conditions in our market areas and that we could experience significantly higher delinquencies and credit losses. An increase in our credit losses or our provision for loan losses would adversely affect our financial condition and results of operations.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a substantial negative effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities or with terms that are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry in light of the recent turmoil faced by banking organizations and the continued deterioration in credit markets.

We rely on customer deposits, advances from the FHLB – San Francisco and other borrowings to fund our operations. Although we have historically been able to replace maturing deposits and advances if desired, no assurance can be given that we would be able to replace such funds in the future if our financial condition or the financial condition of the FHLB – San Francisco or market conditions were to change. Our financial flexibility will be severely constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. Finally, if we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our profitability would be adversely affected.

Although we consider such sources of funds adequate for our liquidity needs, we may seek additional debt in the future to achieve our long-term business objectives. There can be no assurance additional borrowings, if sought, would be available to us or, if available, would be on favorable terms. If additional financing sources are unavailable or are not available on reasonable terms, our growth and future prospects could be adversely affected.

Fluctuations in interest rates could reduce our profitability and affect the value of our assets.

Like other financial institutions, we are subject to interest rate risk. Our primary source of income is net interest income, which is the difference between interest earned on loans and investment securities and the interest paid on interest-bearing deposits and borrowings. We expect that we will periodically experience imbalances in the interest rate sensitivities of our assets and liabilities and the relationships of various interest rates to each other. Over any

period of time, our interest-earning assets may be more sensitive to changes in market interest rates than our interest-bearing liabilities, or vice versa. In addition, the individual market interest rates underlying our loan and deposit products may not change to the same degree over a given time period. In any event, if market interest rates should move contrary to our position, our earnings may be negatively affected. In addition, loan volume and quality and deposit volume and mix can be affected by market interest rates. Changes in levels of market interest rates could materially adversely affect our net interest margin, asset quality, origination volume and overall profitability.

We manage our assets and liabilities in order to achieve long-term profitability while limiting our exposure to the fluctuation of interest rates. We anticipate periodic imbalances in the interest rate sensitivity of our assets and liabilities and the relationship of various interest rates to each other. At any reporting period, we may have earning assets which are more sensitive to changes in interest rates than interest-bearing liabilities, or vice versa. The fluctuation of market interest rates can materially affect our net interest spread, interest margin, loan originations, deposit volumes and overall profitability. Additionally, there is a risk attributable to calculation methods (modeling risks) and assumptions used in the model to calculate our interest rate risk exposure, including loan prepayment and forward interest rate assumptions.

Our mortgage banking business is subject to additional interest rate risk. For instance, rising interest rates may lower the loan origination volume thereby reducing the gain on sale of loans. Additionally, since the loan origination volume is hedged against interest rate fluctuations with forward loan sale commitments and put option contracts or other derivative financial instruments, rising or falling interest rates may alter the actual loan origination volume such that the hedges are insufficient to protect our profitability margins. Also, we cannot be assured that the value of the instruments we use to hedge our loan origination volume will react to the interest rate fluctuations in the same manner as the value of the loan origination commitments. The inconsistencies may also significantly impact profitability.

For further information on our interest rate risks, see the discussion included in “Item 7A. Quantitative and Qualitative Disclosure About Market Risk” on page 65 of this Form 10-K.

Secondary mortgage market conditions could have a material adverse impact on our financial condition and earnings.

In addition to being affected by interest rates, the secondary mortgage markets are also currently experiencing unprecedented disruptions resulting from reduced investor demand for mortgage loans and mortgage-backed securities and increased investor yield requirements for those loans and securities. These conditions may continue or even worsen in the future. In light of current conditions, there is a higher risk to retaining a larger portion of mortgage loans than we would in other environments until they are sold to investors. While our capital and liquidity positions are currently strong and we believe we have sufficient capacity to hold additional mortgage loans until investor demand improves and yield requirements moderate, our capacity to retain mortgage loans is limited. As a result, a prolonged period of secondary market illiquidity may reduce our loan production volumes and could have a material adverse impact on our future earnings and financial condition.

Our profitability depends significantly on economic conditions in the State of California.

Our success depends primarily on the general economic conditions of the State of California and the specific local markets in which we operate. Adverse economic conditions unique to the California markets could have a material adverse effect on our financial condition and results of operations. Further, a significant decline in general economic conditions, caused by inflation, recession, unemployment, changes in securities markets or other factors could impact our state and local markets and, in turn, also have a material adverse effect on our financial condition and results of operations. Of particular concern are the falling real estate values, which may lead to higher loan losses since the majority of our loans are secured by real estate located within California. Falling real estate values may inhibit our ability to recover on defaulted loans by selling the underlying real estate.

Competition with other financial institutions could adversely affect our profitability.

The banking and financial services industry is very competitive. Legal and regulatory developments have made it easier for new and sometimes unregulated competitors to compete with us. Consolidation among financial service

providers has resulted in fewer very large national and regional banking and financial institutions holding a large accumulation of assets. These institutions generally have significantly greater resources, a wider geographic presence or greater accessibility. Some of our competitors are able to offer more services, more favorable pricing or greater customer convenience than we do. In addition, our competition has grown from new banks and other financial services providers that target our existing or potential customers. As consolidation continues among large banks, we expect additional institutions to try to exploit our market.

Technological developments have allowed competitors including some non-depository institutions, to compete more effectively in local markets and have expanded the range of financial products, services and capital available to our target customers. If we are unable to implement, maintain and use such technologies effectively, we may not be able to offer products or achieve cost efficiencies necessary to compete in our industry. In addition, some of these competitors have fewer regulatory constraints and lower cost structures.

The loss of key members of our senior management team could adversely affect our business.

We believe that our success depends largely on the efforts and abilities of our senior management. Their experience and industry contacts significantly benefit us. The competition for qualified personnel in the financial services industry is intense, and the loss of any of our key personnel or an inability to continue to attract, retain and motivate key personnel could adversely affect our business.

We are subject to extensive government regulation and supervision.

We are subject to extensive federal and state regulation and supervision, primarily through the Bank and certain non-bank subsidiaries. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole, not shareholders. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among others. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways. Such changes could subject us to additional costs, limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, there can be no assurance that such violations will not occur. For further information, see “Item 1. Business - REGULATION” on page 31 of this Form 10-K.

We rely heavily on the proper functioning of our technology.

We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposit, loan and other systems. While we have policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems, there can be no assurance that any such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately addressed. The occurrence of any failures, interruptions or security breaches of our information systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations.

We rely on third-party service providers for much of our communications, information, operating and financial control systems technology. If any of our third-party service providers experience financial, operational or technological difficulties, or if there is any other disruption in our relationships with them, we may be required to locate alternative

sources of such services, and we cannot be certain that we could negotiate terms that are as favorable to us, or could obtain services with similar functionality, as found in our existing systems, without the need to expend substantial resources, if at all. Any of these circumstances could have an adverse effect on our business.

Terrorist activities could cause reductions in investor confidence and substantial volatility in real estate and securities markets.

It is impossible to predict the extent to which terrorist activities may occur in the United States or other regions, or their effect on a particular security issue. It is also uncertain what effects any past or future terrorist activities and/or any consequent actions on the part of the United States government and others will have on the United States and world financial markets, local, regional and national economies, and real estate markets across the United States. Among other things, reduced investor confidence could result in substantial volatility in securities markets, a decline in general economic conditions and real estate related investments and an increase in loan defaults. Such unexpected losses and events could materially affect our results of operations.

We rely on dividends from subsidiaries for most of our revenue.

Provident Financial Holdings, Inc is a separate and distinct legal entity from its subsidiaries. We receive substantially all of our revenue from dividends from our subsidiaries. These dividends are the principal source of funds to pay dividends on our common stock and interest and principal on our debt. Various federal and/or state laws and regulations limit the amount of dividends that the Bank may pay us. Also, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. Additionally, the Bank may experience periods of deteriorating earnings and cannot pay dividends to the Corporation. In the event the Bank is unable to pay dividends to us, we may not be able to service our debt, pay obligations or pay dividends on our common stock. The inability to receive dividends from the Bank could have a material adverse effect on our business, financial condition and results of operations.

We rely on effective internal controls.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud, and, as a result, investors and depositors could lose confidence in our financial reporting, which could adversely affect our business, the trading price of our stock and our ability to attract additional deposits.

In connection with the enactment of the Sarbanes-Oxley Act of 2002 and the implementation of the rules and regulations promulgated by the SEC, we document and evaluate our internal control over financial reporting in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act. This requires us to prepare an annual management report on our internal control over financial reporting, including management's assessment of the effectiveness of internal control over financial reporting. If we fail to identify and correct any significant deficiencies in the design or operating effectiveness of our internal control over financial reporting or fail to prevent fraud, current and potential shareholders and depositors could lose confidence in our internal controls and financial reporting, which could adversely affect our business, financial condition and results of operations, the trading price of our stock and our ability to attract additional deposits.

Changes in accounting standards may affect our performance.

Our accounting policies and methods are fundamental to how we record and report our financial condition and results of operations. From time to time there are changes in the financial accounting and reporting standards that govern the preparation of our financial statements. These changes can be difficult to predict and can materially impact how we report and record our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements.

Earthquakes and other natural disasters in our primary market area may result in material losses because of damage to collateral properties and borrowers' inability to repay loans.

Since our geographic concentration is in Southern California, we are subject to earthquakes and other natural disasters. A major earthquake or other natural disaster may disrupt our business operations for an indefinite period of time and could result in material losses, although we have not experienced any losses in the past six years as a result of earthquake damage or other natural disaster. In addition to possibly sustaining damage to our own

property, a substantial number of our borrowers would likely incur property damage to the collateral securing their loans. Although we are in an earthquake prone area, we and other lenders in the market area may not require earthquake insurance as a condition of making a loan. Additionally, if the collateralized properties are only damaged and not destroyed to the point of total insurable loss, borrowers may suffer sustained job interruption or job loss, which may materially impair their ability to meet the terms of their loan obligations.

We may elect or be compelled to seek additional capital in the future, but that capital may not be available when it is needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. In addition, we may elect to raise additional capital to support our business or to finance acquisitions, if any. In that regard, a number of financial institutions have recently raised considerable amounts of capital as a result of a deterioration in their results of operations and financial condition arising from the turmoil in the mortgage loan market, deteriorating economic conditions, declines in real estate values and other factors. Should we be required by regulatory authorities to raise additional capital, we may seek to do so through the issuance of, among other things, our common stock or preferred stock.

Our ability to raise additional capital, if needed, will depend on conditions in the capital markets, economic conditions and a number of other factors, many of which are outside of our control, and on our financial performance. Accordingly, we cannot assure you of our ability to raise additional capital if needed or if terms will be acceptable to us. If we cannot raise additional capital when needed, it may have a material adverse effect on our financial condition, results of operations and prospects.

Item 1B. Unresolved Staff Comments
None.

Item 2. Properties

At June 30, 2008, the net book value of the Bank’s property (including land and buildings) and its furniture, fixtures and equipment was $6.5 million. The Bank’s home office is located in Riverside, California. Including the home office, the Bank has 13 retail banking offices, 12 of which are located in Riverside County in the cities of Riverside (5), Moreno Valley, Hemet, Sun City, Rancho Mirage, Corona, Temecula and Blythe. One office is located in Redlands, San Bernardino County, California. The Bank owns eight of the retail banking offices and five are leased. The leases expire from 2009 to 2013. A new retail banking office in Moreno Valley (on Perris Boulevard) is expected to be opened in September 2008 with a lease expiration of 2013. The Bank also leases four stand-alone loan production offices, which are located in Glendora, Pleasanton, Rancho Cucamonga and Riverside, California. The leases expire from 2008 to 2009.

Item 3. Legal Proceedings

Periodically, there have been various claims and lawsuits involving the Bank, such as claims to enforce liens, condemnation proceedings on properties in which the Bank holds security interests, claims involving the making and servicing of real property loans and other issues in the ordinary course of and incident to the Bank’s business. The Bank is not a party to any pending legal proceedings that it believes would have a material adverse effect on the financial condition, operations and cash flows of the Bank.

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

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended June 30, 2008.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The common stock of Provident Financial Holdings, Inc. is listed on the NASDAQ Global Select Market under the symbol PROV. The following table provides the high and low stock prices for PROV during the last two fiscal years. As of June 30, 2008, there were approximately 338 stockholders of record.

	First (Ended September 30)	Second (Ended December 31)	Third (Ended March 31)	Fourth (Ended June 30)
2008 Quarters:				
High	$ 24.99	$ 25.17	$ 18.40	$ 16.65
Low	$ 17.51	$ 16.03	$ 12.00	$ 9.44
2007 Quarters:				
High	$ 31.42	$ 32.80	$ 30.50	$ 27.77
Low	$ 29.01	$ 28.81	$ 26.80	$ 23.33

The Corporation adopted a quarterly cash dividend policy on July 24, 2002. Quarterly dividends of $0.18, $0.18, $0.18 and $0.10 per share were paid for the quarters ended September 30, 2007, December 31, 2007, March 31, 2008 and June 30, 2008, respectively. By comparison, quarterly dividends of $0.15, $0.18, $0.18 and $0.18 per share were paid for the quarters ended September 30, 2006, December 31, 2006, March 31, 2007 and June 30, 2007, respectively. Future declarations or payments of dividends will be subject to the approval of the Corporation's Board of Directors, which will take into account the Corporation's financial condition, results of operations, tax considerations, capital requirements, industry standards, economic conditions and other factors, including the regulatory restrictions which affect the payment of dividends by the Bank to the Corporation. See "Item 1. Business – Regulation - Federal Regulation of Savings Institutions - Limitations on Capital Distributions" on page 34 of this Form 10-K. Under Delaware law, dividends may be paid either out of surplus or, if there is no surplus, out of net profits for the current fiscal year and/or the preceding fiscal year in which the dividend is declared.

The Corporation repurchases its common stock consistent with Board approved stock repurchase plans. On June 26, 2008, the Corporation announced a new stock repurchase program to repurchase up to five percent of its common stock (approximately 310,385 shares). The new program is the result of the expiration of the June 2007 stock repurchase program. During fiscal 2008, a total of 187,081 shares were purchased under the June 2007 stock repurchase program at an average cost of $21.78 per share. The Corporation also repurchased 995 shares of restricted stock from employees in lieu of distribution (to satisfy the minimum income tax required to be withheld from employees) at an average price of $22.21 per share.

The table below sets forth information regarding the Corporation's purchases of its common stock during the fourth quarter of fiscal 2008.

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plan	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plan
April 1, 2008 – April 30, 2008	-	$ -	-	131,766
May 1, 2008 – May 31, 2008	-	-	-	131,766
June 1, 2008 – June 30, 2008	-	-	-	310,385(1)
Total	-	$ -	-	310,385

(1) On June 25, 2008, the June 2007 stock repurchase program and the authorization to purchase shares through the program expired. On June 26, 2008, the Corporation announced a new stock repurchase plan to repurchase up to 310,385 shares, which expires on June 26, 2009.

Performance Graph

The following graph compares the cumulative total shareholder return on the Corporation's common stock with the cumulative total return on the Nasdaq Stock Index (U.S. Stock) and Nasdaq Bank Index. Total return assumes the reinvestment of all dividends.

COMPARISON OF CUMULATIVE TOTAL RETURNS *

	6/30/03	6/30/04	6/30/05	6/30/06	6/30/07	6/30/08
PROV	$ 100.00	$ 122.57	$ 148.54	$ 161.86	$ 138.25	$ 54.22
NASDAQ Stock Index	$ 100.00	$ 126.94	$ 126.79	$ 134.57	$ 164.61	$ 149.14
NASDAQ Bank Index	$ 100.00	$ 107.52	$ 122.97	$ 128.31	$ 172.57	$ 126.25

* Assumes that the value of the investment in the Corporation's common stock and each index was $100 on June 30, 2003 and that all dividends were reinvested.

Item 6. Selected Financial Data

The information contained under the heading "Financial Highlights" in the Corporation's Annual Report to Shareholders filed as Exhibit 13 to this report on Form 10-K is incorporated herein by reference.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read in conjunction with the Corporation's Consolidated Financial Statements and Notes to the Consolidated Financial Statements included in Item 8 of this Form 10-K.

General

Management's discussion and analysis of financial condition and results of operations are intended to assist in understanding the financial condition and results of operations of the Corporation. The information contained in this section should be read in conjunction with the Consolidated Financial Statements and Notes to the Consolidated Financial Statements included in Item 8 of this Form 10-K. Provident Savings Bank, F.S.B., is a wholly owned

subsidiary of Provident Financial Holdings, Inc. and as such, comprises substantially all of the activity for Provident Financial Holdings, Inc.

Certain matters in this Form 10-K constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. This Form 10-K contains statements that the Corporation believes are "forward-looking statements." These statements relate to the Corporation's financial condition, results of operations, plans, objectives, future performance or business. You should not place undue reliance on these statements, as they are subject to risks and uncertainties. When considering these forward-looking statements, you should keep in mind these risks and uncertainties, as well as any cautionary statements the Corporation may make. Moreover, you should treat these statements as speaking only as of the date they are made and based only on information then actually known to the Corporation. There are a number of important factors that could cause future results to differ materially from historical performance and these forward-looking statements. Factors which could cause actual results to differ materially include, but are not limited to, the credit risks of lending activities, including changes in the level and trend of loan delinquencies and charge-offs; changes in general economic conditions, either nationally or in our market areas; changes in the levels of general interest rates, deposit interest rates, our net interest margin and funding sources; fluctuations in the demand for loans, the number of unsold homes and other properties and fluctuations in real estate values in our market areas; results of examinations by the Office of Thrift Supervision and of our bank subsidiary by the Federal Deposit Insurance Corporation, the Office of Thrift Supervision or other regulatory authorities, including the possibility that any such regulatory authority may, among other things, require us to increase our reserve for loan losses or to write-down assets; our ability to control operating costs and expenses; our ability to implement our branch expansion strategy; our ability to successfully integrate any assets, liabilities, customers, systems, and management personnel we have acquired or may in the future acquire into our operations and our ability to realize related revenue synergies and cost savings within expected time frames and any goodwill charges related thereto; our ability to manage loan delinquency rates; our ability to retain key members of our senior management team; costs and effects of litigation, including settlements and judgments; increased competitive pressures among financial services companies; changes in consumer spending, borrowing and savings habits; legislative or regulatory changes that adversely affect our business; adverse changes in the securities markets; inability of key third-party providers to perform their obligations to us; changes in accounting policies and practices, as may be adopted by the financial institution regulatory agencies or the Financial Accounting Standards Board; war or terrorist activities; other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services and other risks detailed in the Corporation's reports filed with the SEC.

Critical Accounting Policies

The discussion and analysis of the Corporation's financial condition and results of operations are based upon the Corporation's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Allowance for loan losses involves significant judgment and assumptions by management, which have a material impact on the carrying value of net loans. Management considers this accounting policy to be a critical accounting policy. The allowance is based on two principles of accounting: (i) SFAS No. 5, "Accounting for Contingencies," which requires that losses be accrued when they are probable of occurring and can be estimated; and (ii) SFAS No. 114, "Accounting by Creditors for Impairment of a Loan," and SFAS No. 118, "Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures," which require that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance. The allowance has two components: a formula allowance for groups of homogeneous loans and a specific valuation allowance for identified problem loans. Each of these components is based upon estimates that can

change over time. The formula allowance is based primarily on historical experience and as a result can differ from actual losses incurred in the future. The history is reviewed at least quarterly and adjustments are made as needed. Various techniques are used to arrive at specific loss estimates, including historical loss information, discounted cash flows and the fair market value of collateral. The use of these techniques is inherently subjective and the actual losses could be greater or less than the estimates. For further details, see

"Comparison of Operating Results for the Years Ended June 30, 2008 and 2007 - Provision for Loan Losses" on page 56 and page 60 of this Form 10-K. See also Item 1. "Business – Delinquencies and Classified Assets – Allowance for Loan Losses" beginning on page 15.

Interest is not accrued on any loan when its contractual payments are more than 90 days delinquent or if the loan is deemed impaired. In addition, interest is not recognized on any loan where management has determined that collection is not reasonably assured. A non-accrual loan may be restored to accrual status when delinquent principal and interest payments are brought current and future monthly principal and interest payments are expected to be collected.

SFAS No. 133, "Accounting for Derivative Financial Instruments and Hedging Activities," requires that derivatives of the Corporation be recorded in the consolidated financial statements at fair value. Management considers this accounting policy to be a critical accounting policy. The Bank's derivatives are primarily the result of its mortgage banking activities in the form of commitments to extend credit, commitments to sell loans, commitments to purchase MBS and option contracts to mitigate the risk of the commitments. Estimates of the percentage of commitments to extend credit on loans to be held for sale that may not fund are based upon historical data and current market trends. The fair value adjustments of the derivatives are recorded in the consolidated statements of operations with offsets to other assets or other liabilities in the consolidated statements of financial condition.

Management accounts for income taxes by estimating future tax effects of temporary differences between the tax and book basis of assets and liabilities considering the provisions of enacted tax laws. These differences result in deferred tax assets and liabilities, which are included in our Consolidated Statements of Financial Condition. Our judgment is required in determining the amount and timing of recognition of the resulting deferred tax assets and liabilities, including projections of future taxable income. Therefore, management considers its accounting for income taxes a critical accounting policy.

Executive Summary and Operating Strategy

Provident Savings Bank, F.S.B. established in 1956 is a financial services company committed to serving consumers and small to mid-sized businesses in the Inland Empire region of Southern California. The Bank conducts its business operations as Provident Bank, Provident Bank Mortgage, a division of the Bank, and through its subsidiary, Provident Financial Corp. The business activities of the Corporation, primarily through the Bank and its subsidiary, consist of community banking, mortgage banking, and to a lessor degree, investment services and trustee services on behalf of the Bank.

Community banking operations primarily consist of accepting deposits from customers within the communities surrounding the Bank's full service offices and investing those funds in single-family, multi-family, commercial real estate, construction, commercial business, consumer and other loans. Additionally, certain fees are collected from depositors, such as returned check fees, deposit account service charges, ATM fees, IRA/KEOGH fees, safe deposit box fees, travelers check fees, and wire transfer fees, among others. The primary source of income in community banking is net interest income, which is the difference between the interest income earned on loans and investment securities, and the interest expense paid on interest-bearing deposits and borrowed funds. During the next three years the Corporation intends to improve the community banking business by moderately growing total assets; by decreasing the percentage of investment securities to total assets and increasing the percentage of loans held for investment to total assets; by decreasing the concentration of single-family mortgage loans within loans held for investment; and by increasing the concentration of higher yielding multi-family, commercial real estate, construction and commercial business loans (which are sometimes referred to in this report as "preferred loans"). In addition, over time, the Corporation intends to decrease the percentage of time deposits in its deposit base and to increase the percentage of lower cost checking and savings accounts. This strategy is intended to improve core revenue through a higher net interest margin and ultimately, coupled with the growth of the Corporation, an increase in net interest

income.

Mortgage banking operations primarily consist of the origination and sale of mortgage loans secured by single-family residences. The primary sources of income in mortgage banking are gain on sale of loans and certain fees collected from borrowers in connection with the loan origination process. The Corporation will continue to

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restructure its operations in response to the rapidly changing mortgage banking environment. Changes may include a different product mix, further tightening of underwriting standards, a further reduction in its operating expenses or a combination of these and other changes.

Investment services operations primarily consist of selling alternative investment products such as annuities and mutual funds to our depositors. Provident Financial Corp performs trustee services for the Bank's real estate secured loan transactions and has in the past held, and may in the future hold, real estate for investment. Investment services and trustee services contribute a very small percentage of gross revenue.

There are a number of risks associated with the business activities of the Corporation, many of which are beyond the Corporation's control, including: changes in accounting principles, changes in regulation and changes in the economy, among others. The Corporation attempts to mitigate many of these risks through prudent banking practices such as interest rate risk management, credit risk management, operational risk management, and liquidity management. The current economic environment presents heightened risk for the Corporation primarily with respect to falling real estate values. Declining real estate values may lead to higher loan losses since the majority of the Corporation's loans are secured by real estate located within California. Significant declines in the value of California real estate may inhibit the Corporation's ability to recover on defaulted loans by selling the underlying real estate.

Commitments and Derivative Financial Instruments

The Corporation conducts a portion of its operations in leased facilities under non-cancelable agreements classified as operating leases (see Note 14 of the Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K for a schedule of minimum rental payments and lease expenses under such operating leases). For information regarding the Corporation's commitments and derivative financial instruments, see Note 15 of the Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K.

Off-Balance Sheet Financing Arrangements and Contractual Obligations

The following table summarizes the Corporation's contractual obligations at June 30, 2008 and the effect such obligations are expected to have on the Corporation's liquidity and cash flows in future periods:

	Payments Due by Period				
(In Thousands)	1 Year or Less	Over 1 to 3 Years	Over 3 to 5 Years	Over 5 Years	Total
Operating obligations	$ 973	$ 1,346	$ 811	$ 706	$ 3,836
Time deposits	602,588	68,822	7,455	59	678,924
FHLB – San Francisco advances	157,482	259,540	88,715	12,588	518,325
FHLB – San Francisco letter of credit	2,000	-	-	-	2,000
Total	$ 763,043	$ 329,708	$ 96,981	$ 13,353	$ 1,203,085

The expected obligations for time deposits and FHLB – San Francisco advances include anticipated interest accruals based on their respective contractual terms.

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, in the form of originating loans or providing funds under existing lines of credit, forward loan sale agreements to third parties and commitments to purchase investment securities. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the accompanying Consolidated Statements of Financial

Condition included in Item 8 of this Form 10-K. The Corporation's exposure to credit loss, in the event of non-performance by the other party to these financial instruments, is represented by the contractual amount of these instruments. The Corporation uses the same credit policies in making commitments to extend credit as it does for on-balance sheet instruments. As of June 30, 2008 and 2007, these commitments were $29.4 million and $44.5

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million, respectively.

Comparison of Financial Condition at June 30, 2008 and June 30, 2007

Total assets decreased $16.5 million, or 1%, to $1.63 billion at June 30, 2008 from $1.65 billion at June 30, 2007. The decrease was primarily a result of a decrease in the receivable from sale of loans, partly offset by an increase in loans held for sale.

Total investment securities increased $2.3 million, or 2%, to $153.1 million at June 30, 2008 from $150.8 million at June 30, 2007. A total of $78.9 million of investment securities were purchased in fiscal 2008, while $29.0 million of investment securities matured or were called by the issuers and $47.5 million of principal payments were received on mortgage-backed securities. The principal reduction of mortgage-backed securities was primarily attributable to mortgage prepayments and the scheduled principal payments of the underlying mortgage loans.

Loans held for investment increased $17.4 million, or 1%, to $1.37 billion at June 30, 2008 from $1.35 billion at June 30, 2007. This increase was primarily a result of originating and purchasing $283.2 million of loans held for investment, which was partly offset by $253.1 million of loan prepayments.

The table below describes the geographic dispersion of real estate secured loans held for investment at June 30, 2008, as a percentage of the total dollar amount outstanding:

Loan Category	Inland Empire	Southern California (1)	Other California	Other States	Total
Single-family	30%	54%	14%	2%	100%
Multi-family	9%	71%	18%	2%	100%
Commercial real estate	46%	48%	5%	1%	100%
Construction	61%	39%	-	-	100%
Other	100%	-	-	-	100%
Total	27%	58%	14%	1%	100%

(1) Other than the Inland Empire.

During fiscal 2008, the Bank originated $582.2 million in new loans, primarily through PBM, and purchased $99.8 million from other financial institutions, primarily in multi-family loans. A total of $373.5 million of loans were sold during fiscal 2008. PBM loan production was sold primarily on a servicing released basis. The total loan origination volume was lower than last year, due primarily to higher interest rates, more stringent underwriting standards, the general decline in real estate values and a more competitive environment.

The outstanding balance of loans held for sale increased to $28.5 million at June 30, 2008 from $1.3 million at June 30, 2007. The increase was due primarily to an increased use of “best-efforts” loan sale commitments in comparison to firm commitments used in prior periods. The Bank changed its strategy to “best-efforts” commitments because it is very difficult in the current environment to accurately forecast the fallout ratio of loan commitments extended to borrowers. An inaccurate fallout ratio forecast while using firm commitments can be very costly since the Bank could experience unexpected non-delivery fees.

There was no receivable from sale of loans at June 30, 2008, compared to $60.5 million at June 30, 2007. The change was due to the implementation of a “best-efforts” loan sale strategy. Using the “best-efforts” loan sale strategy delays the recognition of income until the loans committed for sale are settled by the investor.

Total real estate owned was $9.4 million at June 30, 2008, up 147% from $3.8 million at June 30, 2007. As of June 30, 2008, real estate owned was comprised of 45 properties, primarily single-family residences and single-family undeveloped lots located in Southern California. This compares to 10 real estate owned properties at June 30, 2007, primarily single-family residences located in Southern California. The increase in real estate owned was due primarily to more foreclosures resulting from weakness in the real estate market, stricter underwriting standards, less

liquidity in the secondary market, deterioration of some borrowers' credit capacity and other related factors. During fiscal 2008, the Bank acquired 72 real estate owned properties in the settlement of loans and sold 37 properties.

Total deposits increased $11.0 million, or 1%, to $1.01 billion at June 30, 2008 from $1.00 billion at June 30, 2007. Although the Bank continued its emphasis on expanding customer relationships, particularly in transaction accounts, decreases in short-term interest rates during fiscal 2008 became a catalyst for depositors to move their funds from savings accounts to time deposits to take advantage of higher yields. Transaction accounts decreased $4.1 million, or 1%, to $348.7 million at June 30, 2008 from $352.8 million at June 30, 2007. These accounts were primarily comprised of savings and checking accounts. Time deposits increased $15.1 million, or 2%, to $663.7 million at June 30, 2008 from $648.6 million at June 30, 2007.

Borrowings, primarily FHLB – San Francisco advances, decreased $23.5 million, or 5%, to $479.3 million at June 30, 2008 from $502.8 million at June 30, 2007. FHLB – San Francisco advances were primarily used to supplement the funding needs of the Bank, to the extent that the increase in deposits and the decrease in receivable from sale of loans did not meet loan funding requirements.

Total stockholders' equity decreased $4.8 million, or 4%, to $124.0 million at June 30, 2008 from $128.8 million at June 30, 2007. The decrease in stockholders' equity during fiscal 2008 was primarily attributable to share repurchases and cash dividends to shareholders, partly offset by earnings in fiscal 2008, allocation of contributions to the ESOP, the exercise of stock options and the related tax benefits. During fiscal 2008, a total of 7,500 shares of stock options were exercised with an average strike price of $9.15 per share and a $6,000 tax benefit from non-qualified equity compensation was recognized. The Corporation repurchased 187,081 shares of common stock, or approximately 3% of its outstanding shares, at an average price of $21.78 per share, totaling $4.1 million. The Corporation also repurchased 995 shares of restricted stock from employees in lieu of distribution (to satisfy the minimum income tax required to be withheld from employees) at an average price of $22.21 per share. During fiscal 2008, the Corporation declared and distributed cash dividends to its shareholders of $4.0 million, or $0.64 per share. The Corporation's book value per share decreased to $19.97 at June 30, 2008 from $20.20 at June 30, 2007.

Comparison of Operating Results for the Years Ended June 30, 2008 and 2007

General. The Corporation had net income of $860,000, or $0.14 per diluted share, for the fiscal year June 30, 2008, as compared to $10.5 million, or $1.57 per diluted share, for the fiscal year June 30, 2007. The $9.6 million decrease in net income in fiscal 2008 was primarily attributable to an $8.0 million increase in the provision for loan losses and a $12.4 million decrease in non-interest income, partly offset by a $4.3 million decrease in non-interest expense. The Corporation's efficiency ratio increased to 65% in fiscal 2008 from 58% in the same period of fiscal 2007. Return on average assets in fiscal 2008 decreased 56 basis points to 0.05% from 0.61% in fiscal 2007. Return on average equity in fiscal 2008 decreased to 0.68% from 7.77% in fiscal 2007.

Net Interest Income. Net interest income before provision for loan losses decreased $287,000, or 1%, to $41.4 million in fiscal 2008 from $41.7 million in fiscal 2007. This decrease resulted principally from a decrease in average earning assets, partly offset by an increase in the net interest margin. The average balance of earning assets decreased $78.9 million, or 5%, to $1.59 billion in fiscal 2008 from $1.67 billion in fiscal 2007. The average net interest margin increased 10 basis points to 2.61% in fiscal 2008 from 2.51% in fiscal 2007.

Interest Income. Interest income decreased $5.3 million, or 5%, to $95.7 million for fiscal 2008 from $101.0 million for fiscal 2007. The decrease in interest income was primarily a result of decreases in the average balance and the average yield of earning assets. The decrease in average assets was primarily attributable to the decrease in loans receivable, investment securities and FHLB – San Francisco stock. The average yield on earning assets decreased two basis points to 6.04% in fiscal 2008 from 6.06% in fiscal 2007. The decrease in the average yield on earning assets was the result of a decrease in the average yield of loans receivable, partly offset by increases in the average yield of

investment securities and FHLB – San Francisco stock during fiscal 2008.

Loan interest income decreased $5.2 million, or 6%, to $86.3 million in fiscal 2008 from $91.5 million in fiscal 2007. This decrease was attributable to a lower average loan balance and a lower average loan yield. The average balance of loans outstanding, including receivable from sale of loans and loans held for sale, decreased $48.9

million, or 3%, to $1.40 billion during fiscal 2008 from $1.45 billion during fiscal 2007. The average loan yield during fiscal 2008 decreased 15 basis points to 6.18% from 6.33% during fiscal 2007. The decrease in the average loan yield was primarily attributable to higher non-accrual loans, which required interest income reversals. Total non-accrual loans increased to $23.2 million at June 30, 2008 from $15.9 million at June 30, 2007.

Interest income from investment securities increased $418,000, or 6%, to $7.6 million in fiscal 2008 from $7.1 million in fiscal 2007. This increase was primarily a result of an increase in the average yield, partly offset by a decrease in the average balance. The average yield on the investment securities increased 80 basis points to 4.87% during fiscal 2008 from 4.07% during fiscal 2007. The increase in the average yield of investment securities was primarily a result of the new purchases with a higher average yield (5.05% versus the average yield of 4.87% in fiscal 2008) and maturing securities and called securities with a lower average yield (3.17%). The premium amortization in fiscal 2008 was $16,000, compared to the premium amortization of $21,000 in fiscal 2007. The average balance of investment securities decreased $19.9 million, or 11%, to $155.5 million in fiscal 2008 from $175.4 million in fiscal 2007 as a result of the Bank’s stated strategy to reduce the percentage of investment securities to earning assets.

FHLB – San Francisco stock dividends decreased by $403,000, or 18%, to $1.8 million in fiscal 2008 from $2.2 million in fiscal 2007. This decrease was attributable to a lower average balance, partly offset by a higher average yield. The average balance of FHLB – San Francisco stock decreased $9.3 million to $32.3 million during fiscal 2008 from $41.6 million during fiscal 2007. The decrease in FHLB – San Francisco stock was due to the stock redemption of $13.6 million in July 2007, in accordance with the borrowing requirements of the FHLB – San Francisco. The average yield on FHLB – San Francisco stock increased 30 basis points to 5.65% during fiscal 2008 from 5.35% during fiscal 2007.

Interest Expense. Total interest expense for fiscal 2008 was $54.3 million as compared to $59.2 million for fiscal 2007, a decrease of $4.9 million, or 8%. This decrease was primarily attributable to a decrease in the average cost and a lower average balance of interest-bearing liabilities. The decrease in the average cost was due to the decrease in the average borrowing cost, partly offset by an increase in the average deposit cost. The average balance of interest-bearing liabilities, principally deposits and borrowings, decreased $68.1 million, or 4%, to $1.48 billion during fiscal 2008 from $1.55 billion during fiscal 2007. The average cost of interest-bearing liabilities was 3.68% during fiscal 2008, down 15 basis points from 3.83% during fiscal 2007.

Interest expense on deposits for fiscal 2008 was $34.6 million as compared to $31.2 million for the same period of fiscal 2007, an increase of $3.4 million, or 11%. The increase in interest expense on deposits was primarily attributable to a higher average cost and a higher average balance. The average cost of deposits increased to 3.42% in fiscal 2008 from 3.30% during fiscal 2007, an increase of 12 basis points. The increase in the average cost of deposits was primarily attributable to a higher proportion of time deposits with higher interest rates than transaction accounts and a higher average cost of checking accounts resulting from promotional interest expense of $95,000, partly offset by a lower average cost of time deposits. The average balance of deposits increased $65.6 million, or 7%, to $1.01 billion during fiscal 2008 from $946.5 million during fiscal 2007. The average balance of transaction accounts decreased by $24.2 million, or 7%, to $345.3 million in fiscal 2008 from $369.5 million in fiscal 2007. The average balance of time deposits increased by $89.8 million, or 16%, to $666.8 million in fiscal 2008 as compared to $577.0 million in fiscal 2007. The average balance of time deposits to total deposits in fiscal 2008 was 66%, compared to 61% in fiscal 2007. The increase in time deposits is primarily attributable to the time deposit marketing campaign and depositors switching from transaction accounts to time deposits to take advantage of higher yields.

Interest expense on borrowings, primarily FHLB – San Francisco advances, for fiscal 2008 decreased $8.3 million, or 30%, to $19.7 million from $28.0 million for fiscal 2007. The decrease in interest expense on borrowings was primarily a result of a lower average cost and a lower average balance. The average cost of borrowings decreased to 4.24% for fiscal 2008 from 4.68% in fiscal 2007, a decrease of 44 basis points. The decrease in the average cost of borrowings was the result of lower overnight interest rates and maturities of long-term advances at higher interest rates. The average balance of borrowings decreased $133.8 million, or 22%, to $465.5 million during fiscal 2008 from $599.3 million during fiscal 2007 as a result of changing liquidity needs.

Provision for Loan Losses. During fiscal 2008, the Corporation recorded a provision for loan losses of $13.1 million, an increase of $8.0 million from $5.1 million during fiscal 2007. The provision for loan losses in fiscal 2008 was primarily attributable to the loan classification downgrades in the loans held for investment ($9.5 million), deterioration in the real estate collateral values securing those loans ($2.6 million) and an increase in loans held for investment ($970,000).

Non-performing assets increased to $32.5 million, or 1.99% of total assets, at June 30, 2008, compared to $19.7 million, or 1.20% of total assets, at June 30, 2007. The non-performing assets at June 30, 2008 were primarily comprised of 52 single-family loans originated for investment ($15.4 million), 12 construction loans originated for investment ($4.7 million), 12 single-family loans repurchased from, or unable to sell to investors ($1.9 million) and real estate owned comprised of 30 single-family properties, one multi-family property and 14 undeveloped lots acquired in the settlement of loans ($9.4 million). The 14 undeveloped lots are located in Coachella, California. Net charge-offs for the fiscal year ended June 30, 2008 were $8.1 million or 0.58% of average loans receivable, compared to $540,000 or 0.04% of average loans receivable in the comparable period last year.

Classified loans at June 30, 2008 were $59.2 million, comprised of $29.4 million in the special mention category and $29.8 million in the substandard category. Classified loans at June 30, 2007 were $32.3 million, consisting of $13.3 million in the special mention category and $19.0 million in the substandard category.

At June 30, 2008, the allowance for loan losses was $19.9 million, comprised of $13.4 million of general loan loss allowances and $6.5 million of specific loan loss allowances. At June 30, 2007, the allowance for loan losses was $14.8 million, comprised of $11.5 million of general loan loss allowances and $3.3 million of specific loan loss allowances. The allowance for loan losses as a percentage of gross loans held for investment was 1.43% at June 30, 2008 compared to 1.09% at June 30, 2007. Management considers the allowance for loan losses sufficient to absorb potential losses inherent in its loans held for investment.

The allowance for loan losses is maintained at a level sufficient to provide for estimated losses based on evaluating known and inherent risks in the loans held for investment and upon management's continuing analysis of the factors underlying the quality of the loans held for investment. These factors include changes in the size and composition of the loans held for investment, actual loan loss experience, current economic conditions, detailed analysis of individual loans for which full collectibility may not be assured, and determination of the realizable value of the collateral securing the loans. Provisions for loan losses are charged against operations on a monthly basis, as necessary, to maintain the allowance at appropriate levels. Management believes that the amount maintained in the allowance will be adequate to absorb losses inherent in the loans held for investment. Although management believes it uses the best information available to make such determinations, there can be no assurance that regulators, in reviewing the Bank's loans held for investment, will not request the Bank to significantly increase its allowance for loan losses. Future adjustments to the allowance for loan losses may be necessary and results of operations could be significantly and adversely affected as a result of economic, operating, regulatory, and other conditions beyond the control of the Bank.

Non-Interest Income. Total non-interest income decreased $12.4 million, or 70%, to $5.2 million in fiscal 2008 from $17.6 million in fiscal 2007. The decrease was primarily attributable to a decrease in the gain on sale of loans, a decrease in the gain on sale of real estate held for investment and a decrease in the sale and operations of real estate owned acquired in the settlement of loans.

Loan servicing and other fees decreased $356,000, or 17%, to $1.8 million during fiscal 2008 from $2.1 million during fiscal 2007. The decrease was primarily attributable to lower brokered loan fees and lower prepayment fees. Total brokered loans in fiscal 2008 were $16.0 million, down $25.6 million, or 62%, from $41.6 million in the same period of fiscal 2007 as a result of adverse real estate markets in Southern California. Total scheduled principal payments and loan prepayments were $253.1 million in the fiscal 2008, down $126.3 million, or 33%, from $379.4 million in fiscal 2007, resulting in lower prepayment fees.

The gain on sale of loans decreased $8.3 million, or 89%, to $1.0 million for fiscal 2008 from $9.3 million in fiscal 2007. The decrease was a result of a lower average loan sale margin and a lower volume of loans originated for sale in fiscal 2008. The average loan sale margin for PBM during fiscal 2008 was 0.27%, down 56 basis points from 0.83% during fiscal 2007. The gain on sale of loans includes a loss of $317,000 on derivative financial instruments

as a result of SFAS No. 133 in fiscal 2008, compared to a gain of $212,000 in fiscal 2007. The gain on sale of loans also includes a recourse provision of $1.5 million in fiscal 2008 and $347,000 in fiscal 2007 for loans sold that are subject to repurchase, resulting from early payment defaults or fraud claims. In addition, the Bank recorded a charge of $142,000 for the mortgage premium disclosure errors on FHA loans sold in fiscal 2008, which the Bank subsequently corrected in July 2008. The volume of loans sold decreased by $749.9 million, or 67%, to $373.5 million in fiscal 2008 as compared to $1.12 billion in fiscal 2007. The loan sale margin and loan sale volume decreased because the mortgage banking environment remains highly competitive and volatile as a result of the well-publicized collapse of the credit markets.

Deposit account fees increased $867,000, or 42%, to $3.0 million in fiscal 2008 from $2.1 million in fiscal 2007. The increase was primarily attributable to an increase in returned check fees.

There was no gain on sale of real estate held for investment in fiscal 2008, as compared to a gain of $2.3 million recorded in fiscal 2007. The gain in fiscal 2007 was the result of the sale of approximately six acres of land in Riverside, California. Currently, the Corporation does not have any real estate held for investment.

The sale and operations of real estate owned acquired in the settlement of loans reflected a net loss of $2.7 million in fiscal 2008, as compared to a net loss of $117,000 in fiscal 2007. The net loss in fiscal 2008 was comprised of a $932,000 net loss on the sale of 37 real estate owned properties, operating expenses of $1.2 million and a provision for losses on real estate owned of $517,000.

Non-Interest Expense. Total non-interest expense in fiscal 2008 was $30.3 million, a decrease of $4.3 million or 12%, as compared to $34.6 million in fiscal 2007. The decrease in non-interest expense was primarily the result of decreases in compensation, premises and occupancy, equipment, marketing and other expenses, partly offset by increases in professional expenses and deposit insurance premiums and regulatory assessments.

Compensation expense decreased $3.9 million, or 17%, to $19.0 million in fiscal 2008 from $22.9 million in fiscal 2007. The decrease in compensation expense was primarily a result of fewer employees, lower incentive compensation and ESOP expenses, partly offset by lower deferred compensation attributable to the application of SFAS No. 91, "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases."

The decreases in premises and occupancy, equipment, marketing and other operating expenses in fiscal 2008 were primarily attributable to the closing of six PBM loan production offices in the first half of fiscal 2008 and lower operating expenses commensurate with lower loan origination volume.

Professional expenses increased $380,000, or 32%, to $1.6 million in fiscal 2008 from $1.2 million in fiscal 2007. The increase was primarily the result of higher legal expenses corresponding to the increase in delinquent loans.

Deposit insurance premiums and regulatory assessments increased $370,000, or 85%, to $804,000 in fiscal 2008 from $434,000 in fiscal 2007. The increase was a result of an increase in FDIC deposit insurance premiums.

Income Taxes. The provision for income taxes was $2.4 million for fiscal 2008, representing an effective tax rate of 73.4%, as compared to $9.1 million in fiscal 2007, representing an effective tax rate of 46.6%. The increase in the effective tax rate was primarily the result of a higher percentage of permanent tax differences relative to income before taxes and an additional tax provision of $407,000 on a disallowed deduction in the fiscal 2006 tax return which was discovered during the ongoing examination by the Internal Revenue Service. The Corporation determined that the above tax rates meet its income tax obligations.

Comparison of Operating Results for the Years Ended June 30, 2007 and 2006

General. The Corporation had net income of $10.5 million, or $1.57 per diluted share, for the fiscal year June 30, 2007, as compared to $19.6 million, or $2.82 per diluted share, for the fiscal year June 30, 2006. The $9.1 million decrease in net income in fiscal 2007 was primarily attributable to a decrease in net interest income, an increase in the provision for loan losses, a decrease in non-interest income and an increase in non-interest expense. The

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Corporation's efficiency ratio increased to 58% in fiscal 2007 from 48% in the same period of fiscal 2006. Return on average assets in fiscal 2007 decreased 63 basis points to 0.61% from 1.24% in fiscal 2006. Return on average equity in fiscal 2007 decreased to 7.77% from 15.02% in fiscal 2006.

Net Interest Income. Net interest income before provision for loan losses decreased $2.3 million, or 5%, to $41.7 million in fiscal 2007 from $44.0 million in fiscal 2006. This decrease resulted principally from a decrease in the net interest margin, partly offset by an increase in average earning assets. The average net interest margin declined 35 basis points to 2.51% in fiscal 2007 from 2.86% in fiscal 2006. The average balance of earning assets increased $129.0 million, or 8%, to $1.66 billion in fiscal 2007 from $1.54 billion in fiscal 2006.

Interest Income. Interest income increased $14.4 million, or 17%, to $101.0 million for fiscal 2007 from $86.6 million for fiscal 2006. The increase in interest income was primarily a result of increases in the average balance and the average yield of earning assets. The increase in average assets was primarily attributable to the increase in loans receivable, which was partly offset by the decrease in investment securities. The average yield on earning assets increased 42 basis points to 6.06% in fiscal 2007 from 5.64% in fiscal 2006. The increase in the average yield on earning assets was the result of increases in the average yield of loans receivable, investment securities, FHLB – San Francisco stock and federal funds investments during fiscal 2007.

Loan interest income increased $13.7 million, or 18%, to $91.5 million in fiscal 2007 from $77.8 million in fiscal 2006. This increase was attributable to a higher average loan balance and a higher average loan yield. The average balance of loans outstanding, including receivable from sale of loans and loans held for sale, increased $155.8 million, or 12%, to $1.45 billion during fiscal 2007 from $1.29 billion during fiscal 2006. The average loan yield during fiscal 2007 increased 30 basis points to 6.33% from 6.03% during fiscal 2006. The increase in the average loan yield was primarily attributable to mortgage loans originated with higher interest rates, the upward repricing of adjustable rate loans during the year and a higher percentage of preferred loans, which generally have a higher yield.

Interest income from investment securities increased $318,000, or 5%, to $7.1 million in fiscal 2007 from $6.8 million in fiscal 2006. This increase was primarily a result of an increase in average yield, partly offset by a decrease in the average balance. The average balance of investment securities decreased $27.7 million, or 14%, to $175.4 million in fiscal 2007 from $203.1 million in fiscal 2006. The average yield on the investment securities increased 71 basis points to 4.07% during fiscal 2007 from 3.36% during fiscal 2006. The increase in the average yield of investment securities was primarily a result of the new purchases with a higher average yield (5.30% versus the average yield of 4.07% in fiscal 2007) and the maturing securities with an average yield of 2.65%. The premium amortization in fiscal 2007 was $21,000, compared to the premium amortization of $258,000 in fiscal 2006.

FHLB – San Francisco stock dividends increased by $394,000, or 22%, to $2.2 million in fiscal 2007 from $1.8 million in fiscal 2006. This increase was attributable to a higher average yield and a higher average balance. The average yield on FHLB – San Francisco stock increased 57 basis points to 5.35% during fiscal 2007 from 4.78% during fiscal 2006. The average balance of FHLB – San Francisco stock increased $3.3 million to $41.6 million during fiscal 2007 from $38.3 million during fiscal 2006. The increase in FHLB – San Francisco stock was in accordance with the borrowing requirements of the FHLB – San Francisco.

Interest Expense. Total interest expense for fiscal 2007 was $59.2 million as compared to $42.6 million for fiscal 2006, an increase of $16.6 million, or 39%. This increase was primarily attributable to an increase in the average cost and a higher average balance of interest-bearing liabilities. The average cost of interest-bearing liabilities was 3.83% during fiscal 2007, up 83 basis points from 3.00% during fiscal 2006. The average balance of interest-bearing liabilities, principally deposits and borrowings, increased $123.4 million, or 9%, to $1.55 billion during fiscal 2007 from $1.42 billion during fiscal 2006.

Interest expense on deposits for fiscal 2007 was $31.2 million as compared to $22.1 million for the same period of fiscal 2006, an increase of $9.1 million, or 41%. The increase in interest expense on deposits was primarily

attributable to a higher average cost and a higher average balance. The average cost of deposits increased to 3.30% in fiscal 2007 from 2.36% during fiscal 2006, an increase of 94 basis points. The increase in the average cost of deposits, primarily in time deposits, was attributable to the general rise in short-term interest rates. The average balance of deposits increased $9.6 million, or 1%, to $946.5 million during fiscal 2007 from $936.9 million during fiscal 2006. The average balance of transaction accounts decreased by $80.0 million, or 18%, to $369.5 million in

fiscal 2007 from $449.5 million in fiscal 2006. The average balance of time deposits increased by $89.6 million, or 18%, to $577.0 million in fiscal 2007 as compared to $487.4 million in fiscal 2006. The increase in time deposits is primarily attributable to the time deposit marketing campaign and depositors switching from transaction accounts to time deposits to take advantage of higher yields. The average balance of transaction account deposits to total deposits in fiscal 2007 was 39%, compared to 48% in fiscal 2006.

Interest expense on borrowings, primarily FHLB – San Francisco advances, for fiscal 2007 increased $7.5 million, or 37%, to $28.0 million from $20.5 million for fiscal 2006. The increase in interest expense on borrowings was primarily a result of a higher average cost and a higher average balance. The average cost of borrowings increased to 4.68% for fiscal 2007 from 4.22% in fiscal 2006, an increase of 46 basis points. The increase in the average cost of borrowings was the result of higher short-term interest rates and maturities of long-term advances at lower interest rates. The average balance of borrowings increased $113.8 million, or 23%, to $599.3 million during fiscal 2007 from $485.5 million during fiscal 2006.

Provision for Loan Losses. During fiscal 2007, the Corporation recorded a provision for loan losses of $5.1 million, an increase of $4.0 million from $1.1 million during fiscal 2006. The provision for loan losses in fiscal 2007 was primarily attributable to a net increase of $3.1 million in specific loan loss reserves, an increase in classified loans and an increase in loans held for investment, primarily in preferred loans. The increase in specific loan loss allowances was primarily attributable to the establishment of a specific loan loss allowance of $2.6 million on 23 individual construction loans, with a disbursed total of $5.0 million, which were classified as non-accrual in November 2006. Classified loans at June 30, 2007 were $32.3 million, comprised of $13.3 million in the special mention category and $19.0 million in the substandard category. Classified loans increased by $23.0 million from June 30, 2006 when classified loans were $9.3 million, comprised of $3.7 million in the special mention category and $5.6 million in the substandard category.

The Corporation’s current operating strategy seeks to grow preferred loans at a faster rate than single-family mortgage loans. While higher yielding, these loans generally have greater risk than single-family mortgage loans. Further growth in these categories of loans may result in additions to the provision for loan losses. In addition, as noted above, the Corporation experienced a significant increase in classified loans during fiscal 2007, a majority of which were single-family mortgage loans. Rising delinquencies in single-family mortgage loans may also result in additions to the provision for loan losses.

At June 30, 2007, the allowance for loan losses was $14.8 million, comprised of $11.5 million of general loan loss allowances and $3.3 million of specific loan loss allowances. At June 30, 2006, the allowance for loan losses was $10.3 million, comprised of $10.1 million of general loan loss allowances and $238,000 of specific loan loss allowances. The allowance for loan losses as a percentage of gross loans held for investment was 1.09% at June 30, 2007 compared to 0.81% at June 30, 2006.

Non-Interest Income. Total non-interest income decreased $8.6 million, or 33%, to $17.6 million in fiscal 2007 from $26.2 million in fiscal 2006. The decrease was primarily attributable to a decrease in the gain on sale of real estate held for investment ($2.3 million versus $6.3 million), a decrease in the gain on sale of loans and a decrease in loan servicing and other fees.

The gain on sale of real estate held for investment in fiscal 2007 was primarily the result of the sale of approximately six acres of land in Riverside, California; while the gain on sale of real estate held for investment in fiscal 2006 was the result of the sale of a commercial office building in Riverside, California. Currently, the Corporation does not have any real estate held for investment.

The gain on sale of loans decreased $4.2 million, or 31%, to $9.3 million for fiscal 2007 from $13.5 million in fiscal 2006. The decrease was a result of a lower average loan sale margin and a lower volume of loans originated for sale in fiscal 2007. The average loan sale margin for PBM during fiscal 2007 was 0.83%, down 25 basis points from

1.08% during fiscal 2006. The gain on sale of loans includes a gain of $212,000 on derivative financial instruments as a result of SFAS No. 133 in fiscal 2007, compared to a gain of $71,000 in fiscal 2006. The gain on sale includes a recourse liability of $347,000 for loans sold to investors as of June 30, 2007. No recourse liability was required for loans sold to investors as of June 30, 2006. The volume of loans originated for sale decreased by $111.2 million, or 9%, to $1.13 billion in fiscal 2007 as compared to $1.24 billion in fiscal 2006. The loan sale margin and loan sale

volume decreased because the mortgage banking environment remains highly competitive and volatile as a result of the well-publicized collapse of the sub-prime loan market.

Loan servicing and other fees decreased $440,000, or 17%, to $2.1 million during fiscal 2007 from $2.6 million during fiscal 2006. The decrease was primarily attributable to lower brokered loan fees and lower prepayment fees. Total brokered loans in fiscal 2007 were $41.6 million, down $4.6 million, or 10%, from $46.2 million in fiscal 2006. Total scheduled principal payments and loan prepayments were $379.4 million in fiscal 2007, down $96.8 million, or 20%, from $476.2 million in fiscal 2006.

Non-Interest Expense. Total non-interest expense in fiscal 2007 was $34.6 million, an increase of $876,000 or 3%, as compared to $33.8 million in fiscal 2006. The increase in non-interest expense was primarily the result of increases in compensation expense and premises and occupancy expenses, partly offset by decreases in equipment, professional, marketing and other expenses.

The increase in compensation expense was primarily a result of lower deferred compensation attributable to the application of SFAS No. 91, "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases," partly offset by lower incentive compensation. On July 1, 2006 the Bank lowered the SFAS No. 91 deferred compensation allocated to each loan originated after completing the annual review and analysis of SFAS No. 91. Additionally, fewer loans were originated during fiscal 2007 in comparison to fiscal 2006, which also reduced deferred compensation attributable to the application of SFAS No. 91.

The increase in premises and occupancy expense was due primarily to a $175,000 charge incurred as a result of closing three loan production offices. The decrease in other operating expenses was primarily attributable to a $500,000 charitable contribution to capitalize the newly established Provident Savings Bank Charitable Foundation in the fourth quarter of fiscal 2006 (not replicated in fiscal 2007).

Income Taxes. The provision for income taxes was $9.1 million for fiscal 2007, representing an effective tax rate of 46.6%, as compared to $15.7 million in fiscal 2006, representing an effective tax rate of 44.4%. The increase in the effective tax rate was primarily the result of a higher percentage of permanent tax differences relative to income before taxes. The Corporation determined that the above tax rates meet its income tax obligations.

Average Balances, Interest and Average Yields/Costs

The following table sets forth certain information for the periods regarding average balances of assets and liabilities as well as the total dollar amounts of interest income from average interest-earning assets and interest expense on average interest-bearing liabilities and average yields and costs thereof. Such yields and costs for the periods indicated are derived by dividing income or expense by the average monthly balance of assets or liabilities, respectively, for the periods presented.

	Year Ended June 30,								
	2008			2007			2006		
	Average Balance	Interest	Average Yield/ Cost	Average Balance	Interest	Average Yield/ Cost	Average Balance	Interest	Average Yield/ Cost
(Dollars In Thousands)									
Interest-earning assets:									
Loans receivable, net (1)	$ 1,397,877	$ 86,340	6.18%	$ 1,446,781	$ 91,525	6.33%	$ 1,291,005	$ 77,821	6.03%
Investment securities	155,509	7,567	4.87%	175,439	7,149	4.07%	203,096	6,831	3.36%
FHLB – San Francisco stock	32,271	1,822	5.65%	41,588	2,225	5.35%	38,266	1,831	4.78%
Interest-earning deposits	588	20	3.40%	1,339	69	5.15%	3,722	144	3.87%
Total interest-earning assets	1,586,245	95,749	6.04%	1,665,147	100,968	6.06%	1,536,089	86,627	5.64%
Non interest-earning assets	36,531			37,959			45,185		
Total assets	$ 1,622,776			$ 1,703,106			$ 1,581,274		
Interest-bearing liabilities:									
Checking and money market accounts (2)	$ 198,445	1,607	0.81%	$ 206,147	1,524	0.74%	$ 226,317	1,286	0.57%
Savings accounts	146,858	2,896	1.97%	163,400	2,823	1.73%	223,162	3,151	1.41%
Time deposits	666,835	30,073	4.51%	576,952	26,867	4.66%	487,391	17,691	3.63%
Total deposits	1,012,138	34,576	3.42%	946,499	31,214	3.30%	936,870	22,128	2.36%

Borrowings	465,536	19,737	4.24%	599,286	28,031	4.68%	485,523	20,507	4.22%
Total interest-bearing liabilities	1,477,674	54,313	3.68%	1,545,785	59,245	3.83%	1,422,393	42,635	3.00%
Non interest-bearing liabilities	17,812			22,816			28,172		
Total liabilities	1,495,486			1,568,601			1,450,565		
Stockholders' equity	127,290			134,505			130,709		
Total liabilities and stockholders' equity	$ 1,622,776			$ 1,703,106			$ 1,581,274		
Net interest income		$ 41,436			$ 41,723			$ 43,992	
Interest rate spread (3)			2.36%			2.23%			2.64%
Net interest margin (4)			2.61%			2.51%			2.86%
Ratio of average interest-earning assets to average interest-bearing liabilities	107.35%			107.72%			107.99%		

(1) Includes receivable from sale of loans, loans held for sale and non-accrual loans, as well as net deferred loan cost amortization of $869, $589 and $363 for the years ended June 30, 2008, 2007 and 2006, respectively.
(2) Includes the average balance of non interest-bearing checking accounts of $44.7 million, $47.6 million and $54.5 million in fiscal 2008, 2007 and 2006, respectively.
(3) Represents the difference between the weighted average yield on total interest-earning assets and weighted average rate on total interest-bearing liabilities.
(4) Represents net interest income before provision for loan losses as a percentage of average interest-earning assets.

Yields Earned and Rates Paid

The following table sets forth (on a consolidated basis), for the periods and at the dates indicated, the weighted average yields earned on the Bank's assets and the weighted average interest rates paid on the Bank's liabilities, together with the net yield on interest-earning assets.

	Quarter Ended June 30,	Year Ended June 30,		
	2008	2008	2007	2006
Weighted average yield on:				
Loans receivable, net (1)	6.07%	6.18%	6.33%	6.03%
Investment securities	4.89%	4.87%	4.07%	3.36%
FHLB – San Francisco stock	6.29%	5.65%	5.35%	4.78%
Interest-earning deposits	1.56%	3.40%	5.15%	3.87%
Total interest-earning assets	5.96%	6.04%	6.06%	5.64%
Weighted average rate paid on:				
Checking and money market accounts (2)	0.66%	0.81%	0.74%	0.57%
Savings accounts	1.61%	1.97%	1.73%	1.41%
Time deposits	4.02%	4.51%	4.66%	3.63%
Borrowings	3.80%	4.24%	4.68%	4.22%
Total interest-bearing liabilities	3.26%	3.68%	3.83%	3.00%
Interest rate spread (3)	2.70%	2.36%	2.23%	2.64%
Net interest margin (4)	2.93%	2.61%	2.51%	2.86%

(1) Includes receivable from sale of loans, loans held for sale and non-accrual loans, as well as net deferred loan cost amortization of $869,000, $589,000 and $363,000 for the years ended June 30, 2008, 2007 and 2006, respectively.
(2) Includes the average balance of non interest-bearing checking accounts of $44.7 million, $47.6 million and $54.5 million in fiscal 2008, 2007 and 2006, respectively.
(3) Represents the difference between the weighted average yield on total interest-earning assets and weighted average rate on total interest-bearing liabilities.
(4) Represents net interest income before provision for loan losses as a percentage of average interest-earning assets.

Rate/Volume Analysis

The following table sets forth the effects of changing rates and volumes on interest income and expense of the Bank. Information is provided with respect to the effects attributable to changes in volume (changes in volume multiplied by prior rate), the effects attributable to changes in rate (changes in rate multiplied by prior volume) and changes that cannot be allocated between rate and volume.

	Year Ended June 30, 2008 Compared to Year Ended June 30, 2007 Increase (Decrease) Due to				Year Ended June 30, 2007 Compared to Year Ended June 30, 2006 Increase (Decrease) Due to			
(In Thousands)	Rate	Volume	Rate/ Volume	Net	Rate	Volume	Rate/ Volume	Net
Interest-earnings assets:								
Loans receivable, net (1)	$ (2,162)	$ (3,096)	$ 73	$ (5,185)	$ 3,844	$ 9,393	$ 467	$ 13,704
Investment securities	1,388	(811)	(159)	418	1,443	(929)	(196)	318
FHLB – San Francisco stock	123	(498)	(28)	(403)	216	159	19	394
Interest-earning deposits	(23)	(39)	13	(49)	48	(92)	(31)	(75)
Total net change in income on interest-earning assets	(674)	(4,444)	(101)	(5,219)	5,551	8,531	259	14,341
Interest-bearing liabilities:								
Checking and money market accounts	145	(57)	(5)	83	387	(115)	(34)	238
Savings accounts	399	(286)	(40)	73	706	(843)	(191)	(328)
Time deposits	(848)	4,189	(135)	3,206	5,003	3,251	922	9,176
Borrowings	(2,623)	(6,260)	589	(8,294)	2,200	4,801	523	7,524
Total net change in expense on interest-bearing liabilities	(2,927)	(2,414)	409	(4,932)	8,296	7,094	1,220	16,610
Net increase (decrease) in net interest income	$ 2,253	$ (2,030)	$ (510)	$ (287)	$ (2,745)	$ 1,437	$ (961)	$ (2,269)

(1) Includes receivable from sale of loans, loans held for sale and non-accrual loans.

Liquidity and Capital Resources

The Corporation's primary sources of funds are deposits, proceeds from the sale of loans originated for sale, proceeds from principal and interest payments on loans, proceeds from the maturity of investment securities and FHLB – San Francisco advances. While maturities and scheduled amortization of loans and investment securities are a relatively predictable source of funds, deposit flows, mortgage prepayments and loan sales are greatly influenced by general interest rates, economic conditions and competition.

The primary investing activity of the Bank is the origination and purchase of loans held for investment. During the fiscal years ended June 30, 2008, 2007 and 2006, the Bank originated loans in the amounts of $582.2 million, $1.42 billion and $1.75 billion, respectively. In addition, the Bank purchased loans from other financial institutions in fiscal 2008, 2007 and 2006 in the amounts of $99.8 million, $119.6 million and $111.7 million, respectively. Total loans sold in fiscal 2008, 2007 and 2006 were $373.5 million, $1.12 billion and $1.26 billion, respectively. At June 30, 2008, the Bank had loan origination commitments totaling $29.4 million and undisbursed loans in process totaling $7.9 million. The Bank anticipates that it will have sufficient funds available to meet its current loan origination commitments.

The Bank's primary financing activity is gathering deposits. During the fiscal years ended June 30, 2008, 2007 and 2006, the net increase (decrease) in deposits was $11.0 million, $80.1 million and ($2.4 million), respectively. On June 30, 2008, time deposits that are scheduled to mature in one year or less were $589.4 million. Historically, the Bank has been able to retain a significant amount of its time deposits as they mature by adjusting deposit rates to the current interest rate environment.

The Bank must maintain an adequate level of liquidity to ensure the availability of sufficient funds to support loan growth and deposit withdrawals, to satisfy financial commitments and to take advantage of investment opportunities. The Bank generally maintains sufficient cash and cash equivalents to meet short-term liquidity needs. At June 30, 2008, total cash and cash equivalents were $15.1 million, or 0.9% of total assets. Depending on market conditions and the pricing of deposit products and FHLB – San Francisco advances, the Bank may continue to rely on FHLB – San Francisco advances for part of its liquidity needs. As of June 30, 2008, the remaining available borrowing capacity at FHLB – San Francisco was $352.7 million, and the remaining available borrowing capacity at the Bank's correspondent bank was $25.0 million.

Although the OTS eliminated the minimum liquidity requirement for savings institutions in April 2002, the regulation still requires thrifts to maintain adequate liquidity to assure safe and sound operations. The Bank's average liquidity ratio (defined as the ratio of average qualifying liquid assets to average deposits and borrowings) for the quarter ended June 30, 2008 decreased to 4.6% from 7.2% during the same quarter ended June 30, 2007. The Bank augments its liquidity by maintaining sufficient borrowing capacity at FHLB – San Francisco and its correspondent bank.

The Bank is required to maintain specific amounts of capital pursuant to OTS requirements. Under the OTS prompt corrective action provisions, a minimum ratio of 1.5% for Tangible Capital is required in order to be deemed other than "critically undercapitalized," while a minimum ratio of 5.0% for Core Capital, 10.0% for Total Risk-Based Capital and 6.0% for Tier 1 Risk-Based Capital is required to be deemed "well capitalized." As of June 30, 2008, the Bank exceeded all regulatory capital requirements with Tangible Capital, Core Capital, Total Risk-Based Capital and Tier 1 Risk-Based Capital ratios of 7.2%, 7.2%, 12.3% and 11.0%, respectively.

Impact of Inflation and Changing Prices

The Corporation's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time as a result of inflation. The impact of inflation is reflected in the increasing cost of the Corporation's operations. Unlike most industrial companies, nearly all assets and liabilities of the Corporation are monetary. As a result, interest rates have a greater impact on the Corporation's performance than do the effects of general levels of inflation. In addition, interest rates do not necessarily move in the direction, or to the same extent, as the prices of goods and services.

Impact of New Accounting Pronouncements

Various elements of the Corporation's accounting policies, by their nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. In particular, management has identified several accounting policies that, as a result of the judgments, estimates and assumptions inherent in those policies, are important to an understanding of the financial statements of the Corporation. These policies relate to the methodology for the recognition of interest income, determination of the provision and allowance for loan and lease losses and the valuation of mortgage servicing rights and real estate held for sale. These policies and the judgments, estimates and assumptions are described in greater detail in Management's Discussion and Analysis of Financial Condition and Results of Operations section and in the section entitled "Summary of Significant Accounting Policies" contained in Note 1 of the Notes to the Consolidated Financial Statements. Management believes that the judgments, estimates and assumptions used in the preparation of the financial statements are appropriate based on the factual circumstances at the time. However, because of the sensitivity of the financial statements to these critical accounting policies, the use of other judgments, estimates and assumptions could result in material differences in the results of operations or financial condition.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Quantitative Aspects of Market Risk. The Bank does not maintain a trading account for any class of financial instrument nor does it purchase high-risk derivative financial instruments. Furthermore, the Bank is not subject to foreign currency exchange rate risk or commodity price risk. The primary market risk that the Bank faces is interest

rate risk. For information regarding the sensitivity to interest rate risk of the Bank's interest-earning assets and interest-bearing liabilities, see "Maturity of Loans Held for Investment," "Investment Securities Activities," "Time Deposits by Maturities" and "Interest Rate Risk" on pages 5, 24, 29 and 66, respectively, of this Form 10-K.

Qualitative Aspects of Market Risk. The Bank's principal financial objective is to achieve long-term profitability while reducing its exposure to fluctuating interest rates. The Bank has sought to reduce the exposure of its earnings to changes in interest rates by attempting to manage the repricing mismatch between interest-earning assets and interest-bearing liabilities. The principal element in achieving this objective is to increase the interest-rate sensitivity of the Bank's interest-earning assets by retaining for its portfolio new loan originations with interest rates subject to periodic adjustment to market conditions and by selling fixed-rate, single-family mortgage loans. In addition, the Bank maintains an investment portfolio, which is largely in U.S. government agency MBS and U.S. government sponsored enterprise MBS with contractual maturities of up to 30 years that reprice frequently. The Bank relies on retail deposits as its primary source of funds while utilizing FHLB – San Francisco advances as a secondary source of funding. Management believes retail deposits, unlike brokered deposits, reduce the effects of interest rate fluctuations because they generally represent a more stable source of funds. As part of its interest rate risk management strategy, the Bank promotes transaction accounts and time deposits with terms up to five years. For additional information, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" beginning on page 50 of this Form 10-K.

Interest Rate Risk. The principal financial objective of the Corporation's interest rate risk management function is to achieve long-term profitability while limiting its exposure to the fluctuation of interest rates. The Corporation, through its ALCO, has sought to reduce the exposure of its earnings to changes in interest rates by managing the repricing mismatch between interest-earning assets and interest-bearing liabilities. The principal element in achieving this objective is to manage the interest-rate sensitivity of the Corporation's assets by retaining loans with interest rates subject to periodic market adjustments. In addition, the Bank maintains a liquid investment portfolio primarily comprised of U.S. government agency MBS and government sponsored enterprise MBS that reprice frequently. The Bank relies on retail deposits as its primary source of funding while utilizing FHLB – San Francisco advances as a secondary source of funding which can be structured with favorable interest rate risk characteristics. As part of its interest rate risk management strategy, the Bank promotes transaction accounts.

Using data from the Bank's quarterly report to the OTS, the OTS produces a report for the Bank that measures interest rate risk by modeling the change in Net Portfolio Value ("NPV") over a variety of interest rate scenarios. The interest rate risk analysis received from the OTS is similar to the Bank's own interest rate risk model. NPV is defined as the net present value of expected future cash flows from assets, liabilities and off-balance sheet contracts. The calculation is intended to illustrate the change in NPV that would occur in the event of an immediate change in interest rates of -100, -50, +50, +100, +200 and +300 basis points with no effect given to any steps that management might take to counter the effect of the interest rate change.

The following table is provided by the OTS and sets forth as of June 30, 2008 the estimated changes in NPV based on the indicated interest rate environments. The Bank's balance sheet position as of June 30, 2008 can be summarized as follows: if interest rates increase or decrease, the NPV of the Bank is expected to decrease, except under the negative 50 basis point rate shock.

Basis Points (bp) Change in Rates	Net Portfolio Value	NPV Change (1)	Portfolio Value Assets	NPV as Percentage Of Portfolio Value Assets (2)	Sensitivity Measure (3)
(Dollars In Thousands)					
+300 bp	$ 110,093	$ (41,459)	$1,601,001	6.88%	-217bp
+200 bp	132,372	(19,180)	1,633,651	8.10%	-95bp
+100 bp	147,572	(3,980)	1,659,684	8.89%	-16bp
+50 bp	150,724	(828)	1,668,536	9.03%	-2bp
0 bp	151,552	-	1,674,896	9.05%	-bp
-50 bp	151,767	215	1,680,312	9.03%	-2bp
-100 bp	150,979	(573)	1,684,981	8.96%	-9bp

(1) Represents the (decrease) increase of the estimated NPV at the indicated change in interest rates compared to the NPV calculated at June 30, 2008 ("base case").

(2) Calculated as the estimated NPV divided by the portfolio value of total assets.

(3) Calculated as the change in the NPV ratio from the base case at the indicated change in interest rates.

The following table provided by the OTS, is based on the calculations contained in the previous table, and sets forth the change in the NPV at a +200 basis point rate shock at June 30, 2008 and 2007 (by regulation the Bank must measure and manage its interest rate risk for an interest rate shock of +/- 200 basis points, whichever produces the largest decline in NPV).

Risk Measure: +200 bp Rate Shock	At June 30, 2008 (+200 bp)	At June 30, 2007 (+200 bp)
Pre-Shock NPV Ratio	9.05%	9.84%
Post-Shock NPV Ratio	8.10%	8.31%
Sensitivity Measure	95 bp	153 bp
Thrift Bulletin 13a Level of Risk	Minimal	Minimal

As with any method of measuring interest rate risk, certain shortcomings are inherent in the method of analysis presented in the foregoing tables. For example, although certain assets and liabilities may have similar maturities or repricing characteristics, they may react in different degrees to changes in interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in interest rates, while interest rates on other types of assets and liabilities may lag behind changes in interest rates. Additionally, certain assets, such as ARM loans, have features which restrict changes on a short-term basis and over the life of the loan. Further, in the event of a change in interest rates, expected rates of prepayments on loans and early withdrawals of time deposits could likely deviate significantly from those assumed in calculating the respective results. It is also possible that, as a result of an interest rate increase, the increased mortgage payments required of ARM borrowers could result in an increase in delinquencies and defaults. Changes in interest rates could also affect the volume and profitability of the Bank's

mortgage banking operations. Accordingly, the data presented in the tables above should not be relied upon as indicative of actual results in the event of changes in interest rates. Furthermore, the NPV presented in the foregoing tables is not intended to present the fair market value of the Bank, nor does it represent amounts that would be available for distribution to stockholders in the event of the liquidation of the Corporation.

The Bank also models the sensitivity of net interest income for the 12-month period subsequent to any given month-end assuming a dynamic balance sheet (accounting for the Bank's current balance sheet, 12-month business plan, embedded options, rate floors, periodic caps, lifetime caps, and loan, investment, deposit and borrowing cash flows, among others), and immediate, permanent and parallel movements in interest rates of plus or minus 100 and 200 basis points. The following table describes the results of the analysis for June 30, 2008 and June 30, 2007.

June 30, 2008		June 30, 2007	
Basis Point (bp) Change in Rates	Change in Net Interest Income	Basis Point (bp) Change in Rates	Change in Net Interest Income
+200 bp	-9.78%	+200 bp	-0.97%
+100 bp	-5.29%	+100 bp	+3.76%
-100 bp	+3.62%	-100 bp	+11.52%
-200 bp	+8.58%	-200 bp	+11.18%

For the fiscal year ended June 30, 2008, the Bank is liability sensitive, as its interest-bearing liabilities expected to reprice during the subsequent 12-month period exceeded its interest-earning assets expected to reprice during that period. Therefore, in a rising interest rate environment, the model projects a decline in net interest income over the subsequent 12-month period. In a falling interest rate environment, the results project an increase in net interest income over the subsequent 12-month period. For the fiscal year ended June 30, 2007, the Bank is liability sensitive, as its interest-bearing liabilities expected to reprice during the subsequent 12-month period exceeded its interest-earning assets expected to reprice during that period. Therefore, in a rising interest rate environment, the model projects a decline in net interest income over the subsequent 12-month period, except in the +100 basis point scenario where net interest income is projected to increase. In a falling interest rate environment, the results project an increase in net interest income over the subsequent 12-month period.

Management believes that the assumptions used to complete the analysis described in the table above are reasonable. However, past experience has shown that immediate, permanent and parallel movements in interest rates will not necessarily occur. Additionally, while the analysis provides a tool to evaluate the projected net interest income to changes in interest rates, actual results may be substantially different if actual experience differs from the assumptions used to complete the analysis. Therefore the model results that we disclose should be thought of as a risk management tool to compare the trends of our current disclosure to previous disclosures, over time, within the context of the actual performance of the treasury yield curve.

Item 8. Financial Statements and Supplementary Data

Please refer to exhibit 13 beginning on page 76 for the Consolidated Financial Statements and Notes to Consolidated Financial Statements.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

a) An evaluation of the Corporation's disclosure controls and procedure (as defined in Section 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934 (the "Act")) was carried out under the supervision and with the participation of the Corporation's Chief Executive Officer, Chief Financial Officer and the Corporation's Disclosure Committee as of June 30, 2008, pursuant to the SEC rules. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing

disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. In April 2008, the Corporation identified material weaknesses in the internal controls governing the operation of the Corporation's ESOP, as described in Form 10-K/A for the fiscal year ended June 30, 2007. The Corporation implemented corrective actions in May 2008 which remediated the material weaknesses.

Based on their evaluation of the Corporation's financial statements and the corrective actions implemented regarding the Corporation's ESOP, the Corporation's Chief Executive Officer and Chief Financial Officer concluded that the Corporation's disclosure controls and procedures as of June 30, 2008 are effective in ensuring that the information required to be disclosed by the Corporation in the reports it files or submits under the Act is (i) accumulated and communicated to the Corporation's management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

b) There have been no other material changes in our internal control over financial reporting, other than the corrective actions implemented regarding the Corporations' ESOP, (as defined in Rule 13a-15(f) of the Act) that occurred during the fiscal year ended June 30, 2008, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. The Corporation does not expect that its internal control over financial reporting will prevent all error and all fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Corporation have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

Management Report on Internal Control Over Financial Reporting:

The management of Provident Financial Holdings, Inc. and subsidiary (the "Corporation") is responsible for establishing and maintaining adequate internal control over financial reporting. The Corporation's internal control over financial reporting was designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

To comply with the requirements of Section 404 of the Sarbanes–Oxley Act of 2002, the Corporation designed and implemented a structured and comprehensive assessment process to evaluate its internal control over financial reporting across the enterprise. The assessment of the effectiveness of the Corporation's internal control over financial reporting was based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Because of its inherent limitations, including the possibility of human error and the circumvention of overriding controls, a system of internal control over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Based on its assessment, management has concluded that the Corporation's internal control over financial reporting was effective as of June 30, 2008.

The effectiveness of internal control over financial reporting as of June 30, 2008, has been audited by Deloitte & Touche LLP, the independent registered public accounting firm who also audited the Corporation's consolidated financial statements. Deloitte & Touche LLP's attestation report on the Corporation's internal control over financial reporting follows.

Date: September 12, 2008

/s/ Craig G. Blunden
Craig G. Blunden
Chairman, President and Chief Executive Officer

/s/ Donavon P. Ternes
Donavon P. Ternes
Chief Operating Officer and Chief Financial Officer

Report of Independent Registered Public Accounting Firm:

To the Board of Directors and Stockholders of
Provident Financial Holdings, Inc.
Riverside, California

We have audited the internal control over financial reporting of Provident Financial Holdings, Inc. and subsidiary (the "Corporation") as of June 30, 2008, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Because management's assessment and our audit were conducted to meet the reporting requirements of Section 112 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA), management's assessment and our audit of the Corporation's internal control over financial reporting included controls over the preparation of the schedules equivalent to the basic financial statements in accordance with the instructions for the Office of Thrift Supervision Instructions for Thrift Financial Reports. The Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Corporation's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Corporation maintained, in all material respects, effective internal control over financial reporting as of June 30, 2008, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

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We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended June 30, 2008 of the Corporation and our report dated September 12, 2008 expressed an unqualified opinion on those financial statements.

/s/ DELOITTE & TOUCHE LLP

Costa Mesa, California
September 12, 2008

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

For information regarding the Corporation’s Board of Directors, see the section captioned “Proposal I – Election of Directors” which is included in the Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end, and is incorporated herein by reference.

The executive officers of the Corporation and the Bank are elected annually and hold office until their respective successors have been elected and qualified or until death, resignation or removal by the Board of Directors. For information regarding the Corporation’s executive officers, see Item 1 - “Executive Officers” beginning on page 39 of this Form 10-K.

Compliance with Section 16(a) of the Exchange Act

The information contained under the section captioned “Compliance with Section 16(a) of the Exchange Act” is included in the Corporation’s Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end, and is incorporated herein by reference.

Code of Ethics for Senior Financial Officers

The Corporation has adopted a Code of Ethics, which applies to all directors, officers, and employees of the Corporation. The Code of Ethics is publicly available as Exhibit 14 to the Corporation’s Annual Report on Form 10-K for the fiscal year June 30, 2007, and is available on the Corporation’s website, www.myprovident.com. If the Corporation makes any substantial amendments to the Code of Ethics or grants any waiver, including any implicit waiver, from a provision of the Code to the Corporation’s Chief Executive Officer, Chief Financial Officer or Controller, the Corporation will disclose the nature of such amendment or waiver on the Corporation’s website and in a report on Form 8-K.

Audit Committee Financial Expert

The Corporation has designated Joseph P. Barr, Audit Committee Chairman, as its audit committee financial expert. Mr. Barr is independent, as independence for audit committee members is defined under the listing standards of the NASDAQ Stock Market, a Certified Public Accountant in California and Ohio and has been practicing public

accounting for over 38 years.

Item 11. Executive Compensation

The information contained under the section captioned “Executive Compensation” and “Directors’ Compensation” is included in the Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later

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than 120 days after the Corporation’s fiscal year end, and incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

(a) Security Ownership of Certain Beneficial Owners.

The information contained under the section captioned "Security Ownership of Certain Beneficial Owners and Management" is included in the Corporation's Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end, and is incorporated herein by reference.

(b) Security Ownership of Management.

The information contained under the sections captioned "Security Ownership of Certain Beneficial Owners and Management" and "Proposal I -- Election of Directors" is included in the Corporation's Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end, and is incorporated herein by reference.

(c) Changes In Control.

The Corporation is not aware of any arrangements, including any pledge by any person of securities of the Corporation, the operation of which may at a subsequent date result in a change in control of the Corporation.

(d) Equity Compensation Plan Information.

The information contained under the section captioned “Executive Compensation – Equity Compensation Plan Information” is included in the Corporation’s Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end, and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information contained under the section captioned “Transactions with Management” is included in the Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end and is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

The information contained under the section captioned “Proposal II - Approval of Appointment of Independent Auditors” is included in the Corporation’s Proxy Statement, a copy of which will be filed with the Securities and Exchange Commission no later than 120 days after the Corporation’s fiscal year end and is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) 1. Financial Statements

See Exhibit 13 to Consolidated Financial Statements beginning on page 76.

2. Financial Statement Schedules

Schedules to the Consolidated Financial Statements have been omitted as the required information is

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inapplicable.

(b) Exhibits

Exhibits are available from the Corporation by written request

3.1 Certificate of Incorporation of Provident Financial Holdings, Inc. (Incorporated by reference to Exhibit 3.1 to the Corporation's Registration Statement on Form S-1 (File No. 333-2230))

3.2 Bylaws of Provident Financial Holdings, Inc. (Incorporated by reference to Exhibit 3.2 to the Corporation's Registration Statement on Form S-1 (File No. 333-2230))

10.1 Employment Agreement with Craig G. Blunden (Incorporated by reference to Exhibit 10.1 to the Corporation's Form 8-K dated December 19, 2005)

10.2 Post-Retirement Compensation Agreement with Craig G. Blunden (Incorporated by reference to Exhibit 10.2 to the Corporation's Form 8-K dated December 19, 2005)

10.3 1996 Stock Option Plan (incorporated by reference to Exhibit A to the Corporation's proxy statement dated December 12, 1996)

10.4 1996 Management Recognition Plan (incorporated by reference to Exhibit B to the Corporation's proxy statement dated December 12, 1996)

10.5 Form of Severance Agreement with Richard L. Gale, Kathryn R. Gonzales, Lilian Salter, Donavon P. Ternes and David S. Weiant (incorporated by reference to Exhibit 10.1 in the Corporation's Form 8-K dated July 3, 2006)

10.6 2003 Stock Option Plan (incorporated by reference to Exhibit A to the Corporation's proxy statement dated October 21, 2003)

10.7 Form of Incentive Stock Option Agreement for options granted under the 2003 Stock Option Plan (incorporated by reference to Exhibit 10.13 to the Corporation's Annual Report on Form 10-K for the fiscal year June 30, 2005).

10.8 Form of Non-Qualified Stock Option Agreement for options granted under the 2003 Stock Option Plan (incorporated by reference to Exhibit 10.14 to the Corporation's Annual Report on Form 10-K for the fiscal year June 30, 2005).

10.9 2006 Equity Incentive Plan (incorporated by reference to Exhibit A to the Corporation's proxy statement dated October 12, 2006)

10.10 Form of Incentive Stock Option Agreement for options granted under the 2006 Equity Incentive Plan (incorporated by reference to Exhibit 10.10 in the Corporation's Form 10-Q for the quarter ended December 31, 2006)

10.11 Form of Non-Qualified Stock Option Agreement for options granted under the 2006 Equity Incentive Plan (incorporated by reference to Exhibit 10.11 in the Corporation's Form 10-Q for the quarter ended December 31, 2006)

10.12

	Form of Restricted Stock Agreement for restricted shares awarded under the 2006 Equity Incentive Plan (incorporated by reference to Exhibit 10.12 in the Corporation's Form 10-Q for the quarter ended December 31, 2006)
13	2008 Annual Report to Stockholders
14	Code of Ethics for the Corporation's directors, officers and employees

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21.1	Subsidiaries of Registrant
23.1	Consent of Independent Registered Public Accounting Firm
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
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Date: September 12, 2008

Provident Financial Holdings, Inc.

/s/ Craig G. Blunden
Craig G. Blunden
Chairman, President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

SIGNATURES	TITLE	DATE
/s/Craig G. Blunden Craig G. Blunden	Chairman, President and Chief Executive Officer (Principal Executive Officer)	September 12, 2008
/s/Donavon P. Ternes Donavon P. Ternes	Chief Operating Officer and Chief Financial Officer (Principal Financial and Accounting Officer)	September 12, 2008
/s/Joseph P. Barr Joseph P. Barr	Director	September 12, 2008
/s/Bruce W. Bennett Bruce W. Bennett	Director	September 12, 2008
/s/Debbi H. Guthrie Debbi H. Guthrie	Director	September 12, 2008

/s/Robert G. Schrader		
Robert G. Schrader	Director	September 12, 2008
/s/Roy H. Taylor		
Roy H. Taylor	Director	September 12, 2008
/s/William E. Thomas		
William E. Thomas	Director	September 12, 2008

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EXHIBIT INDEX

Exhibit 13	2008 Annual Report to Stockholders
Exhibit 23.1	Consent of Independent Registered Public Accounting Firm
Exhibit 31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

EXHIBIT 13

2008 Annual Report to Stockholders

2008 Annual Report

Message From the Chairman

Dear Shareholders:

I am pleased to forward our Annual Report for fiscal 2008, although I am disappointed with our results. We reported net income of $860,000 or $0.14 per diluted share, significantly lower than last year and reflective of the current challenges facing the financial services industry. The operating environment in fiscal 2008 was the most demanding in memory, made difficult by the poor economic conditions and deterioration of credit quality. Consequently, the Board of Directors made the tough decision to lower the most recent quarterly cash dividend to $0.05 per share. Additionally, the Company significantly reduced its common stock repurchase activity to 187,000 shares in fiscal 2008 from 665,000 shares in fiscal 2007. Both of these actions were taken to preserve the Company's capital levels and capital ratios given the uncertain operating environment. The Bank is considered "well-capitalized" by its primary regulator and the Company believes that these actions will support the Bank's favorable designation.
Although the Company quickly responded to pressing issues arising from the unfavorable operating environment, long-term strategies were not forgotten. Last year, I described five initiatives for fiscal 2008, four for Provident Bank and one for Provident Bank Mortgage.
I am pleased to report that we made progress in connection with three of the four initiatives at Provident Bank, albeit tempered by the operating environment. Specifically, loans held for investment grew by a modest 1% during the year while operating expenses declined significantly, by 13%, from the prior year. Additionally, total deposits grew by 1%, although transaction account balances declined by the same percentage. The slight decline in our transaction account balances did not accomplish the growth we intended. Our success in fulfilling the final initiative, making sound capital management decisions, was described in the first paragraph and demonstrated by maintaining prudent capital levels in a stressed operating environment.
The breakeven operating results initiative for Provident Bank Mortgage during fiscal 2008 was not met, although significant actions were taken throughout the year to respond to deteriorating business conditions. We reduced our origination capacity by closing six loan production offices and reducing the number of employees. As a result, operating expenses attributable to the division declined by approximately 34%, a significant improvement. Tighter underwriting standards were adopted during the course of the fiscal year consistent with investor requirements and our expertise in FHA loan products was enhanced since a larger percentage of origination volume is being generated in this product.

Provident Bank
We remain committed to the strategies implemented in prior years that we believe will improve our fundamental performance over time, although our fiscal 2009 outlook for meaningful improvement is guarded since the current operating environment is very challenging. Therefore, we have prepared our Business Plan to preserve capital, limit asset growth and maintain the Bank's "well-capitalized" regulatory capital designation.
We continue to explore branching opportunities within our geographic footprint and have identified several sites that may meet our criteria. In keeping with this strategy, we opened a new branch location in the La Sierra area of Riverside in January 2007, which has grown to $11.1 million in deposits at June 30, 2008. Additionally, in September 2008 we opened a second branch location in Moreno Valley. If you are a member of that community, please look for our grand opening information and drop by our newest branch.

Provident Bank Mortgage
Fiscal 2008 turned out to be a poor year for our mortgage banking business requiring significant modifications in our operating model, described earlier. I believe that we have made the changes necessary to position the division for

improved operating results in fiscal 2009. Loan sale margins have returned to historically profitable levels and loan origination volumes have stabilized, which we believe is commensurate with our operating expense structure. We are prepared to make additional changes that become necessary and we will be diligent in making them. Those changes may be in the form of a different product mix, further tightening of our underwriting standards, a further reduction in our operating expenses or a combination of these and other changes.

Message From the Chairman

A Final Word

I began my message by describing that I am disappointed with our fiscal 2008 operating results. However, I wish to point out that I am pleased with the actions we took during the course of the fiscal year because in some respects, we begin fiscal 2009 in a better position than the start of last year. For instance, much of the heavy-lifting regarding operating expense reductions have been completed and we will realize a full year's benefit of those actions. Additionally, we begin the year with a significantly higher net interest margin than last year and a significantly steeper yield curve, which historically, is a favorable situation for thrifts. I remain cautious though because the Southern California real estate market is under significant stress, which will negatively impact many of our borrowers if they experience financial difficulty. While I believe we have sufficient resources to withstand any elevated credit quality costs, those costs may also affect our earnings. As a result, we will concentrate our efforts on risk management and mitigation laying the foundation for the Company's future growth once the operating environment becomes more favorable.

Sincerely,

/s/ Craig G. Blunden
Craig G. Blunden
Chairman, President and
Chief Executive Officer

Message From the Chairman

Message From the Chairman

Message From the Chairman

Financial Highlights

The following tables set forth information concerning the consolidated financial position and results of operations of the Corporation and its subsidiary at the dates and for the periods indicated.

	At or For The Year Ended June 30,				
	2008	2007	2006	2005	2004
(In Thousands, Except Per Share Information)					
FINANCIAL CONDITION DATA:					
Total assets	$ 1,632,447	$ 1,648,923	$ 1,624,452	$ 1,634,690	$ 1,320,939
Loans held for investment, net	1,368,137	1,350,696	1,264,979	1,134,473	864,439
Loans held for sale	28,461	1,337	4,713	5,691	20,127
Receivable from sale of loans	-	60,513	99,930	167,813	86,480
Cash and cash equivalents	15,114	12,824	16,358	25,902	38,349
Investment securities	153,102	150,843	177,189	232,432	252,580
Deposits	1,012,410	1,001,397	921,279	923,670	854,798
Borrowings	479,335	502,774	546,211	560,845	324,877
Stockholders' equity	123,980	128,797	136,148	122,965	109,977
Book value per share	19.97	20.20	19.47	17.68	15.51
OPERATING DATA:					
Interest income	$ 95,749	$ 100,968	$ 86,627	$ 75,495	$ 62,151
Interest expense	54,313	59,245	42,635	33,048	25,957
Net interest income	41,436	41,723	43,992	42,447	36,194
Provision for loan losses	13,108	5,078	1,134	1,641	819
Net interest income after provision	28,328	36,645	42,858	40,806	35,375
Loan servicing and other fees	1,776	2,132	2,572	1,675	2,292
Gain on sale of loans, net	1,004	9,318	13,481	18,706	14,346
Deposit account fees	2,954	2,087	2,093	1,789	1,986
Net gain on sale of investment securities	-	-	-	384	-
Net gain on sale of real estate held for investment	-	2,313	6,335	-	-
(Loss) gain on sale and operations of real estate owned acquired in the settlement of loans, net	(2,683)	(117)	20	-	171
Other non-interest income	2,160	1,828	1,708	1,864	1,358

Operating expenses	30,311	34,631	33,755	33,341	29,261
Income before income taxes	3,228	19,575	35,312	31,883	26,267
Provision for income taxes	2,368	9,124	15,676	14,077	11,717
Net income	$ 860	$ 10,451	$ 19,636	$ 17,806	$ 14,550
Basic earnings per share	$ 0.14	$ 1.59	$ 2.93	$ 2.68	$ 2.16
Diluted earnings per share	$ 0.14	$ 1.57	$ 2.82	$ 2.49	$ 2.01
Cash dividend per share	$ 0.64	$ 0.69	$ 0.58	$ 0.52	$ 0.33

Financial Highlights

	At or For The Year Ended June 30,				
	2008	2007	2006	2005	2004
KEY OPERATING RATIOS:					
Performance Ratios					
Return on average assets	0.05%	0.61%	1.24%	1.19%	1.13%
Return on average stockholders' equity	0.68	7.77	15.02	15.33	13.64
Interest rate spread	2.36	2.23	2.64	2.80	2.83
Net interest margin	2.61	2.51	2.86	2.95	2.97
Average interest-earning assets to average interest-bearing liabilities	107.35	107.72	107.99	106.65	106.65
Operating and administrative expenses as a percentage of average total assets	1.87	2.03	2.13	2.24	2.28
Efficiency ratio	64.98	58.42	48.08	49.86	51.93
Stockholders’ equity to total assets ratio	7.59	7.81	8.38	7.52	8.33
Dividend payout ratio	457.14	43.95	20.57	20.88	16.42
Regulatory Capital Ratios					
Tangible capital	7.19%	7.62%	8.08%	6.56%	6.90%
Tier 1 leverage capital	7.19	7.62	8.08	6.56	6.90
Total risk-based capital	12.25	12.49	13.37	11.21	12.39
Tier 1 risk-based capital	10.99	11.39	12.36	10.29	11.40
Asset Quality Ratios					
Non-accrual and 90 days or more past due loans as a percentage of loans held for investment, net	1.70%	1.18%	0.20%	0.05%	0.13%
Non-performing assets as a percentage of total assets	1.99	1.20	0.16	0.04	0.08
Allowance for loan losses as a percentage of gross loans held for investment	1.43	1.09	0.81	0.81	0.87
Allowance for loan losses as a					

percentage of non-performing loans	85.79	93.32	407.71	1,561.86	701.75
Net charge-offs to average loans receivable, net	0.58	0.04	-	-	0.05

Consolidated Financial Statements of
Provident Financial Holdings, Inc.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Provident Financial Holdings, Inc.
Riverside, California

We have audited the accompanying consolidated statements of financial condition of Provident Financial Holdings, Inc. and subsidiary (the "Corporation") as of June 30, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended June 30, 2008. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Provident Financial Holdings, Inc. and subsidiary as of June 30, 2008 and 2007, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 2008, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Corporation's internal control over financial reporting as of June 30, 2008, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated September 12, 2008 expressed an unqualified opinion on the Corporation's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Costa Mesa, California
September 12, 2008

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Consolidated Statements of Financial Condition

(In Thousands, Except Share Information)

	June 30,	
	2008	2007
Assets		
Cash and cash equivalents	$ 15,114	$ 12,824
Investment securities – held to maturity (fair value $ - and $18,837, respectively)	-	19,001
Investment securities – available for sale, at fair value	153,102	131,842
Loans held for investment, net of allowance for loan losses of $19,898 and $14,845, respectively	1,368,137	1,350,696
Loans held for sale, at lower of cost or market	28,461	1,337
Receivable from sale of loans	-	60,513
Accrued interest receivable	7,273	7,235
Real estate owned, net	9,355	3,804
Federal Home Loan Bank (“FHLB”) – San Francisco stock	32,125	43,832
Premises and equipment, net	6,513	7,123
Prepaid expenses and other assets	12,367	10,716
Total assets	$ 1,632,447	$ 1,648,923
Liabilities and Stockholders’ Equity		
Liabilities:		
Non interest-bearing deposits	$ 48,056	$ 45,112
Interest-bearing deposits	964,354	956,285
Total deposits	1,012,410	1,001,397
Borrowings	479,335	502,774
Accounts payable, accrued interest and other liabilities	16,722	15,955
Total liabilities	1,508,467	1,520,126
Commitments and contingencies (Note 14)		
Stockholders’ equity:		
Preferred stock, $0.01 par value (2,000,000 shares authorized; none issued and outstanding)	-	-
Common stock, $0.01 par value (15,000,000 shares authorized; 12,435,865 and 12,428,365 shares issued, respectively; 6,207,719 and 6,376,945 shares outstanding, respectively)	124	124
Additional paid-in capital	75,164	72,935
Retained earnings	143,053	146,194
Treasury stock at cost (6,228,146 and 6,051,420 shares, respectively)	(94,798)	(90,694)

Unearned stock compensation		(102)		(455)
Accumulated other comprehensive income, net of tax		539		693
Total stockholders’ equity		123,980		128,797
Total liabilities and stockholders’ equity	$	1,632,447	$	1,648,923

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

Consolidated Statements of Operations

(In Thousands, Except Share Information)

	Year Ended June 30,		
	2008	2007	2006
Interest income:			
Loans receivable, net	$ 86,340	$ 91,525	$ 77,821
Investment securities	7,567	7,149	6,831
FHLB – San Francisco stock	1,822	2,225	1,831
Interest-earning deposits	20	69	144
Total interest income	95,749	100,968	86,627
Interest expense:			
Deposits	34,576	31,214	22,128
Borrowings	19,737	28,031	20,507
Total interest expense	54,313	59,245	42,635
Net interest income, before provision for loan losses	41,436	41,723	43,992
Provision for loan losses	13,108	5,078	1,134
Net interest income, after provision for loan losses	28,328	36,645	42,858
Non-interest income:			
Loan servicing and other fees	1,776	2,132	2,572
Gain on sale of loans, net	1,004	9,318	13,481
Deposit account fees	2,954	2,087	2,093
Gain on sale of real estate held for investment	-	2,313	6,335
(Loss) gain on sale and operations of real estate owned acquired in the settlement of loans, net	(2,683)	(117)	20
Other	2,160	1,828	1,708
Total non-interest income	5,211	17,561	26,209
Non-interest expense:			
Salaries and employee benefits	18,994	22,867	21,384
Premises and occupancy	2,830	3,314	3,036
Equipment expense	1,552	1,570	1,689
Professional expense	1,573	1,193	1,317
Sales and marketing expense	524	945	1,125
Deposit insurance premium and regulatory assessments	804	434	436
Other	4,034	4,308	4,768
Total non-interest expense	30,311	34,631	33,755
Income before income taxes	3,228	19,575	35,312
Provision for income taxes	2,368	9,124	15,676
Net income	$ 860	$ 10,451	$ 19,636
Basic earnings per share	$ 0.14	$ 1.59	$ 2.93
Diluted earnings per share	$ 0.14	$ 1.57	$ 2.82
Cash dividends per share	$ 0.64	$ 0.69	$ 0.58

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

Consolidated Statements of Stockholders' Equity
(In Thousands, Except Share Information)

	Common Stock						Accumulat-ed Other	
	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Unearned Stock Compensation	Comprehen-sive Income (Loss), Net of Tax	Total
Balance at July 1, 2005	6,956,815	$ 120	$ 61,212	$ 124,791	$ (62,046)	$ (1,421)	$ 309	$ 122,965
Comprehensive income:								
Net income				19,636				19,636
Unrealized holding loss on securities available for sale, net of tax benefit of $ (521)							(720)	(720)
Total comprehensive income								18,916
Purchase of treasury stock	(367,169)				(10,437)			(10,437)
Purchase of restricted stock from employees in lieu of distribution	(1,436)				(41)			(41)
Exercise of stock options	403,632	4	2,929					2,933
Reclassification of unearned restricted stock			(155)			155		-
Amortization of restricted stock			92					92
Stock options expense			394					394
Tax benefit from non-qualified equity compensation			2,572					2,572
Allocation of contributions to ESOP			2,396			412		2,808
Cash dividends				(4,054)				(4,054)
Balance at June 30, 2006	6,991,842	124	69,440	140,373	(72,524)	(854)	(411)	136,148
Comprehensive income:								
Net income				10,451				10,451
Unrealized holding gain on securities available for sale, net of tax expense of $799							1,104	1,104
Total comprehensive income								11,555
Purchase of treasury stock	(664,594)				(18,652)			(18,652)
	(1,696)				(51)			(51)

Purchase of restricted stock from employees in lieu of distribution								
Exercise of stock options	51,393		1,017					1,017
Amortization of restricted stock			165					165
Awards of restricted stock			(533)		533			-
Stock options expense			462					462
Tax benefit from non-qualified equity compensation			81					81
Allocation of contributions to ESOP			2,303			399		2,702
Cash dividends				(4,630)				(4,630)
Balance at June 30, 2007	6,376,945	124	72,935	146,194	(90,694)	(455)	693	128,797

(continued)

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

Consolidated Statements of Stockholders' Equity
(In Thousands, Except Share Information)

	Common Stock						Accumulat-ed Other	
	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Unearned Stock Compensation	Comprehen-sive Income (Loss), Net of Tax	Total
Balance at July 1, 2007	6,376,945	124	72,935	146,194	(90,694)	(455)	693	128,797
Comprehensive income:								
Net income				860				860
Unrealized holding loss on securities available for sale, net of tax benefit of $ (112)							(154)	(154)
Total comprehensive income								706
Purchase of treasury stock	(187,081)				(4,075)			(4,075)
Purchase of restricted stock from employees in lieu of distribution	(995)				(22)			(22)
Exercise of stock options	7,500		69					69
Distribution of restricted stock	11,350							-
Amortization of restricted stock			281					281
Awards of restricted stock			(45)		45			-
Forfeiture of restricted stock			52		(52)			-
Stock options expense			742					742
Tax benefit from non-qualified equity compensation			6					6
Allocation of contributions to ESOP			1,124			353		1,477
Cash dividends				(4,001)				(4,001)

Balance at June 30, 2008	6,207,719	$ 124	$ 75,164	$ 143,053	$ (94,798)	$ (102)	$ 539	$ 123,980

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

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Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended June 30, 2008	2007	2006
Cash flows from operating activities:			
Net income	$ 860	$ 10,451	$ 19,636
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	2,366	2,212	3,195
Provision for loan losses	13,108	5,078	1,134
Provision for losses on real estate owned	517	-	-
Gain on sale of loans	(1,004)	(9,318)	(13,481)
Net loss (gain) on sale of real estate	932	(2,359)	(6,355)
Stock-based compensation	2,410	3,082	2,968
FHLB – San Francisco stock dividend	(1,892)	(2,154)	(1,757)
Deferred income taxes	(5,486)	164	(2,049)
Tax benefit from non-qualified equity compensation	(6)	(81)	(2,572)
Increase (decrease) in accounts payable, accrued interest and other liabilities	3,587	(6,435)	(1,091)
Increase in prepaid expenses and other assets	(2,366)	(1,764)	(3,096)
Loans originated for sale	(398,726)	(1,126,616)	(1,237,806)
Proceeds from sale of loans and net change in receivable from sale of loans	433,752	1,176,489	1,301,586
Net cash provided by operating activities	48,052	48,749	60,312
Cash flows from investing activities:			
Net increase in loans held for investment	(49,210)	(94,375)	(113,853)
Maturities and calls of investment securities held to maturity	19,000	32,030	1,200
Maturities and calls of investment securities available for sale	9,979	12,434	3,000
Principal payments from mortgage backed securities	47,457	40,089	49,020
Purchases of investment securities available for sale	(78,935)	(56,539)	-
Purchases of FHLB – San Francisco stock	(39)	(4,093)	(896)
Redemption of FHLB – San Francisco stock	13,638	-	2,198
Sales of real estate	13,125	4,829	16,051
Purchases of premises and equipment	(395)	(1,235)	(688)
Net cash used for investing activities	$ (25,380)	$ (66,860)	$ (43,968)

(continued)

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

Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended June 30,		
	2008	2007	2006
Cash flows from financing activities:			
Net increase (decrease) in deposits	$ 11,013	$ 80,118	$ (2,391)
Proceeds from (repayments of) short-term borrowings, net	18,600	(38,400)	(17,600)
Proceeds of long-term borrowings	110,000	45,000	30,000
Repayments of long-term borrowings	(152,039)	(50,037)	(27,034)
ESOP loan payment	67	131	164
Treasury stock purchases	(4,097)	(18,703)	(10,478)
Exercise of stock options	69	1,017	2,933
Tax benefit from non-qualified equity compensation	6	81	2,572
Cash dividends	(4,001)	(4,630)	(4,054)
Net cash (used for) provided by financing activities	(20,382)	14,577	(25,888)
Net increase (decrease) in cash and cash equivalents	2,290	(3,534)	(9,544)
Cash and cash equivalents at beginning of year	12,824	16,358	25,902
Cash and cash equivalents at end of year	$ 15,114	$ 12,824	$ 16,358
Supplemental information:			
Cash paid for interest	$ 54,618	$ 58,961	$ 42,501
Cash paid for income taxes	$ 4,900	$ 10,550	$ 16,200
Transfer of loans held for investment to loans held for sale	$ -	$ -	$ 18,472
Transfer of loans held for sale to loans held for investment	$ 10,369	$ 21,624	$ 6,827
Real estate acquired in the settlement of loans	$ 28,006	$ 5,902	$ 411

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

Notes to Consolidated Financial Statements

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1. Summary of Significant Accounting Policies:

Provident Savings Bank, F.S.B. (the "Bank") converted from a federally chartered mutual savings bank to a federally chartered stock savings bank effective June 27, 1996. Provident Financial Holdings, Inc., a Delaware corporation organized by the Bank, acquired all of the capital stock of the Bank issued in the conversion; the transaction was recorded on a book value basis.

The consolidated financial statements include the accounts of Provident Financial Holdings, Inc., and its wholly owned subsidiary, Provident Savings Bank, F.S.B. (collectively, the "Corporation"). All inter-company balances and transactions have been eliminated.

The Corporation operates in two business segments: community banking (Provident Bank) and mortgage banking (Provident Bank Mortgage ("PBM"), a division of Provident Bank). Provident Bank activities include attracting deposits, offering banking services and originating multi-family, commercial real estate, construction, commercial business and consumer loans. Deposits are collected primarily from 13 banking locations located in Riverside and San Bernardino counties in California. PBM activities include originating single-family loans (first mortgage, one-to-four units), second mortgages and equity lines of credit for sale to investors or held for investment. Loans are primarily originated in Southern California by loan agents employed by the Bank, as well as from the banking locations and freestanding lending offices. PBM originates loans from three freestanding lending offices in Southern California and one free standing lending office in Northern California, as well as from the banking locations.

The accounting and reporting policies of the Corporation conform to accounting principles generally accepted in the United States of America. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of deferred tax assets, the valuation of loan servicing assets, the valuation of REOs, the determination of the loan repurchase reserve and the valuation of derivative financial instruments.

The following accounting policies, together with those disclosed elsewhere in the consolidated financial statements, represent the significant accounting policies of Provident Financial Holdings, Inc. and the Bank.

Cash and cash equivalents
Cash and cash equivalents include cash on hand and due from banks, as well as overnight deposits placed at correspondent banks.

Investment securities
The Corporation classifies its qualifying investments as available for sale or held to maturity. The Corporation's policy of classifying investments as held to maturity is based upon its ability and management's positive intent to hold such securities to maturity. Securities expected to be held to maturity are carried at amortized historical cost. All other securities are classified as available for sale and are carried at fair value. Fair value is determined based upon quoted market prices. Unrealized holding gains and losses on securities available for sale are included in accumulated

other comprehensive income, net of tax. Gains and losses on dispositions of investment securities are included in non-interest income and are determined using the specific identification method. Purchase premiums and discounts are amortized over the expected average life of the securities using the effective interest method. Declines in the fair value of held to maturity and available for sale securities below their amortized historical cost that are deemed to be other than temporary are reflected in earnings as realized losses.

Notes to Consolidated Financial Statements

Loans
Loans held for investment consist primarily of long-term loans secured by first trust deeds on single-family residences, other residential property, commercial property and land. The single-family adjustable-rate mortgage ("ARM") is the Corporation's primary loan investment. Additionally, multi-family, commercial real estate, construction, and to a lesser extent, commercial business and consumer loans, are becoming a substantial part of loans held for investment. These loans are generally offered to customers and businesses located in Southern California, primarily in Riverside and San Bernardino counties, commonly known as the Inland Empire, and to a lesser extent in Orange, Los Angeles, San Diego and other counties, including Alameda county and surrounding counties in Northern California. Further deterioration in the economic conditions of these markets could adversely affect the Corporation's business, financial condition and profitability. Such further deterioration could give rise to increased loan delinquencies, an increase in problem assets and foreclosures, decreased loan demand and a decline in real estate values.

Loan origination fees and certain direct origination expenses are deferred and amortized to interest income over the contractual life of the loan using the effective interest method. The amortization is discontinued for non-performing loans. Interest receivable represents, for the most part, the current month's interest, which will be included as a part of the borrower's next monthly loan payment. Interest receivable is accrued only if deemed collectible. Loans are deemed to be in non-accrual status when they become 90 days past due or if the loan is deemed impaired. When a loan is placed on non-accrual status, interest accrued but not received is reversed against interest income. Interest income on non-accrual loans is subsequently recognized only to the extent that cash is received and the loans' principal balance is deemed collectible. Non-accrual loans that become current as to both principal and interest are returned to accrual status after demonstrating satisfactory payment history and when future payments are expected to be collected.

Receivable from sale of loans
Receivable from sale of loans represents expected settlement proceeds from the sale of loans, which have closed but have not settled. The duration of the loan sale settlement generally ranges from three to 30 days.

PBM (Provident Bank Mortgage) activities
Loans are originated for both investment and sale in the secondary market. Since the Corporation is primarily an adjustable-rate mortgage and consumer lender for its own portfolio, most fixed-rate loans are originated for sale to institutional investors.

Loans held for sale are carried at the lower of cost or fair value. Fair value is generally determined by outstanding commitments from investors or investors' current yield requirements as calculated on the aggregate loan basis. Loans are generally sold without recourse, other than standard representations and warranties, except those loans sold to the FHLB – San Francisco under the Mortgage Partnership Finance ("MPF") program which has a specific recourse provision. Most loans are sold on a servicing released basis. In some transactions, primarily loans sold under the MPF program, the Corporation may retain the servicing rights in order to generate servicing income. Where the Corporation continues to service loans after sale, investors are paid their share of the principal collections together with interest at an agreed-upon rate, which generally differs from the loan's contractual interest rate.

As described in the preceding paragraph, loans sold to the FHLB – San Francisco under the MPF program have a recourse liability. The FHLB – San Francisco absorbs the first four basis points of loss and a credit scoring process is

used to calculate the maximum recourse amount for the Bank. All losses above the Bank's maximum recourse are the responsibility of the FHLB – San Francisco. The FHLB – San Francisco pays the Bank a credit enhancement fee on a monthly basis to compensate the Bank for accepting the recourse obligation. As of June 30, 2008, the Bank has

Notes to Consolidated Financial Statements

$150.9 million of loans outstanding under this program and has established a recourse liability of $166,000 as compared to $173.2 million of loans outstanding and a recourse liability of $191,000 at June 30, 2007. As of June 30, 2008, no losses had been experienced in this program.

Occasionally, the Bank is required to repurchase loans sold to Freddie Mac, Fannie Mae or other institutional investors if it is determined that such loans do not meet the credit requirements of the investor, or if one of the parties involved in the loan misrepresented pertinent facts, committed fraud, or if such loans were 90-days past due within 120 days of the loan funding date. During the year ended June 30, 2008, the Bank repurchased $4.5 million of single-family mortgage loans as compared to $14.6 million in fiscal 2007 and $2.0 million in fiscal 2006. In addition to the specific recourse liability for the MPF program, the Bank has established a recourse liability of $1.9 million and $194,000 for loans sold to other investors as of June 30, 2008 and 2007, respectively.

Activity in the recourse liability for the years ended June 30, 2008 and 2007 was as follows:

(In Thousands)	2008	2007
Balance, beginning of year	$ 385	$ 222
Provision	1,688	163
Balance, end of the year	$ 2,073	$ 385

The Bank is obligated to refund loan sale premiums to investors when loans pay off within a specific time period following the loan sale; the time period ranges from three to six months, depending upon the sale agreement. Total loan sale premium (recovery) refunds in fiscal 2008, 2007 and 2006 were $(25,000), $358,000 and $648,000, respectively. As of June 30, 2008 and 2007, the Bank has an outstanding liability of $52,000 and $149,000, respectively, for future loan sale premium refunds.

Gains or losses on the sale of loans, including fees received or paid, are recognized at the time of sale and are determined by the difference between the net sales proceeds and the allocated book value of the loans sold. When loans are sold with servicing retained, the carrying value of the loans is allocated between the portion sold and the portion retained (i.e., servicing assets and interest-only strips), based on estimates of their relative fair values.

Servicing assets are amortized in proportion to and over the period of the estimated net servicing income and are carried at the lower of cost or fair value. The fair value of servicing assets is based on the present value of estimated net future cash flows related to contractually specified servicing fees. The Bank periodically evaluates servicing assets for impairment, which is measured as the excess of cost over fair value. This review is performed on a disaggregated basis, based on loan type and interest rate. In estimating fair values at June 30, 2008 and 2007, the Bank used a weighted average Constant Prepayment Rate ("CPR") of 8.58% and 3.53%, respectively, and a weighted-average discount rate of 9.00% for both periods. Servicing assets, which are included in Other Assets in the accompanying Consolidated Statements of Financial Condition, had a carrying value of $673,000 and a fair value of $1.4 million at June 30, 2008. Servicing assets at June 30, 2007 had a carrying value of $991,000 and a fair value of $2.0 million. There were no impairment allowances required for the servicing assets as of June 30, 2008 and 2007. Total additions to loan servicing assets during the fiscal years ended June 30, 2008 and 2007 were $21,000 and $33,000, respectively. Total amortization of the loan servicing assets during fiscal years ended June 30, 2008, 2007 and 2006 were $339,000, $421,000 and $473,000, respectively.

Rights to future income from serviced loans that exceed contractually specified servicing fees are recorded as interest-only strips. Interest-only strips are carried at fair value, utilizing the same assumptions that are used to value the related servicing assets, with any unrealized gain or loss, net of tax, recorded as a component of accumulated other comprehensive income. Interest-only strips are included in Other Assets in the accompanying Consolidated Statements of Financial Condition and had a fair value of $419,000, gross unrealized gains of $286,000 and an unamortized cost of $133,000 at June 30, 2008. Interest-only strips at June 30, 2007 had a fair value of $603,000, gross unrealized gains of $378,000 and an unamortized cost of $225,000. There were no

additions to interest-only strips during fiscal 2008, while $5,000 was added during fiscal 2007. Total amortization of the interest-only strips during fiscal years ended June 30, 2008, 2007 and 2006 were $92,000, $105,000 and $114,000, respectively.

During the years ended June 30, 2008, 2007 and 2006, the Corporation sold 48%, 38% and 26%, respectively, of its loans originated for sale to a single primary investor. If the Corporation is unable to sell loans to its primary investor, find alternative investors, or change its loan programs to meet investor guidelines, it may have a significant negative impact on the Corporation's operations.

During the first half of fiscal 2008, the Bank closed the PBM loan production offices in Diamond Bar, La Quinta, San Diego, Temecula, Torrance and Vista, California. The closures were due primarily to the decline in loan demand resulting from, among other factors, a decline in the real estate market, stricter loan underwriting standards and the well documented deterioration of the mortgage banking environment.

For the fiscal year ended June 30, 2008, the Bank recognized $210,000 of charges related to the loan production offices closings ($166,000 in premises and occupancy expense and $44,000 in salaries and employee benefits expense). As of June 30, 2008, the Bank did not have a remaining liability with respect to these actions and does not believe that additional charges will be incurred.

Allowance for loan losses

It is the policy of the Corporation to provide an allowance for loan losses inherent in the loans held for investment as of the balance sheet date when any significant and permanent decline in the borrower's ability to pay has occurred. Periodic reviews are made in an attempt to identify potential problems at an early stage. Individual loans are periodically reviewed and are classified according to their inherent risk. The internal asset review policy used by the Corporation is the primary basis by which the Corporation evaluates the probable loss exposure. Management's determination of the adequacy of the allowance for loan losses is based on an evaluation of the loans held for investment, past experience, prevailing market conditions, and other relevant factors. The determination of the allowance for loan losses is based on estimates that are particularly susceptible to changes in the economic environment and market conditions. The allowance is increased by the provision for loan losses charged against income and reduced by charge-offs, net of recoveries.

Allowance for unfunded loan commitments

The Corporation maintains the allowance for unfunded loan commitments at a level that is adequate to absorb estimated probable losses related to these unfunded credit facilities. The Corporation determines the adequacy of the allowance based on periodic evaluations of the unfunded credit facilities, including an assessment of the probability of commitment usage, credit risk factors for loans outstanding to these same customers, and the terms and expiration dates of the unfunded credit facilities. The allowance for unfunded loan commitments is recorded as a liability on the Consolidated Statements of Financial Condition. Net adjustments to the allowance for unfunded loan commitments are included in other non-interest expense on the Consolidated Statements of Operations.

Restructured loans

A troubled debt restructuring is a loan which the Corporation, for reasons related to a borrower's financial difficulties, grants a concession to the borrower that the Corporation would not otherwise consider.

The loan terms which have been modified or restructured due to a borrower's financial difficulty, include but are not limited to:

a) A reduction in the stated interest rate.

b) An extension of the maturity at an interest rate below market.
c) A reduction in the face amount of the debt.
d) A reduction in the accrued interest.
e) Re-aging, extensions, deferrals, renewals and rewrites.

The restructured loans are classified “Special Mention” or “Substandard” depending on the severity of the modification. Loans that were paid current at the time of modification may be upgraded in their classification after a sustained period of repayment performance, usually six months or longer.

Loans that are past due at the time of modification are classified “substandard” and placed on non-accrual status. Those loans may be upgraded in their classification and placed on accrual status once there is a sustained period of repayment performance (usually six months or longer) and there is a reasonable assurance that the repayment will continue.

Impaired loans

The Corporation assesses loans individually and identifies impairment when the accrual of interest has been discontinued, loans have been restructured or management has serious doubts about the future collectibility of principal and interest, even though the loans may currently be performing. Factors considered in determining impairment include, but are not limited to, expected future cash flows, the financial condition of the borrower and current economic conditions. The Corporation measures each impaired loan based on the fair value of its collateral or cash flow and charges off those loans or portions of loans deemed uncollectible.

Real estate

Real estate acquired through foreclosure is initially recorded at the lesser of the loan balance at the time of foreclosure or the fair value of the real estate acquired, less estimated selling costs. Subsequent to foreclosure, the Corporation charges current earnings with a provision for estimated losses if the carrying value of the property exceeds its fair value. Gains or losses on the sale of real estate are recognized upon disposition of the property. Costs relating to improvement of the property are capitalized. Other costs are expensed as incurred.

Impairment of long-lived assets

The Corporation reviews its long-lived assets for impairment annually or when events or circumstances indicate that the carrying amount of these assets may not be recoverable. Long-lived assets include buildings, land, fixtures, furniture and equipment. An asset is considered impaired when the expected undiscounted cash flows over the remaining useful life are less than the net book value. When impairment is indicated for an asset, the amount of impairment loss is the excess of the net book value over its fair value.

Premises and equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed primarily on a straight-line basis over the estimated useful lives as follows:

Buildings ………………………………….. 10 to 40 years

Furniture and fixtures …………………….	3 to 10 years
Automobiles ………………………………	3 years
Computer equipment ……………………..	3 to 5 years

Leasehold improvements are amortized over the respective lease terms or the useful life of the improvement, which range from one to 10 years. Maintenance and repair costs are charged to operations as incurred.

Notes to Consolidated Financial Statements

Income taxes

In July 2006, the FASB issued FASB Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109". FIN 48 prescribes a more-likely-than-not threshold for the financial statement recognition of uncertain tax positions. In this regard, an uncertain tax position represents the Corporation's expected treatment of a tax position taken in a filed tax return, or planned to be taken in a future tax return, that has not been reflected in measuring income tax expense for financial reporting purposes. FIN 48 clarifies the accounting for income taxes by prescribing a minimum recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 provides guidance on the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken in income tax returns. On July 1, 2007, the Corporation adopted the provisions of FIN 48 and had no cumulative effect adjustment recognized upon adoption. In addition, as a result of adoption of FIN 48, the Corporation does not have any unrecognized tax benefits as a result of uncertainty in income taxes on its Consolidated Statements of Financial Condition as of July 1, 2007 and June 30, 2008. It is the Corporation's policy to record any penalties or interest arising from federal or state taxes as a component of income tax expense. There were $104,000 in interest and no penalties included in the Consolidated Statements of Operations for the fiscal year ended June 30, 2008. The Corporation files income tax returns with the United States federal and state of California jurisdictions. The Corporation is no longer subject to United States federal and state income tax examinations by tax authorities for years ended on or before June 30, 2003. Accordingly, the tax years ended June 30, 2004 through 2007 remain open to examination by the federal and state taxing authorities. The Corporation is currently undergoing a regular review by the Internal Revenue Service for fiscal 2006 and 2007, and as part of that review, a tax adjustment of $407,000 was recorded in fiscal 2008 tax expense, which includes $104,000 in interest, for a disallowed tax deduction related to the sale of the commercial building sold in 2006. Management has not been made aware of any other significant issues at this time.

Cash dividend

A declaration or payment of dividends will be subject to the consideration of the Corporation's Board of Directors, which will take into account the Corporation's financial condition, results of operations, tax considerations, capital requirements, industry standards, economic conditions and other factors, including the regulatory restrictions which affect the payment of dividends by the Bank to the Corporation. Under Delaware law, dividends may be paid either out of surplus or, if there is no surplus, out of net profits for the current fiscal year and/or the preceding fiscal year in which the dividend is declared.

Stock repurchases

The Corporation repurchases its common stock consistent with Board-approved stock repurchase plans. During fiscal 2008, the Corporation repurchased 187,081 shares under the June 2007 stock repurchase program (59% of the authorized shares) with an average cost of $21.78 per share. The June 2007 program expired in June 2008. During fiscal 2008, the Corporation also repurchased 995 shares of restricted stock in lieu of distribution to employees (to satisfy the minimum income tax required to be withheld from employees) at an average cost of $22.21 per share. On June 26, 2008, the Corporation announced a stock repurchase program for the repurchase of up to 5% of its common stock or approximately 310,385 shares. As of June 30, 2008, no shares have been repurchased under the June 2008 stock repurchase program, leaving all authorized shares available for future repurchase activity.

Earnings per common share (EPS)

Basic EPS represents net income divided by the weighted average common shares outstanding during the period excluding any potential dilutive effects. Diluted EPS gives effect to all potential issuance of common stock that would have caused basic EPS to be lower as if the issuance had already occurred. Accordingly, diluted EPS reflects

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an increase in the weighted average shares outstanding as a result of the assumed exercise of stock options and the vesting of restricted stock.

Stock-based compensation

Prior to the fiscal year ended June 30, 2005, stock options were accounted for under Accounting Principles Board ("APB") Opinion No. 25 using the intrinsic value method. Accordingly, no stock option expense was recorded in periods prior to the fiscal year ended June 30, 2005, since the exercise price of the options issued has always been equal to the market value at the date of grant. Statement of Financial Accounting Standards ("SFAS") No. 123(R), "Share-Based Payment," requires companies to recognize in the statement of operations the grant-date fair value of stock options and other equity-based compensation issued to employees and directors. Effective July 1, 2005, the Corporation adopted SFAS No. 123(R) using the modified prospective method under which the provisions of SFAS No. 123(R) are applied to new awards and to awards modified, repurchased or cancelled after June 30, 2005 and to awards outstanding on June 30, 2005 for which requisite service has not yet been rendered.

The adoption of SFAS No. 123(R) resulted in incremental stock-based compensation expense solely related to issued and unvested stock option grants. The incremental stock-based compensation expense for fiscal years ended June 30, 2008, 2007 and 2006 was $742,000, $462,000 and $394,000, respectively. Cash provided by operating activities for fiscal 2008, 2007 and 2006 decreased by $6,000, $81,000 and $2.6 million, respectively, and cash provided by financing activities increased by an identical amount for fiscal 2008, 2007 and 2006, respectively, related to excess tax benefits from stock-based payment arrangements.

ESOP (Employee Stock Ownership Plan)

The Corporation recognizes compensation expense when shares are committed to be released to employees in an amount equal to the fair value of the shares so committed. The difference between the amount of compensation expense and the cost of the shares released is recorded as additional paid-in capital. Any cash dividends received on the unallocated ESOP shares which are applied as a prepayment to the ESOP loan leads to additional shares released and additional compensation expense.

Restricted stock

The Corporation recognizes compensation expense over the vesting period of the shares awarded, equal to the fair value of the shares at the award date.

Post retirement benefits

The estimated obligation for post retirement health care and life insurance benefits is determined based on an actuarial computation of the cost of current and future benefits for the eligible (grandfathered) retirees and employees. The post retirement benefit liability is included in other liabilities in the accompanying consolidated financial statements. Effective July 1, 2003, the Corporation discontinued the post retirement health care and life insurance benefits to any employee not previously qualified (grandfathered) for these benefits. At June 30, 2008, the accrued liability for post retirement benefits is $86,000 and is fully funded consistent with actuarially determined estimates of the future obligation.

Comprehensive income

Accounting principles generally require that realized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains or losses on available for sale securities, are reported as a separate component of the stockholders' equity section of the Consolidated Statements of Financial Condition, such items, along with income, are components of comprehensive income.

Notes to Consolidated Financial Statements

The components of other comprehensive income (loss) and their related tax effects are as follows:

	For the Year Ended June 30,		
(In Thousands)	2008	2007	2006
Unrealized holding (losses) gains on securities available for sale, net	$ (266)	$ 1,903	$ (1,241)
Reclassification adjustment for gains realized in income	-	-	-
Net unrealized (losses) gains	(266)	1,903	(1,241)
Tax effect	112	(799)	521
Net-of-tax amount	$ (154)	$ 1,104	$ (720)

Recent accounting pronouncements

Statement of Financial Accounting Standards ("SFAS" or "Statement") No. 161:
In March 2008, the Financial Accounting Standards Board ("FASB") issued SFAS No. 161, "Disclosures about Derivative and Hedging Activities - an amendment of FASB Statement No. 133." SFAS 161 requires enhanced disclosures on derivative and hedging activities. These enhanced disclosures will discuss (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 161 is effective for fiscal years beginning on or after November 15, 2008, with earlier adoption encouraged. Management does not anticipate a material impact, if any, to the Corporation's financial condition, results of operations, or cash flows.

SFAS No. 159:
In February 2007, the Financial Accounting Standards Board ("FASB") issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115." This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the FASB's long-term measurement objectives for accounting for financial instruments. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The adoption of this statement did not have a material impact to the Corporation's financial condition, results of operations, or cash flows.

SFAS No. 157:
In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." This Statement defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The adoption of this statement did not have a material impact to the Corporation's financial condition, results of operations, or cash flows.

Notes to Consolidated Financial Statements

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2. Investment Securities:

The amortized cost and estimated fair value of investment securities as of June 30, 2008 and 2007 were as follows:

June 30, 2008 (In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Carrying Value
Available for sale					
U.S. government sponsored enterprise debt securities	$ 5,250	$ -	$ (139)	$ 5,111	$ 5,111
U.S. government agency MBS	90,960	247	(269)	90,938	90,938
U.S. government sponsored enterprise MBS (1)	53,847	422	(15)	54,254	54,254
Private issue CMO (2)	2,275	-	(50)	2,225	2,225
Freddie Mac common stock	6	92	-	98	98
Fannie Mae common stock	1	7	-	8	8
Other common stock	118	350	-	468	468
Total available for sale	152,457	1,118	(473)	153,102	153,102
Total investment securities	$ 152,457	$ 1,118	$ (473)	$ 153,102	$ 153,102

(1) Mortgage-backed securities ("MBS")
(2) Collateralized Mortgage Obligations ("CMO")

June 30, 2007 (In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Carrying Value
Held to maturity					
U.S. government sponsored enterprise debt securities	$ 19,000	$ -	$ (164)	$ 18,836	$ 19,000
U.S. government agency MBS	1	-	-	1	1
Total held to maturity	19,001	-	(164)	18,837	19,001
Available for sale					
U.S. government sponsored enterprise debt securities	9,849	-	(166)	9,683	9,683
U.S. government agency MBS	57,555	19	(35)	57,539	57,539
U.S. government sponsored enterprise MBS	58,861	337	(132)	59,066	59,066
Private issue CMO	4,627	22	(8)	4,641	4,641
Freddie Mac common stock	6	358	-	364	364
Fannie Mae common stock	1	25	-	26	26
Other common stock	118	405	-	523	523
Total available for sale	131,017	1,166	(341)	131,842	131,842

Total investment securities	$ 150,018	$ 1,166	$ (505)	$ 150,679	$ 150,843

During fiscal 2008, $29.0 million of investment securities matured or were called by the issuer, $47.5 million of MBS principal payments were received and $78.9 million of investment securities were purchased. In fiscal 2007,

Notes to Consolidated Financial Statements

$44.5 million of investment securities matured or were called by the issuer, $40.1 million of MBS principal payments were received and $56.5 million of investment securities were purchased. In fiscal 2006, $4.2 million of investment securities matured and $49.0 million of MBS principal payments were received. No investment securities were sold during the fiscal years ended June 30, 2008, 2007 and 2006.

As of June 30, 2008 and 2007, the Corporation held investments with an unrealized loss position totaling $473,000 and $505,000, respectively, consisting of the following:

As of June 30, 2008	Unrealized Holding Losses		Unrealized Holding Losses		Unrealized Holding Losses	
(In Thousands)	Less Than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government sponsored enterprise debt securities:						
Fannie Mae	$ 1,940	$ 60	$ -	$ -	$ 1,940	$ 60
FHLB	3,171	79	-	-	3,171	79
U.S. government agency MBS:						
GNMA (1)	47,048	269	-	-	47,048	269
U.S. government sponsored enterprise MBS:						
Freddie Mac	8,770	15	-	-	8,770	15
Private issue CMO:						
Other institutions	1,836	49	389	1	2,225	50
Total	$ 62,765	$ 472	$ 389	$ 1	$ 63,154	$ 473

(1) Government National Mortgage Association ("GNMA")

As of June 30, 2007	Unrealized Holding Losses		Unrealized Holding Losses		Unrealized Holding Losses	
(In Thousands)	Less Than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government sponsored enterprise debt securities:						
Freddie Mac	$ -	$ -	$ 10,869	$ 130	$ 10,869	$ 130
FHLB	-	-	17,650	200	17,650	200
U.S. government agency MBS:						
GNMA	27,769	32	4,762	3	32,531	35
U.S. government sponsored enterprise MBS:						
Fannie Mae	-	-	2,988	54	2,988	54
Freddie Mac	14,821	78	-	-	14,821	78
Private issue CMO:						

Other institutions	-	-	1,222	8	1,222	8
Total	$ 42,590	$ 110	$ 37,491	$ 395	$ 80,081	$ 505

As of June 30, 2008, the unrealized holding losses relate to a total of 15 investment securities, which consist of 11 adjustable rate MBS (primarily U.S. government agency MBS), two adjustable rate private issue CMO and two fixed rate government sponsored enterprise debt obligations, ranging from a de minimus percentage to 3.1% of cost. Of

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these unrealized losses in investment securities, only one has been in an unrealized loss position for more than 12 months. Such unrealized holding losses are primarily the result of fluctuations in interest rates during fiscal 2008 and to a lesser degree, of credit concerns perceived by the market on agency and private issue investment securities. Based on the nature of the investments, management concluded that such unrealized losses were not other than temporary as of June 30, 2008. The Corporation has the ability and positive intent to hold the investment securities to maturity, thereby realizing a full recovery.

Contractual maturities of investment securities as of June 30, 2008 and 2007 were as follows:

	June 30, 2008		June 30, 2007	
(In Thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Held to maturity				
Due in one year or less	$ -	$ -	$ 19,000	$ 18,836
Due after one through five years	-	-	1	1
Due after five years	-	-	-	-
	-	-	19,001	18,837
Available for sale				
Due in one year or less	-	-	8,095	7,965
Due after one through five years	-	-	1,850	1,813
Due after five through ten years	5,250	5,111	-	-
Due after ten years	147,082	147,417	120,947	121,151
No stated maturity (common stock)	125	574	125	913
	152,457	153,102	131,017	131,842
Total investment securities	$ 152,457	$ 153,102	$ 150,018	$ 150,679

3. Loans Held for Investment:

Loans held for investment consisted of the following:

		June 30,	
(In Thousands)		2008	2007
Mortgage loans:			
	Single-family	$ 808,836	$ 827,656
	Multi-family	399,733	330,231
	Commercial real estate	136,176	147,545
	Construction	32,907	60,571
Commercial business loans		8,633	10,054
Consumer loans		625	509
Other loans		3,728	9,307
		1,390,638	1,385,873
Less:			

Undisbursed loan funds	(7,864)	(25,484)
Deferred loan costs	5,261	5,152
Allowance for loan losses	(19,898)	(14,845)
Total loans held for investment, net	$ 1,368,137	$ 1,350,696

Notes to Consolidated Financial Statements

Fixed-rate loans comprised 4% of loans held for investment at June 30, 2008, unchanged from June 30, 2007. As of June 30, 2008, the Bank had $80.0 million in mortgage loans that are subject to negative amortization, consisting of $45.1 million in multi-family loans, $22.0 million in commercial real estate loans and $12.9 million in single-family loans. This compares to negative amortization mortgage loans of $87.4 million at June 30, 2007, consisting of $47.8 million in multi-family loans, $27.0 million in commercial real estate loans and $12.6 million in single-family loans. The amount of negative amortization included in loan balances increased to $610,000 at June 30, 2008 from $397,000 at June 30, 2007. During fiscal 2008, approximately $274,000, or 0.32%, of loan interest income represented negative amortization, up from $272,000, or 0.30% in fiscal 2007. Negative amortization involves a greater risk to the Bank because the loan principal balance may increase by a range of 110% to 115% of the original loan amount. Also, the Bank has invested in interest-only ARM loans, which typically have a fixed interest rate for the first two to five years coupled with an interest only payment, followed by a periodic adjustable interest rate and a fully amortizing loan payment. As of June 30, 2008 and 2007, the interest-only ARM loans were $601.3 million and $619.7 million, or 43.5% and 45.4% of loans held for investment, respectively.

The following table sets forth information at June 30, 2008 regarding the dollar amount of loans held for investment that are contractually repricing during the periods indicated, segregated between adjustable interest rate loans and fixed interest rate loans. Adjustable interest rate loans having no stated repricing dates and checking account overdrafts are reported as repricing within one year. The table does not include any estimate of prepayments which may cause the Bank's actual repricing experience to differ materially from that shown below.

	Adjustable Rate						
(In Thousands)	Within One Year	After One Year Through 3 Years	After 3 Years Through 5 Years	After 5 Years Through 10 Years	Beyond 10 Years	Fixed Rate	Total
Mortgage loans:							
Single-family	$ 150,547	$ 390,942	$ 256,588	$ 2,876	$ -	$ 7,883	$ 808,836
Multi-family	135,597	86,019	128,494	34,386	-	15,237	399,733
Commercial real estate	38,312	41,701	30,164	2,435	-	23,564	136,176
Construction	32,907	-	-	-	-	-	32,907
Commercial business loans	5,951	-	-	-	-	2,682	8,633
Consumer loans	601	-	-	-	-	24	625
Other loans	3,223	-	-	-	-	505	3,728
Total loans held for investment	$ 367,138	$ 518,662	$ 415,246	$ 39,697	$ -	$ 49,895	$ 1,390,638

The following summarizes the components of the net change in the allowance for loan losses:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006

Balance, beginning of year	$ 14,845	$ 10,307	$ 9,215
Provision for loan losses	13,108	5,078	1,134
Recoveries	223	1	2
Charge-offs	(8,278)	(541)	(44)
Balance, end of year	$ 19,898	$ 14,845	$ 10,307

Notes to Consolidated Financial Statements

Non-accrual loans were $23.2 million and $15.9 million at June 30, 2008 and 2007, respectively. The effect of non-accrual and restructured loans on interest income for the years ended June 30, 2008, 2007 and 2006 is presented below:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Contractual interest due	$ 2,127	$ 1,162	$ 146
Interest recognized	(263)	(173)	(33)
Net interest foregone	$ 1,864	$ 989	$ 113

The following tables identify the Corporation's total recorded investment in impaired loans by type, net of specific allowances, at June 30, 2008 and 2007:

	June 30, 2008		
(In Thousands)	Recorded Investment	Allowance For Loan Losses	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 20,356	$ (5,004)	$ 15,352
Without a related allowance	1,978	-	1,978
Total single-family loans	22,334	(5,004)	17,330
Commercial real estate:			
Without a related allowance	572	-	572
Total commercial real estate loans	572	-	572
Construction:			
With a related allowance	2,219	(1,425)	794
Without a related allowance	3,922	-	3,922
Total construction loans	6,141	(1,425)	4,716
Commercial business loans:			
With a related allowance	59	(59)	-
Total commercial business loans	59	(59)	-
Other loans:			
With a related allowance	47	(15)	32
Without a related allowance	543	-	543
Total other loans	590	(15)	575
Total impaired loans	$ 29,696	$ (6,503)	$ 23,193

Notes to Consolidated Financial Statements

	June 30, 2007		
(In Thousands)	Recorded Investment	Allowance For Loan Losses	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 2,651	$ (621)	$ 2,030
Without a related allowance	11,241	-	11,241
Total single-family loans	13,892	(621)	13,271
Construction:			
With a related allowance	4,981	(2,624)	2,357
Total construction loans	4,981	(2,624)	2,357
Commercial business loans:			
With a related allowance	252	(81)	171
Total commercial business loans	252	(81)	171
Other loans:			
Without a related allowance	108	-	108
Total other loans	108	-	108
Total impaired loans	$ 19,233	$ (3,326)	$ 15,907

At June 30, 2008 and 2007, there were no commitments to lend additional funds to those borrowers whose loans were classified as impaired.

During the fiscal years ended June 30, 2008, 2007 and 2006, the Corporation's average investment in impaired loans was $17.2 million, $10.2 million and $1.8 million, respectively. Interest income of $2.2 million, $646,000 and $192,000 was recognized, based on cash receipts, on impaired loans during the years ended June 30, 2008, 2007 and 2006, respectively. The Corporation records interest on non-accrual loans utilizing the cash basis method of accounting during the periods when the loans are on non-accrual status.

During the fiscal year ended June 30, 2008, 32 loans for $10.5 million were modified from their original terms, were re-underwritten at current market interest rates and were identified in our asset quality reports as restructured loans. As of June 30, 2008, these restructured loans are classified as follows: six are classified as pass ($2.3 million); 13 are classified as special mention and remain on accrual status ($4.0 million); eight are classified as substandard and remain on accrual status ($2.8 million); and five are classified as substandard on non-accrual status ($1.4 million).

Notes to Consolidated Financial Statements

The following table shows the restructured loans by type, net of specific allowances, at June 30, 2008:

	June 30, 2008		
(In Thousands)	Recorded Investment	Allowance For Loan Losses	Net Investment
Mortgage loans:			
Single-family:			
With a related allowance	$ 1,900	$ (545)	$ 1,355
Without a related allowance	9,101	-	9,101
Total single-family loans	11,001	(545)	10,456
Other loans:			
Without a related allowance	28	-	28
Total other loans	28	-	28
Total restructured loans	$ 11,029	$ (545)	$ 10,484

In the ordinary course of business, the Bank makes loans to its directors, officers and employees at substantially the same terms prevailing at the time of origination for comparable transactions with unaffiliated borrowers. The following is a summary of related-party loan activity:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Balance, beginning of year	$ 3,123	$ 5,497	$ 5,417
Originations	1,443	3,157	4,111
Sales/payments	(2,169)	(5,531)	(4,031)
Balance, end of year	$ 2,397	$ 3,123	$ 5,497

4. Mortgage Loan Servicing and Loans Originated for Sale:

The following summarizes the unpaid principal balance of loans serviced for others by the Corporation:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Loans serviced for Freddie Mac	$ 4,215	$ 6,315	$ 8,918
Loans serviced for Fannie Mae	20,496	21,206	22,484
Loans serviced for FHLB – San Francisco	150,908	173,239	201,644
Loans serviced for other institutional investors	5,413	5,028	6,604
Total loans serviced for others	$ 181,032	$ 205,788	$ 239,650

Mortgage servicing assets are recorded when loans are sold to investors and the servicing of those loans is retained by the Bank. Mortgage servicing assets are subject to interest rate risk and may become impaired when interest rates

Notes to Consolidated Financial Statements

fall and the borrowers refinance or prepay their mortgage loans. The mortgage servicing assets are derived primarily from single-family loans.

Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors and processing foreclosures. Income from servicing loans is reported as loan servicing and other fees in the Corporation's consolidated financial statements of operations, and the amortization of mortgage servicing assets is reported as a reduction to the loan servicing income. Loan servicing income includes servicing fees from investors and certain charges collected from borrowers, such as late payment fees. As of June 30, 2008 and 2007, the Corporation held borrowers' escrow balances related to loans serviced for others of $478,000 and $493,000, respectively.

Loans sold to the FHLB – San Francisco were completed under the MPF Program, which entitles the Bank to a credit enhancement fee collected from FHLB – San Francisco on a monthly basis.

The following table summarizes the Corporation's mortgage servicing assets ("MSA") for fiscal years ended June 30, 2008 and 2007.

	Year Ended June 30,	
(Dollars In Thousands)	2008	2007
MSA balance, beginning of fiscal year	$ 991	$ 1,379
Additions	21	33
Amortization	(339)	(421)
MSA balance, end of fiscal year, before impairment allowance	673	991
Impairment allowance	-	-
MSA balance, end of fiscal year	$ 673	$ 991
Fair value, beginning of fiscal year	$ 1,998	$ 2,152
Fair value, end of fiscal year	$ 1,387	$ 1,998
Impairment allowance, beginning of fiscal year	$ -	$ -
Impairment provision	-	-
Impairment allowance, end of fiscal year	$ -	$ -
Key Assumptions:		
Weighted-average discount rate	9.00%	9.00%
Weighted-average prepayment speed	8.58%	3.53%

Notes to Consolidated Financial Statements

The following table summarizes the estimated future amortization of mortgage servicing assets for the next five years and thereafter:

Year Ending June 30,	Amount (In Thousands)
2009	$ 261
2010	150
2011	115
2012	91
2013	50
Thereafter	6
Total estimated amortization expense	$ 673

The following table represents the hypothetical effect on the fair value of the Corporation's mortgage servicing assets using an unfavorable shock analysis of certain key assumptions used in the valuation of the mortgage servicing assets as of June 30, 2008 and 2007. This analysis is presented for hypothetical purposes only. As the amounts indicate, changes in fair value based on changes in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear.

	Year Ended June 30,	
(Dollars In Thousands)	2008	2007
MSA net carrying value	$ 673	$ 991
CPR assumption (weighted-average)	8.58%	3.53%
Impact on fair value of 10% adverse change of prepayment speed	$ (32)	$ (28)
Impact on fair value of 20% adverse change of prepayment speed	$ (62)	$ (56)
Discount rate assumption (weighted-average)	9.00%	9.00%
Impact on fair value of 10% adverse change of discount rate	$ (56)	$ (91)
Impact on fair value of 20% adverse change of discount rate	$ (109)	$ (175)

Loans sold consisted of the following:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Loans sold:			
Servicing – released	$ 368,925	$ 1,119,330	$ 1,242,093
Servicing – retained	4,534	4,108	19,348
Total loans sold	$ 373,459	$ 1,123,438	$ 1,261,441

Notes to Consolidated Financial Statements

Loans held for sale consisted of the following:

(In Thousands)	June 30, 2008	2007
Fixed rate	$ 27,390	$ 1,337
Adjustable rate	1,071	-
Total loans held for sale	$ 28,461	$ 1,337

5. Real Estate Owned:

Real estate owned consisted of the following:

(In Thousands)	June 30, 2008	2007
Real estate owned	$ 9,872	$ 3,804
Less the allowance for real estate owned losses	(517)	-
Total real estate owned, net	$ 9,355	$ 3,804

Real estate owned was primarily the result of real estate acquired in the settlement of loans. As of June 30, 2008, real estate owned was comprised of 45 properties, primarily single-family residences and land located in Southern California. This compares to 10 real estate owned properties at June 30, 2007, primarily single-family residences located in Southern California. The increase in real estate owned was due primarily to more foreclosures resulting from weakness in the real estate market, stringent underwriting standards, less liquidity in the secondary market and other related factors.

During fiscal 2008, the Bank acquired 72 real estate owned properties in the settlement of loans and sold 37 properties for a net loss of $932,000.

A summary of the disposition and operations of real estate owned acquired in the settlement of loans for the fiscal years ended June 30, 2008, 2007 and 2006 consisted of the following:

(In Thousands)	Year Ended June 30, 2008	2007	2006
Net (losses) gains on sale	$ (932)	$ 46	$ 20
Net operating expenses	(1,234)	(163)	-
Provision for estimated losses	(517)	-	-
(Loss) gain on sale and operations of real estate owned acquired in the settlement of loans, net	$ (2,683)	$ (117)	$ 20

Notes to Consolidated Financial Statements

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6. Premises and Equipment:

Premises and equipment consisted of the following:

(In Thousands)	June 30, 2008	June 30, 2007
Land	$ 3,051	$ 3,051
Buildings	8,167	8,416
Leasehold improvements	1,524	1,525
Furniture and equipment	6,535	7,030
Automobiles	106	81
	19,383	20,103
Less accumulated depreciation and amortization	(12,870)	(12,980)
Total premises and equipment, net	$ 6,513	$ 7,123

Depreciation and amortization expense for the years ended June 30, 2008, 2007 and 2006 amounted to $1.0 million, $972,000 and $1.2 million, respectively.

7. Deposits:

	June 30, 2008		June 30, 2007	
(Dollars in Thousands)	Interest Rate	Amount	Interest Rate	Amount
Checking deposits – non interest-bearing	-	$ 48,056	-	$ 45,112
Checking deposits – interest-bearing (1)	0% - 1.50%	122,065	0% - 3.92%	122,588
Savings deposits (1)	0% - 3.25%	144,883	0% - 5.11%	153,036
Money market deposits (1)	0% - 2.47%	33,675	0% - 5.12%	32,054
Time deposits				
Under $100	0.40% - 5.84%	300,467	0.40% - 5.84%	302,738
$100 and over (2)	1.36% - 5.84%	363,264	2.47% - 5.70%	345,869
Total deposits		$ 1,012,410		$ 1,001,397
Weighted average interest rate on deposits		2.95%		3.63%

(1) Certain interest-bearing checking, savings and money market accounts require a minimum balance to earn interest.

(2) Includes a single depositor with balances of $100.3 million and $100.0 million at June 30, 2008 and 2007, respectively.

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The aggregate annual maturities of time deposits are as follows:

	June 30,	
(In Thousands)	2008	2007
One year or less	$ 589,384	$ 434,463
Over one to two years	60,159	162,722
Over two to three years	7,020	46,985
Over three to four years	2,430	1,912
Over four to five years	4,680	2,525
Over five years	58	-
Total time deposits	$ 663,731	$ 648,607

Interest expense on deposits is summarized as follows:

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Checking deposits – interest-bearing	$ 881	$ 961	$ 814
Savings deposits	2,896	2,823	3,151
Money market deposits	726	563	472
Time deposits	30,073	26,867	17,691
Total interest expense on deposits	$ 34,576	$ 31,214	$ 22,128

The Corporation is required to maintain reserve balances with the Federal Reserve Bank. Such reserves are calculated based on deposit balances and are offset by the cash balances maintained by the Bank. The cash balances maintained by the Bank at June 30, 2008 and 2007 were sufficient to cover the reserve requirements.

8. Borrowings:

Advances from the FHLB – San Francisco, which mature on various dates through 2021, are collateralized by pledges of certain real estate loans with an aggregate principal balance at June 30, 2008 and 2007 of $899.3 million and $875.2 million, respectively. In addition, the Bank pledged investment securities totaling $26.4 million at June 30, 2008 to collateralize its FHLB – San Francisco advances under the Securities-Backed Credit ("SBC") program as compared to $24.9 million at June 30, 2007. At June 30, 2008, the Bank's FHLB – San Francisco borrowing capacity, which is limited to 50% of total assets reported on the Bank's quarterly thrift financial report, is approximately $837.1 million as compared to $885.2 million at June 30, 2007. As of June 30, 2008 and 2007, the remaining borrowing facility was $352.7 million and $370.9 million, respectively, with the remaining collateral of $439.9 million and $391.9 million, respectively.

In addition, the Bank has a borrowing arrangement in the form of a federal funds facility with its correspondent bank for $25.0 million which matures on November 30, 2008. Management intends to request a renewal. As of June 30, 2008 and 2007, the Bank has no borrowings outstanding under this facility.

Notes to Consolidated Financial Statements

Borrowings consisted of the following:

(In Thousands)	June 30, 2008	2007
FHLB – San Francisco advances	$ 466,335	$ 478,774
SBC FHLB – San Francisco advances	13,000	24,000
Total borrowings	$ 479,335	$ 502,774

As a member of the FHLB – San Francisco, the Bank is required to maintain a minimum investment in FHLB – San Francisco stock. The Bank held the required investment of $30.0 million and an excess investment of $2.1 million at June 30, 2008, as compared to the required investment of $32.2 million and an excess investment of $11.7 million at June 30, 2007. Any excess may be redeemed at par by the Bank or returned by FHLB – San Francisco.

The following tables set forth certain information regarding borrowings by the Bank at the dates and for the years indicated:

	At or For the Year Ended June 30,		
(Dollars in Thousands)	2008	2007	2006
Balance outstanding at the end of year:			
FHLB – San Francisco advances	$ 479,335	$ 502,774	$ 546,211
Correspondent bank advances	-	-	-
Weighted average rate at the end of year:			
FHLB – San Francisco advances	3.81%	4.55%	4.53%
Correspondent bank advances	-	-	-
Maximum amount of borrowings outstanding at any month end:			
FHLB – San Francisco advances	$ 499,744	$ 689,443	$ 572,342
Correspondent bank advances	$ -	$ 1,000	-
Average short-term borrowings during the year (1) with respect to:			
FHLB – San Francisco advances	$ 188,390	$ 281,267	$ 121,950
Correspondent bank advances	$ 143	$ 168	$ 205
Weighted average short-term borrowing rate during the year (1) with respect to:			
FHLB – San Francisco advances	3.76%	4.89%	4.11%
Correspondent bank advances	5.36%	5.34%	3.46%

(1) Borrowings with a remaining term of 12 months or less.

Notes to Consolidated Financial Statements

The aggregate annual contractual maturities of borrowings are as follows:

	June 30,	
(Dollars in Thousands)	2008	2007
Within one year	$ 142,600	$ 246,000
Over one to two years	112,000	30,000
Over two to three years	128,000	72,000
Over three to four years	65,000	88,000
Over four to five years	20,000	65,000
Over five years	11,735	1,774
Total borrowings	$ 479,335	$ 502,774
Weighted average interest rate	3.81%	4.55%

9. Income Taxes:

The provision for income taxes consisted of the following:

		Year Ended June 30,	
(In Thousands)	2008	2007	2006
Current:			
Federal	$ 5,902	$ 6,568	$ 13,221
State	1,952	2,392	4,504
	7,854	8,960	17,725
Deferred:			
Federal	(4,042)	233	(1,561)
State	(1,444)	(69)	(488)
	(5,486)	164	(2,049)
Provision for income taxes	$ 2,368	$ 9,124	$ 15,676

The Corporation’s tax benefit from non-qualified equity compensation in fiscal 2008, fiscal 2007 and fiscal 2006 was approximately $6,000, $81,000 and $2.6 million, respectively.

The provision for income taxes differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pre-tax income from continuing operations as a result of the following differences:

		Year Ended June 30,	
	2008	2007	2006
Federal statutory income tax rate	35.0%	35.0%	35.0%
State taxes, net of federal tax effect	7.9	7.5	7.2
Other	30.5	4.1	2.2

Effective income tax rate	73.4%	46.6%	44.4%

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Notes to Consolidated Financial Statements

The increase in the effective income tax rate in fiscal 2008 was attributable to a higher percentage of permanent tax differences relative to income before taxes (primarily related to stock based compensation) and an additional tax provision of $407,000 on a disallowed deduction in the fiscal 2006 tax return which was discovered during the ongoing examination by the Internal Revenue Service.

Deferred tax assets by jurisdiction were as follows:

(In Thousands)	June 30, 2008	June 30, 2007
Deferred taxes – federal	$ (4,036)	$ 105
Deferred taxes – state	(1,589)	(133)
Total net deferred tax assets	$ (5,625)	$ (28)

Deferred tax assets were comprised of the following:

(In Thousands)	June 30, 2008	June 30, 2007
Depreciation	$ 66	$ 156
FHLB – San Francisco stock dividends	4,325	5,067
Unrealized gain on investment securities	120	343
Unrealized gain on interest-only strips	270	159
Deferred loan costs	2,932	3,038
Total deferred tax liabilities	7,713	8,763
State taxes	(39)	(757)
Loss reserves	(11,326)	(6,387)
Deferred compensation	(1,797)	(1,486)
Accrued vacation	(160)	(142)
Other	(16)	(19)
Total deferred tax assets	(13,338)	(8,791)
Net deferred tax assets	$ (5,625)	$ (28)

The net deferred tax assets are included in Other Assets in the accompanying Consolidated Statements of Financial Condition. Management believes that it is more likely than not, the Company will generate sufficient taxable income in the future to realize the deferred tax assets recorded at June 30, 2008.

Retained earnings at June 30, 2008 included approximately $9.0 million for which federal income tax of $3.1 million had not been provided. If the amounts that qualify as deductions for federal income tax purposes are later used for purposes other than for bad debt losses, including distribution in liquidation, they will be subject to federal income tax at the then-current corporate tax rate. If those amounts are not so used, they will not be subject to tax even in the event the Bank were to convert its charter from a thrift to a bank.

10. Capital:

Federal regulations require that institutions with investments in subsidiaries conducting real estate investment and joint venture activities maintain sufficient capital over the minimum regulatory requirements. The Bank maintains capital in excess of the minimum requirements.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Corporation's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of Total and Tier 1 Capital (as defined in the regulations) to Risk-Weighted Assets (as defined), and of Core Capital (as defined) to Adjusted Tangible Assets (as defined). Management believes, as of June 30, 2008 and 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of June 30, 2008 and 2007, the most recent notification from the Office of Thrift Supervision categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Bank must maintain minimum Total Risk-Based Capital (to risk-weighted assets), Core Capital (to adjusted tangible assets) and Tier 1 Risk-Based Capital (to risk-weighted assets) as set forth in the table. There are no conditions or events since the notification that management believes have changed the Bank's category.

The Bank may not declare or pay cash dividends on or repurchase any of its shares of common stock, if the effect would cause stockholders equity to be reduced below applicable regulatory capital maintenance requirements or if such declaration and payment would otherwise violate regulatory requirements. In fiscal 2008, 2007 and 2006, the Bank declared and paid cash dividends of $12.0 million, $20.0 million and $6.0 million, respectively to, its parent, the Corporation.

Notes to Consolidated Financial Statements

The Bank's actual capital amounts and ratios as of June 30, 2008 and 2007 are as follows:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
(Dollars in Thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of June 30, 2008						
Total Risk-Based Capital	$ 127,411	12.25%	$ 83,236	> 8.0%	$> 104,045	10.0%
Core Capital	117,326	7.19%	65,252	> 4.0%	81,565>	5.0%
Tier 1 Risk-Based Capital	114,345	10.99%	N/A	N/A	62,427>	6.0%
Tangible Capital	117,326	7.19%	24,470	> 1.5%	N/A	N/A
As of June 30, 2007						
Total Risk-Based Capital	$ 134,474	12.49%	$ 86,103	> 8.0%	$> 107,629	10.0%
Core Capital	125,568	7.62%	65,884	> 4.0%	82,355>	5.0%
Tier 1 Risk-Based Capital	122,591	11.39%	N/A	N/A	64,577>	6.0%
Tangible Capital	125,568	7.62%	24,707	> 1.5%	N/A	N/A

11. Benefit Plans:

The Corporation has a 401(k) defined-contribution plan covering all employees meeting specific age and service requirements. Under the plan, employees may contribute to the plan from their pretax compensation up to the limits set by the Internal Revenue Service. The Corporation makes matching contributions up to 3% of participants' pretax compensation. Participants vest immediately in their own contributions with 100% vesting in the Corporation's contributions occurring after six years of credited service. The Corporation's expense for the plan was approximately $304,000, $426,000 and $411,000 for the years ended June 30, 2008, 2007 and 2006, respectively.

The Corporation has a multi-year employment agreement with one executive officer, which requires payments of certain benefits upon retirement. At June 30, 2008, the accrued liability is $2.3 million; costs are being accrued and expensed annually; and the current obligation is fully funded consistent with contractual requirements and actuarially determined estimates of the total future obligation.

ESOP (Employee Stock Ownership Plan)

An ESOP was established on June 27, 1996 for all employees who are age 21 or older and have completed one year of service with the Corporation during which they have served a minimum of 1,000 hours. The ESOP Trust borrowed $4.1 million from the Corporation to purchase 922,538 shares of the common stock issued in the conversion. Shares purchased with the loan proceeds are held in an unearned ESOP account and released on a pro rata basis based on the

distribution schedule and repayment of the ESOP loan. The loan is principally repaid from the Corporation's contributions to the ESOP over a period of 15 years. In addition to the scheduled principal payments, the ESOP Trust has paid additional principal amounts, which came from cash dividends received on the unallocated ESOP shares. The additional principal payments in fiscal 2008 and 2007 were $52,000 and $131,000, respectively. These loan payments resulted in additional compensation expense and ESOP share releases. At June 30, 2008 and 2007, the outstanding balance on the loan was $144,000 and $622,000, respectively. Contributions to the ESOP and share releases from the unearned ESOP account are allocated among participants on the basis of

compensation, as described in the plan, in the year of allocation. Benefits generally become 100% vested after six years of credited service. Vesting accelerates upon retirement, death or disability of the participant or in the event of a change in control of the Corporation. Forfeitures are reallocated among remaining participating employees in the same proportion as contributions. Benefits are payable upon death, retirement, early retirement, disability or separation from service. Since the annual contributions are discretionary, the benefits payable under the ESOP cannot be estimated. The expense related to the ESOP was $1.4 million, $2.6 million and $2.6 million for the years ended June 30, 2008, 2007 and 2006, respectively. Of these expenses, $271,000, $835,000 and $904,000 were related to additional share releases consistent with the prepayment of the ESOP loan for the years ended June 30, 2008, 2007 and 2006, respectively. At June 30, 2008 and 2007, the unearned ESOP account of $102,000 and $455,000, respectively, was reported as a reduction to stockholders' equity.

The table below reflects ESOP activity for the year indicated (in number of shares):

	June 30,		
	2008	2007	2006
Unallocated shares at beginning of year	102,309	192,255	284,885
Allocated	(79,436)	(89,946)	(92,630)
Unallocated shares at end of year	22,873	102,309	192,255

The fair value of unallocated ESOP shares was $216,000, $2.6 million and $5.8 million at June 30, 2008, 2007 and 2006, respectively.

12. Incentive Plans:

As of June 30, 2008, the Corporation had three share-based compensation plans, which are described below. These plans include the 2006 Equity Incentive Plan, 2003 Stock Option Plan and 1996 Stock Option Plan. The 1997 Management Recognition Plan was fully distributed in July 2007 and is no longer an active incentive plan. The compensation cost that has been charged against income for these plans was $1.0 million, $511,000 and $324,000 for fiscal years ended June 30, 2008, 2007 and 2006, respectively. The income tax benefit recognized in the Consolidated Statements of Operations for share-based compensation plans was $6,000, $81,000 and $2.6 million for fiscal years ended June 30, 2008, 2007 and 2006, respectively.

Equity Incentive Plan. The Corporation established and the shareholders approved the 2006 Equity Incentive Plan ("2006 Plan") for directors, advisory directors, directors emeriti, officers and employees of the Corporation and its subsidiary. The 2006 Plan authorizes 365,000 stock options and 185,000 shares of restricted stock. The 2006 Plan also provides that no person may be granted more than 73,000 stock options or awarded 27,750 shares of restricted stock in any one year.

a) Equity Incentive Plan - Stock Options. Under the 2006 Plan, options may not be granted at a price less than the fair market value at the date of the grant. Options typically vest over a five-year period on a pro-rata basis as long as the director, advisory director, director emeriti, officer or employee remains in service to the Corporation. The options are exercisable after vesting for up to the remaining term of the original grant. The maximum term of the options

granted is 10 years.

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option valuation model with the assumptions noted in the following table. The expected volatility is based on implied volatility from historical common stock closing prices for the last 84 months. The expected dividend yield is based on the most recent quarterly dividend on an annualized basis. The expected term is based on the historical experience of all fully vested stock option grants and is reviewed annually. The risk-free interest rate is based on the U.S. Treasury note

rate with a term similar to the underlying stock option on the particular grant date.

	Fiscal 2008	Fiscal 2007
Expected volatility range	-	19%
Weighted-average volatility	-	19%
Expected dividend yield	-	2.5%
Expected term (in years)	-	7.4
Risk-free interest rate	-	4.8%

In fiscal 2008, no options were granted or exercised from the 2006 Plan, while 12,000 options were forfeited in fiscal 2008. A total of 187,300 options were granted in fiscal 2007 and the weighted-average fair value of options granted as of the grant date was $6.49 per option. There was no other activity in fiscal 2007. As of June 30, 2008 and 2007, there were 189,700 and 177,700 options, respectively, available for future grants under the 2006 Plan.

The following is a summary of stock option activity since the inception of the 2006 Plan and changes during the fiscal years ended June 30, 2008 and 2007 are presented below:

Equity Incentive Plan – Stock Options	Stock Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at July 1, 2006	-	-		
Granted	187,300	$ 28.31		
Exercised	-	-		
Forfeited	-	-		
Outstanding at June 30, 2007	187,300	$ 28.31	9.61	$ -
Vested and expected to vest at June 30, 2007	149,840	$ 28.31	9.61	$ -
Exercisable at June 30, 2007	-	-	-	$ -
Outstanding at July 1, 2007	187,300	$ 28.31		
Granted	-	-		
Exercised	-	-		
Forfeited	(12,000)	$ 28.31		
Outstanding at June 30, 2008	175,300	$ 28.31	8.61	$ -
Vested and expected to vest at June 30, 2008	147,252	$ 28.31	8.61	$ -
Exercisable at June 30, 2008	35,060	$ 28.31	8.61	$ -

As of June 30, 2008 and 2007, there was $701,000 and $895,000 of unrecognized compensation expense, respectively, related to unvested share-based compensation arrangements granted under the 2006 Plan. The expense is

expected to be recognized over a weighted-average period of 3.6 years and 4.6 years, respectively. The forfeiture rate during fiscal 2008 and 2007 was 20 percent, calculated by using the historical forfeiture experience of all fully vested stock option grants and is reviewed annually.

b) Equity Incentive Plan – Restricted Stock. The Corporation will use 185,000 shares of its treasury stock to fund the 2006 Plan. Awarded shares typically vest over a five-year period as long as the director, advisory director, director emeriti, officer or employee remains in service to the Corporation. Once vested, a recipient of restricted stock will have all the rights of a shareholder, including the power to vote and the right to receive dividends. The Corporation recognizes compensation expense for the restricted stock awards based on the fair value of the shares at

the award date.

In fiscal 2008, a total of 4,000 shares of restricted stock were awarded, 6,000 shares were forfeited and 11,350 shares were vested and distributed. In fiscal 2007, a total of 62,750 shares of restricted stock were awarded and there was no other activity. As of June 30, 2008 and 2007, there were 124,250 shares and 122,250 shares of restricted stock, respectively, available for future awards.

A summary of the status of the Corporation's restricted stock since the inception of the plan and changes during the fiscal years ended June 30, 2008 and 2007 are presented below:

Equity Incentive Plan - Restricted Stock	Shares	Weighted-Average Award Date Fair Value
Unvested at July 1, 2006	-	-
Awarded	62,750	$ 26.49
Vested and distributed	-	-
Forfeited	-	-
Unvested at June 30, 2007	62,750	$ 26.49
Expected to vest at June 30, 2007	50,200	$ 26.49
Unvested at July 1, 2007	62,750	$ 26.49
Awarded	4,000	$ 18.09
Vested and distributed	(11,350)	$ 26.49
Forfeited	(6,000)	$ 26.49
Unvested at June 30, 2008	49,400	$ 25.81
Expected to vest at June 30, 2008	39,520	$ 25.81

As of June 30, 2008 and 2007, the unrecognized compensation expense under the 2006 Plan was $1.4 million and $1.6 million, respectively. The expense is expected to be recognized over a weighted-average period of 3.6 years and 4.6 years, respectively. Similar to options, a forfeiture rate of 20 percent is used for the restricted stock compensation expense calculations for both fiscal years. The fair value of shares vested and distributed during the fiscal year ended June 30, 2008 was $178,000.

Stock Option Plans. The Corporation established the 1996 Stock Option Plan and the 2003 Stock Option Plan (collectively, the "Stock Option Plans") for key employees and eligible directors under which options to acquire up to 1.15 million shares and 352,500 shares of common stock, respectively, may be granted. Under the Stock Option Plans, options may not be granted at a price less than the fair market value at the date of the grant. Options typically vest over a five-year period on a pro-rata basis as long as the employee or director remains an employee or director of the Corporation. The options are exercisable after vesting for up to the remaining term of the original grant. The maximum term of the options granted is 10 years.

On April 28, 2005, the Board of Directors accelerated the vesting of 136,950 unvested stock options, which were previously granted to directors, officers and key employees who had three or more continuous years of service with

the Corporation or an affiliate of the Corporation. The Board believed that it was in the best interest of the shareholders to accelerate the vesting of these options, which were granted prior to January 1, 2004, since it will have a positive impact on the future earnings of the Corporation. This action was taken as a result of SFAS No. 123(R) which the Corporation adopted on July 1, 2005.

As a result of accelerating the vesting of these options, the Corporation recorded a $320,000 charge to compensation expense during the quarter ended June 30, 2005. This charge represents a new measurement of compensation cost

for these options as of the modification date. The modification introduced the potential for an effective renewal of the awards as some of these options may have been forfeited by the holders. This charge will require quarterly adjustment in future periods for actual forfeiture experience. For the fiscal year ended June 30, 2008, a recovery of $23,000 was realized; and since inception, a $301,000 recovery has been realized. The Corporation estimates that the compensation expense related to these options that would have been recognized over their remaining vesting period pursuant to the transition provisions of SFAS No. 123(R) was $1.7 million. Because these options are now fully vested, they are not subject to the provisions of SFAS No. 123(R).

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option valuation model with the assumptions noted in the following table. The expected volatility is based on implied volatility from historical common stock closing prices for the last 84 months (or 30 months for grants prior to September 2006). The expected dividend yield is based on the most recent quarterly dividend on an annualized basis. The expected term is based on the historical experience of all fully vested stock option grants and is reviewed annually. The risk-free interest rate is based on the U.S. Treasury note rate with a term similar to the underlying stock option on the particular grant date.

	Fiscal 2008	Fiscal 2007	Fiscal 2006
Expected volatility range	22%	23%	20% - 21%
Weighted-average volatility	22%	23%	20%
Expected dividend yield	3.6%	2.0%	1.9% - 2.0%
Expected term (in years)	6.9	7.4	7.6 – 7.8
Risk-free interest rate	4.8%	4.5% - 5.0%	4.1% - 4.7%

In fiscal 2008, the total options (under both plans) granted, exercised and forfeited were 50,000 options, 7,500 options and 57,700 options, respectively. In fiscal 2007, the total options (under both plans) granted and exercised were 64,000 options and 51,393 options, respectively. No options were forfeited in fiscal 2007. As of June 30, 2008 and 2007, the number of options available for future grants under the Stock Option Plans were 14,900 options and 42,000 options, respectively.

Notes to Consolidated Financial Statements

The following is a summary of stock option activity under the 1996 and 2003 Plans:

Stock Option Plans	Stock Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value ($000)
Outstanding at July 1, 2005	974,625	$ 14.62		
Granted	19,000	$ 30.03		
Exercised	(403,632)	$ 7.27		
Forfeited	(37,000)	$ 25.83		
Outstanding at June 30, 2006	552,993	$ 19.77	6.92	$ 5,657
Vested and expected to vest at June 30, 2006	503,353	$ 19.18	6.79	$ 5,447
Exercisable at June 30, 2006	344,793	$ 16.66	6.30	$ 4,600
Outstanding at July 1, 2006	552,993	$ 19.77		
Granted	64,000	$ 30.02		
Exercised	(51,393)	$ 19.80		
Forfeited	-	-		
Outstanding at June 30, 2007	565,600	$ 20.93	6.28	$ 2,822
Vested and expected to vest at June 30, 2007	523,980	$ 20.48	6.17	$ 2,795
Exercisable at June 30, 2007	357,500	$ 17.64	5.48	$ 2,689
Outstanding at July 1, 2007	565,600	$ 20.93		
Granted	50,000	$ 19.92		
Exercised	(7,500)	$ 9.15		
Forfeited	(57,700)	$ 25.47		
Outstanding at June 30, 2008	550,400	$ 20.52	5.61	$ 78
Vested and expected to vest at June 30, 2008	519,280	$ 20.24	5.48	$ 78
Exercisable at June 30, 2008	394,800	$ 18.71	4.79	$ 78

The weighted-average grant-date fair value of options granted during the fiscal years ended June 30, 2008, 2007 and 2006 was $3.94, $8.43 and $7.77 per share, respectively. The total intrinsic value of options exercised during the years ended June 30, 2008, 2007 and 2006 was $104,000, $411,000 and $8.3 million, respectively.

As of June 30, 2008 and 2007, there was $1.4 million and $1.4 million of unrecognized compensation expense, respectively, related to non-vested share-based compensation arrangements granted under the 1996 and 2003 Stock Option Plans. The expense is expected to be recognized over a weighted-average period of 2.7 years and 2.6 years, respectively. The forfeiture rate during fiscal 2008 and 2007 was 20%, which was calculated based on the historical experience of all fully vested stock option grants and is reviewed annually.

Management Recognition Plan ("MRP"). The Corporation established the MRP to provide key employees and eligible directors with a proprietary interest in the growth, development and financial success of the Corporation through the award of restricted stock. The Corporation acquired 461,250 shares of its common stock in the open market to fund the MRP in 1997. All of the MRP shares have been awarded. Awarded shares vest over a five-year period as long as the employee or director remains an employee or director of the Corporation. The Corporation recognizes compensation expense for the MRP based on the fair value of the shares at the award date. MRP

Notes to Consolidated Financial Statements

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compensation expense was $4,000, $58,000 and $92,000 for the years ended June 30, 2008, 2007 and 2006, respectively.

A summary of the activity of the Corporation's MRP is presented below:

Management Recognition Plan	Shares	Weighted-Average Award Date Fair Value
Unvested at July 1, 2005	23,058	$ 11.17
Awarded	-	-
Vested and distributed	(13,470)	10.00
Forfeited	-	-
Unvested at June 30, 2006	9,588	$ 12.81
Awarded	-	-
Vested and distributed	(5,820)	12.26
Forfeited	-	-
Unvested at June 30, 2007	3,768	$13.67
Awarded	-	-
Vested and distributed	(3,768)	13.67
Forfeited	-	-
Unvested at June 30, 2008	-	-

As of June 30, 2008, the MRP was fully distributed and is no longer an active plan. As of June 30, 2007, the unrecognized compensation expense related to the non-vested share-based compensation arrangements awarded under the MRP was $4,000. The forfeiture rate during fiscal 2008 and 2007 was 0%, which was based on the full retention of the remaining participants. The fair value of shares vested during the years ended June 30, 2008, 2007 and 2006, was $85,000, $174,000 and $366,000, respectively.

13. Earnings Per Share:

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted average number of shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would then share in the earnings of the Corporation. There were 725,700 options, 752,900 options and 552,993 options outstanding as of June 30, 2008, 2007 and 2006, respectively. As of June 30, 2008, 2007 and 2006, there were 658,200 options, 292,800 options and 10,000 options, respectively, excluded from the diluted EPS computation as their effect was anti-dilutive.

	For the Year Ended June 30, 2008		
(Dollars in Thousands, Except Share Amount)	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS	$ 860	6,171,480	$ 0.14

Effect of dilutive shares:			
Stock options		42,649	
Restricted stock		296	
Diluted EPS	$ 860	6,214,425	$ 0.14

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Notes to Consolidated Financial Statements

	For the Year Ended June 30, 2007		
(Dollars in Thousands, Except Share Amount)	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS	$ 10,451	6,557,550	$ 1.59
Effect of dilutive shares:			
Stock options		114,274	
Restricted stock		3,893	
Diluted EPS	$ 10,451	6,675,717	$ 1.57

	For the Year Ended June 30, 2006		
(Dollars in Thousands, Except Share Amount)	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS	$ 19,636	6,704,865	$ 2.93
Effect of dilutive shares:			
Stock options		249,048	
Restricted stock		6,409	
Diluted EPS	$ 19,636	6,960,322	$ 2.82

14. Commitments and Contingencies:

The Corporation is involved in various legal matters associated with its normal operations. In the opinion of management, these matters will be resolved without material effect on the Corporation's financial position, results of operations or cash flows.

The Corporation conducts a portion of its operations in leased facilities and has software maintenance contracts under non-cancelable agreements classified as operating leases. The following is a schedule of minimum rental payments under such operating leases, which expire in various years:

Year Ending June 30,	Amount (In Thousands)
2009	$ 973
2010	771
2011	575
2012	421
2013	390
Thereafter	706
Total minimum payments required	$ 3,836

Lease expense under operating leases was approximately $919,000, $1.2 million and $1.0 million for the years ended June 30, 2008, 2007 and 2006, respectively.

In the ordinary course of business, the Corporation enters into contracts with third parties under which the third parties provide services on behalf of the Corporation. In many of these contracts, the Corporation agrees to

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indemnify the third party service provider under certain circumstances. The terms of the indemnity vary from contract to contract and the amount of the indemnification liability, if any, cannot be determined. The Corporation also enters into other contracts and agreements; such as, loan sale agreements, litigation settlement agreements, confidentiality agreements, loan servicing agreements, leases and subleases, among others, in which the Corporation agrees to indemnify third parties for acts by our agents, assignees and/or sub-lessees, and employees. Due to the nature of these indemnification provisions, the Corporation cannot calculate our aggregate potential exposure under them.

Pursuant to their bylaws, the Corporation and its subsidiaries provide indemnification to directors, officers and, in some cases, employees and agents against certain liabilities incurred as a result of their service on behalf of or at the request of the Corporation and its subsidiaries. It is not possible for us to determine the aggregate potential exposure resulting from the obligation to provide this indemnity.

15. Derivatives and Other Financial Instruments with Off-Balance Sheet Risks:

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, in the form of originating loans or providing funds under existing lines of credit, and forward loan sale agreements to third parties. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the accompanying Consolidated Statements of Financial Condition. The Corporation's exposure to credit loss, in the event of non-performance by the counterparty to these financial instruments, is represented by the contractual amount of these instruments. The Corporation uses the same credit policies in making commitments to extend credit as it does for on-balance sheet instruments.

	June 30,	
Commitments	2008	2007
(In Thousands)		
Undisbursed loan funds – Construction loans	$ 7,864	$ 25,484
Undisbursed lines of credit – Mortgage loans	4,880	3,326
Undisbursed lines of credit – Commercial business loans	6,833	14,532
Undisbursed lines of credit – Consumer loans	1,672	1,637
Commitments to extend credit on loans held for investment	6,232	9,387
	$ 27,481	$ 54,366

Commitments to extend credit are agreements to lend money to a customer at some future date as long as all conditions have been met in the agreement. These commitments generally have expiration dates within 60 days of the commitment date and may require the payment of a fee. Since some of these commitments are expected to expire, the total commitment amount outstanding does not necessarily represent future cash requirements. The Corporation evaluates each customer's creditworthiness on a case-by-case basis prior to issuing a commitment. At June 30, 2008 and 2007, interest rates on commitments to extend credit ranged from 5.00% to 7.00% and 5.88% to 12.00%, respectively.

In an effort to minimize its exposure to interest rate fluctuations on commitments to extend credit where the underlying loan will be sold, the Corporation may enter into forward loan sale agreements to sell certain dollar amounts of fixed rate and adjustable rate loans to third parties. These agreements specify the minimum maturity of the loans, the yield to the purchaser, the servicing spread to the Corporation (if servicing is retained), the maximum principal amount of all loans to be delivered and the maximum principal amount of individual loans to be delivered. The Corporation typically satisfies these forward loan sale agreements with its current loan production. If the

Notes to Consolidated Financial Statements

Corporation is unable to reasonably predict the dollar amounts of loans which may not fund, the Corporation may enter into "best efforts" loan sale agreements rather than "mandatory" loan sale agreements.

In addition to the instruments described above, the Corporation may also purchase over-the-counter put option contracts (with expiration dates that generally coincide with the terms of the commitments to extend credit), which mitigates the interest rate risk inherent in commitments to extend credit. In addition to put option contracts, the Corporation may purchase call option contracts to adjust its risk positions. The contract amounts of these instruments reflect the extent of involvement the Corporation has in this particular class of financial instruments. The Corporation's exposure to loss on these financial instruments is limited to the premiums paid for the put and call option contracts. Put and call options are adjusted to market in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. There were no call or put option contracts outstanding at June 30, 2008. As of June 30, 2007, the notional value of put option contracts were $11.5 million with a fair value of $112,000 and the notional value of call option contracts were $1.0 million with a fair value of $4,000. The Corporation may also enter into forward commitments to purchase MBS (commonly referred to as a "synthetic call") to lock in profits or losses from its put option contracts. The Corporation did not have forward commitments to purchase MBS at June 30, 2008. As of June 30, 2007, total forward commitments to purchase MBS were $6.5 million with a fair value of $23,000.

In accordance with SFAS No. 133 and interpretations of the FASB's Derivative Implementation Group, the fair value of the commitments to extend credit on loans to be held for sale, forward loan sale agreements, forward commitments to purchase MBS, put option and call option contracts are recorded at fair value on the balance sheet, and are included in other assets or other liabilities. The Corporation does not apply hedge accounting to its derivative financial instruments; therefore, all changes in fair value are recorded in earnings. The net impact of derivative financial instruments on the Consolidated Statements of Operations during the years ended June 30, 2008, 2007 and 2006 was a loss of $317,000, a gain of $212,000 and a gain of $71,000, respectively.

	June 30, 2008		June 30, 2007	
Derivative Financial Instruments	Amount	Fair Value	Amount	Fair Value
(In Thousands)				
Commitments to extend credit on loans to be held for sale (1)	$ 23,191	$ (304)	$ 35,130	$ 24
Forward loan sale agreements (2)	(51,652)	-	(27,012)	(51)
Forward commitments to purchase MBS	-	-	6,500	23
Put option contracts	-	-	(11,500)	112
Call option contracts	-	-	1,000	4
Total	$ (28,461)	$ (304)	$ 4,118	$ 112

(1) Net of an estimated 48.0% of commitments at June 30, 2008 and 34.7% of commitments at June 30, 2007, which may not fund.

(2) "Best efforts" at June 30, 2008 and "mandatory" at June 30, 2007.

16. Fair Values of Financial Instruments:

The reported fair values of financial instruments are based on various factors. In some cases, fair values represent quoted market prices for identical or comparable instruments. In other cases, fair values have been estimated based on assumptions concerning the amount and timing of estimated future cash flows, assumed discount rates and other factors reflecting varying degrees of risk. The estimates are subjective in nature and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates. Accordingly, the reported fair values

may not represent actual values of the financial instruments that could have been realized as of year-end or that will be realized in the future. The following methods and assumptions were used to estimate fair value of each class of significant financial instrument:

Cash and cash equivalents: The carrying amount of these financial assets approximates the fair value.

Investment securities: The fair value of investment securities is based on quoted market prices.

Loans held for investment: For loans that reprice frequently at market rates, the carrying amount approximates the fair value. For fixed-rate loans, the fair value is determined by either (i) discounting the estimated future cash flows of such loans over their estimated remaining contractual maturities using a current interest rate at which such loans would be made to borrowers, or (ii) quoted market prices. The allowance for loan losses is subtracted as an estimate of the underlying credit risk.

Loans held for sale: Fair values for loans held for sale are based on the lower of cost or quoted market prices.

Receivable from sale of loans: The carrying value for the receivable from sale of loans approximates fair value because of the short-term nature of the financial instruments.

Accrued interest receivable/payable: The carrying value for accrued interest receivable/payable approximates fair value because of the short-term nature of the financial instruments.

FHLB – San Francisco stock: The carrying amount reported for FHLB – San Francisco stock approximates fair value. If redeemed, the Corporation will receive an amount equal to the par value of the stock.

Deposits: The fair value of the deposits is estimated using a discounted cash flow calculation. The discount rate on such deposits is based upon rates currently offered for borrowings of similar remaining maturities.

Borrowings: The fair value of borrowings has been estimated using a discounted cash flow calculation. The discount rate on such borrowings is based upon rates currently offered for borrowings of similar remaining maturities.

Commitments: Commitments to extend credit on existing obligations are discounted in a manner similar to loans held for investment.

Derivative Financial Instruments: The fair value of the derivative financial instruments are based upon quoted market prices, current market bids, outstanding forward loan sale agreements and estimates from independent pricing sources.

Notes to Consolidated Financial Statements

The carrying amount and fair values of the Corporation's financial instruments were as follows:

	June 30, 2008		June 30, 2007	
(In Thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	$ 15,114	$ 15,114	$ 12,824	$ 12,824
Investment securities	153,102	153,102	150,843	150,679
Loans held for investment, net	1,368,137	1,372,012	1,350,696	1,343,574
Loans held for sale	28,461	28,792	1,337	1,337
Receivable from sale of loans	-	-	60,513	60,513
Accrued interest receivable	7,273	7,273	7,235	7,235
FHLB – San Francisco stock	32,125	32,125	43,832	43,832
Financial liabilities:				
Deposits	1,012,410	983,869	1,001,397	961,507
Borrowings	479,335	482,364	502,774	497,636
Accrued interest payable	2,018	2,018	2,322	2,322
Derivative Financial Instruments:				
Commitments to extend credit on loans to be held for sale	(304)	(304)	24	24
Forward loan sale agreements	-	-	(51)	(51)
Forward commitments to purchase MBS	-	-	23	23
Put option contracts	-	-	112	112
Call option contracts	-	-	4	4

Notes to Consolidated Financial Statements

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17. Operating Segments:

The segment reporting is organized consistent with the Corporation's executive summary and operating strategy. The business activities of the Corporation, primarily through the Bank and its subsidiary, consist of community banking and mortgage banking. Community banking operations primarily consist of accepting deposits from customers within the communities surrounding the Bank's full service offices and investing those funds in single-family, multi-family, commercial real estate, construction, commercial business, consumer and other loans. Mortgage banking operations primarily consist of the origination and sale of mortgage loans secured by single-family residences. The following table and discussions explain the results of the Corporation's two major operating segments, community banking ("Provident Bank') and mortgage banking ("Provident Bank Mortgage").

The following tables illustrate the Corporation's operating segments for the years ended June 30, 2008, 2007 and 2006, respectively.

	Year Ended June 30, 2008		
(In Thousands)	Provident Bank	Provident Bank Mortgage	Consolidated Total
Net interest income (loss), before provision for loan losses	$ 41,634	$ (198)	$ 41,436
Provision for loan losses	8,905	4,203	13,108
Net interest income (loss), after provision for loan losses	32,729	(4,401)	28,328
Non-interest income:			
Loan servicing and other fees	206	1,570	1,776
Gain on sale of loans, net	49	955	1,004
Deposit account fees	2,954	-	2,954
Loss on sale and operations of real estate owned acquired in the settlement of loans, net	(777)	(1,906)	(2,683)
Other	2,152	8	2,160
Total non-interest income	4,584	627	5,211
Non-interest expense:			
Salaries and employee benefits	14,168	4,826	18,994
Premises and occupancy	2,073	757	2,830
Operating and administrative expenses	4,699	3,788	8,487
Total non-interest expenses	20,940	9,371	30,311
Income (loss) before income taxes	16,373	(13,145)	3,228
Provision (benefit) for income taxes	9,373	(7,005)	2,368
Net income (loss)	$ 7,000	$ (6,140)	$ 860
Total assets, end of period		$ 30,944	$ 1,632,447

$ 1,601,503

Notes to Consolidated Financial Statements

	Year Ended June 30, 2007		
(In Thousands)	Provident Bank	Provident Bank Mortgage	Consolidated Total
Net interest income, before provision for loan losses	$ 41,072	$ 651	$ 41,723
Provision for loan losses	4,192	886	5,078
Net interest income (loss), after provision for loan losses	36,880	(235)	36,645
Non-interest income:			
Loan servicing and other fees	(311)	2,443	2,132
Gain on sale of loans, net	210	9,108	9,318
Deposit account fees	2,087	-	2,087
Gain on sale of real estate held for investment	2,313	-	2,313
Loss on sale and operations of real estate owned acquired in the settlement of loans, net	(96)	(21)	(117)
Other	1,828	-	1,828
Total non-interest income	6,031	11,530	17,561
Non-interest expense:			
Salaries and employee benefits	14,190	8,677	22,867
Premises and occupancy	2,152	1,162	3,314
Operating and administrative expenses	4,139	4,311	8,450
Total non-interest expenses	20,481	14,150	34,631
Income (loss) before income taxes	22,430	(2,855)	19,575
Provision (benefit) for income taxes	10,245	(1,121)	9,124
Net income (loss)	$ 12,185	$ (1,734)	$ 10,451
Total assets, end of period	$ 1,584,011	$ 64,912	$ 1,648,923

Notes to Consolidated Financial Statements

(In Thousands)	Year Ended June 30, 2006 Provident Bank	Provident Bank Mortgage	Consolidated Total
Net interest income, before provision for loan losses	$ 41,849	$ 2,143	$ 43,992
Provision for loan losses	1,093	41	1,134
Net interest income, after provision for loan losses	40,756	2,102	42,858
Non-interest income:			
Loan servicing and other fees	(1,504)	4,076	2,572
Gain on sale of loans, net	491	12,990	13,481
Deposit account fees	2,093	-	2,093
Gain on sale of real estate held for investment	6,335	-	6,335
Gain on sale and operations of real estate owned acquired in the settlement of loans, net	20	-	20
Other	1,707	1	1,708
Total non-interest income	9,142	17,067	26,209
Non-interest expense:			
Salaries and employee benefits	13,389	7,995	21,384
Premises and occupancy	2,041	995	3,036
Operating and administrative expenses	5,275	4,060	9,335
Total non-interest expenses	20,705	13,050	33,755
Income before income taxes	29,193	6,119	35,312
Provision for income taxes	12,866	2,810	15,676
Net income	$ 16,327	$ 3,309	$ 19,636
Total assets, end of period	$ 1,518,335	$ 106,117	$ 1,624,452

The information above was derived from the internal management reporting system used by management to measure performance of the segments.

The Corporation's internal transfer pricing arrangements determined by management primarily consist of the following:

1. Borrowings for PBM are indexed monthly to the higher of the three-month FHLB – San Francisco advance rate on the first Friday of the month plus 50 basis points or the Bank's cost of funds for the prior month.
2. PBM receives servicing released premiums for new loans transferred to the Bank's loans held for investment. The servicing released premiums in the years ended June 30, 2008, 2007 and 2006 were $1.2 million, $2.1 million and $3.3 million, respectively.
3. PBM receives a premium (gain on sale of loans) or a discount (loss on sale of loans) for the new loans transferred to the Bank's loans held for investment. The loss on sale of loans in the years ended June 30, 2008, 2007 and 2006 was $17,000, $192,000 and $128,000, respectively.
4.

Loan servicing costs are charged to PBM by the Bank based on the number of loans held for sale multiplied by a fixed fee which is subject to management's review. The loan servicing costs in the years ended June 30, 2008, 2007 and 2006 were $37,000, $65,000 and $80,000, respectively.

5. The Bank allocates quality assurance costs to PBM for its loan production, subject to management's review. Quality assurance costs allocated to PBM in the years ended June 30, 2008, 2007 and 2006 were $133,000, $129,000 and $165,000, respectively.

Notes to Consolidated Financial Statements

6. The Bank allocates loan vault service costs to PBM for its loan production, subject to management's review. The loan vault service costs allocated to PBM in the years ended June 30, 2008, 2007 and 2006 were $61,000, $72,000 and $70,000, respectively.
7. Office rents for PBM offices located in the Bank branches or offices are internally charged based on the square footage used. Office rents allocated to PBM in the years ended June 30, 2008, 2007 and 2006 were $127,000, $151,000 and $189,000, respectively.
8. A management fee, which is subject to regular review, is charged to PBM for services provided by the Bank. The management fee in the years ended June 30, 2008, 2007 and 2006 was $1.2 million, $1.1 million and $1.1 million, respectively.

18. Holding Company Condensed Financial Information:

This information should be read in conjunction with the other notes to the consolidated financial statements. The following is the condensed statements of financial condition for Provident Financial Holdings (Holding Company only) as of June 30, 2008 and 2007 and condensed statements of operations and cash flows for each of the three years for the period ended June 30, 2008.

Condensed Statements of Financial Condition

	June 30,	
(In Thousands)	2008	2007
Assets		
Cash and cash equivalents	$ 5,568	$ 1,405
Investment in subsidiary	118,460	126,922
Other assets	159	638
	$ 124,187	$ 128,965
Liabilities and Stockholders' Equity		
Other liabilities	$ 207	$ 168
Stockholders' equity	123,980	128,797
	$ 124,187	$ 128,965

Condensed Statements of Operations

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Interest and other income	$ 91	$ 119	$ 146
General and administrative expenses	661	630	657

Loss before equity in net earnings of the subsidiary	(570)	(511)	(511)
Equity in net earnings of the subsidiary	1,191	10,744	19,931
Income before income taxes	621	10,233	19,420
Benefit from income taxes	(239)	(218)	(216)
Net income	$ 860	$ 10,451	$ 19,636

Notes to Consolidated Financial Statements

Condensed Statements of Cash Flows

	Year Ended June 30,		
(In Thousands)	2008	2007	2006
Cash flows from operating activities:			
Net income	$ 860	$ 10,451	$ 19,636
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in net earnings of the subsidiary	(1,191)	(10,744)	(19,931)
Tax benefit from non-qualified equity compensation	(6)	(81)	(2,572)
Decrease in other assets	417	484	4,715
Increase in other liabilities	39	67	73
Net cash provided by operating activities	119	177	1,921
Cash flow from investing activities:			
Cash dividend received from the Bank	12,000	20,000	6,000
Net cash provided by investing activities	12,000	20,000	6,000
Cash flow from financing activities:			
ESOP loan payment	67	131	164
Exercise of stock options	69	1,017	2,933
Tax benefit from non-qualified equity compensation	6	81	2,572
Treasury stock purchases	(4,097)	(18,703)	(10,478)
Cash dividends	(4,001)	(4,630)	(4,054)
Net cash used for financing activities	(7,956)	(22,104)	(8,863)
Net increase (decrease) in cash and cash equivalent	4,163	(1,927)	(942)
Cash and cash equivalents at beginning of year	1,405	3,332	4,274
Cash and cash equivalents at end of year	$ 5,568	$ 1,405	$ 3,332

Notes to Consolidated Financial Statements

19. Quarterly Results of Operations (Unaudited):

The following tables set forth the quarterly financial data for the fiscal years ended June 30, 2008 and 2007.

		For Fiscal Year 2008			
(Dollars in Thousands, Except Per Share Amount)	For the Year Ended June 30, 2008	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$ 95,749	$ 23,947	$ 24,027	$ 24,039	$ 23,736
Interest expense	54,313	12,171	13,308	14,471	14,363
Net interest income	41,436	11,776	10,719	9,568	9,373
Provision for loan losses	13,108	6,299	3,150	2,140	1,519
Net interest income, after provision for loan losses	28,328	5,477	7,569	7,428	7,854
Non-interest income	5,211	285	1,604	1,947	1,375
Non-interest expense	30,311	7,924	7,299	7,320	7,768
Income (loss) before income taxes	3,228	(2,162)	1,874	2,055	1,461
Provision (benefit) for income taxes	2,368	(409)	917	1,011	849
Net income (loss)	$ 860	$ (1,753)	$ 957	$ 1,044	$ 612
Basic earnings (loss) per share	$ 0.14	$ (0.28)	$ 0.16	$ 0.17	$ 0.10
Diluted earnings (loss) per share	$ 0.14	$ (0.28)	$ 0.15	$ 0.17	$ 0.10

Notes to Consolidated Financial Statements

(Dollars in Thousands, Except Per Share Amount)	For the Year Ended June 30, 2007	For Fiscal Year 2007 Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$ 100,968	$ 25,148	$ 26,164	$ 25,469	$ 24,187
Interest expense	59,245	15,306	15,507	14,984	13,448
Net interest income	41,723	9,842	10,657	10,485	10,739
Provision (recovery) for loan losses	5,078	(490)	1,185	3,746	637
Net interest income, after provision (recovery) for loan losses	36,645	10,332	9,472	6,739	10,102
Non-interest income	17,561	2,214	3,679	4,274	7,394
Non-interest expense	34,631	8,938	8,761	8,483	8,449
Income before income taxes	19,575	3,608	4,390	2,530	9,047
Provision for income taxes	9,124	1,777	2,031	1,295	4,021
Net income	$ 10,451	$ 1,831	$ 2,359	$ 1,235	$ 5,026
Basic earnings per share	$ 1.59	$ 0.29	$ 0.36	$ 0.19	$ 0.74
Diluted earnings per share	$ 1.57	$ 0.28	$ 0.36	$ 0.18	$ 0.73

20. Subsequent Events (Unaudited):

Cash dividend

On July 31, 2008, the Corporation announced a cash dividend of $0.05 per share on the Corporation’s outstanding shares of common stock for shareholders of record at the close of business on August 25, 2008, payable on September 19, 2008.

Shareholder Information

ANNUAL MEETING

The annual meeting of shareholders will be held at the Riverside Art Museum at 3425 Mission Inn Avenue, Riverside, California on Tuesday, November 25, 2008 at 11:00 a.m. (Pacific). A formal notice of the meeting, together with a proxy statement and proxy form, will be mailed to shareholders.

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10 Commerce Drive
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MARKET INFORMATION

Provident Financial Holdings, Inc. is traded on the NASDAQ Global Select Market under the symbol PROV.

Shareholder Information

FINANCIAL INFORMATION

Requests for copies of the Form 10-K and Forms 10-Q filed with the Securities and Exchange Commission should be directed in writing to:

Donavon P. Ternes
Chief Operating Officer and Chief Financial Officer
Provident Financial Holdings, Inc.
3756 Central Avenue
Riverside, CA 92506

CORPORATE PROFILE

Provident Financial Holdings, Inc. (the "Corporation"), a Delaware corporation, was organized in January 1996 for the purpose of becoming the holding company for Provident Savings Bank, F.S.B. (the "Bank") upon the Bank's conversion from a federal mutual to a federal stock savings bank ("Conversion"). The Conversion was completed on June 27, 1996. The Corporation does not engage in any significant activity other than holding the stock of the Bank. The Bank serves the banking needs of select communities in Riverside and San Bernardino Counties and has mortgage lending operations in Southern and Northern California.

Board of Directors and Senior Officers

Board of Directors

Joseph P. Barr, CPA
Principal
Swenson Accountancy Corporation

Bruce W. Bennett
President
Community Care & Rehabilitation Center

Craig G. Blunden
Chairman, President and CEO
Provident Bank

Debbi H. Guthrie
Private Investor

Robert G. Schrader
Retired Executive Vice President and COO
Provident Bank

Roy H. Taylor
Chief Executive Officer
Hub International of California
Insurance Services, Inc.

William E. Thomas
Principal
William E. Thomas, Inc.,
A Professional Law Corporation

Senior Officers

Provident Financial Holdings, Inc.

Craig G. Blunden
Chairman, President and CEO

Donavon P. Ternes
Chief Operating Officer
Chief Financial Officer
Corporate Secretary

Provident Bank

Craig G. Blunden
Chairman, President and CEO

Richard L. Gale
Senior Vice President
Provident Bank Mortgage

Kathryn R. Gonzales
Senior Vice President
Retail Banking

Lilian Salter
Senior Vice President
Chief Information Officer

Donavon P. Ternes
Executive Vice President
Chief Operating Officer
Chief Financial Officer
Corporate Secretary

David S. Weiant
Senior Vice President
Chief Lending Officer

Provident Locations

RETAIL BANKING CENTERS

Blythe
350 E. Hobson Way
Blythe, CA 92225

Canyon Crest
5225 Canyon Crest Drive, Suite 86
Riverside, CA 92507

Corona
487 Magnolia Avenue, Suite 101
Corona, CA 92879

Corporate Office
3756 Central Avenue
Riverside CA 92506

Downtown Business Center
4001 Main Street
Riverside, CA 92501

Hemet
1690 E. Florida Avenue
Hemet, CA 92544

La Sierra
3312 La Sierra Avenue, Suite 105
Riverside, CA 92503

Moreno Valley I
12460 Heacock Street
Moreno Valley, CA 92553

Moreno Valley II (September 2008)
16110 Perris Boulevard
Moreno Valley, CA 92553

WHOLESALE OFFICES

Pleasanton
5934 Gibraltar Drive, Suite 102
Pleasanton, CA 94588

Rancho Cucamonga
10370 Commerce Center Drive, Suite 200
Rancho Cucamonga, CA 91730

RETAIL OFFICES

Glendora
1200 E. Route 66, Suite 102
Glendora, CA 91740

Riverside
6529 Riverside Avenue, Suite 160
Riverside, CA 92506

Orangecrest
19348 Van Buren Boulevard, Suite 119
Riverside, CA 92508

Rancho Mirage
71-991 Highway 111
Ranch Mirage, CA 92270

Redlands
125 E. Citrus Avenue
Redlands, CA 92373

Sun City
27010 Sun City Boulevard
Sun City, CA 92586

Temecula
40325 Winchester Road
Temecula, CA 92591

Customer Information 1-800-442-5201 or www.myprovident.com

Corporate Office
3756 Central Avenue, Riverside, CA 92506
(951) 686-6060

www.myprovident.com

NASDAQ Global Select Market - PROV

EXHIBIT 23.1

Consent of Independent Registered Public Accounting Firm

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in Registration Statement Nos. 333-30935, 333-112700, and 333-140229 on Form S-8 of our reports dated September 12, 2008, relating to the consolidated financial statements of Provident Financial Holdings, Inc. and subsidiary (the “Corporation”) and the effectiveness of the Corporation’s internal control over financial reporting, appearing in this Annual Report on Form 10-K of Provident Financial Holdings, Inc. for the year ended June 30, 2008.

/s/ DELOITTE & TOUCHE LLP

Costa Mesa, California
September 12, 2008

EXHIBIT 31.1

Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Craig G. Blunden, certify that:

1. I have reviewed this Annual Report on Form 10-K of Provident Financial Holdings, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15-(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b)

Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 12, 2008

/s/ Craig G. Blunden
Craig G. Blunden
Chairman, President and Chief Executive Officer

EXHIBIT 31.2

Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Donavon P. Ternes, certify that:

1. I have reviewed this Annual Report on Form 10-K of Provident Financial Holdings, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15-(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b)

Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 12, 2008

/s/Donavon P. Ternes
Donavon P. Ternes
Chief Operating Officer and Chief Financial Officer

EXHIBIT 32

Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Annual Report on Form 10-K of Provident Financial Holdings, Inc. (the "Corporation") for the fiscal year ended June 30, 2008 (the "Report"), I, Craig G. Blunden, Chairman, President and Chief Executive Officer of the Corporation, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation as of the dates and for the periods presented in the financial statements included in the Report.

Date: September 12, 2008

/s/Craig G. Blunden
Craig G. Blunden
Chairman, President and Chief Executive Officer

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Annual Report on Form 10-K of Provident Financial Holdings, Inc. (the "Corporation") for the fiscal year ended June 30, 2008 (the "Report"), I, Donavon P. Ternes, Chief Operating Officer and Chief Financial Officer of the Corporation, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation as of the dates and for the periods presented in the financial statements included in the Report.

Date: September 12, 2008

/s/Donavon P. Ternes
Donavon P. Ternes
Chief Operating Officer and Chief Financial Officer