

SECOND QUARTER REPORT

To Our Shareholders:

The first half of 2009 has proven to be no less challenging than last year, with the economy showing little, if any definitive improvement.

Your Bank continues to “hold the line” with regard to growth, in an effort to maintain adequate capital levels and asset quality. Our loan portfolio, while reflecting some deterioration in performance, remains well collateralized, and significant losses have not materialized. Having said that, the Bank continues to increase its loss reserves as a precautionary measure.

While caution and conservatism continue to be the guidelines under which we operate, we recognize that there are significant opportunities for growth as consumers become disenchanted with our competition. Surely, the “big” banks have left consumers bewildered by virtue of their well-publicized troubles, and smaller banks have pulled in the reins to the extent that “business as usual” has become a thing of the past.

Being cognizant of growth limitations due to the need to maintain capital levels, much effort has been expended in trying to develop new sources of capital to fuel the Bank’s growth. Obviously, in this economy, capital raising has been challenging at best. We are confident that we will succeed in raising additional capital which will enable us to take advantage of some of these growth opportunities. In the meantime, we concentrate on controlling expenses, maximizing net interest income, and developing new sources of fee income. Our earnings profile, while still not where we’d like it to be, has improved steadily and, in the absence of our precautionary increases to the loan loss reserve, would reflect moderate profitability.

As the economy stabilizes, and interest rates return to “normal” levels, we anticipate continued improvement in margins which, coupled with normalized new business acquisition, should provide the basis for additional improvements in net earnings. We look forward to reporting these expected improvements in quarters to come.

Your continued confidence in, and support of, First State Bank is greatly appreciated.

Sincerely,

Joseph D. Natale
Chairman & CEO

Theodore M. Kest
President & CFO