EAGLE BANCORP INC
Form 10-K
March 14, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2007

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

For the transition period from to
Commission file number: 0-25923

Eagle Bancorp, Inc.

(Exact Name of Registrant as Specified in its Charter)

Maryland	**52-2061461**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
7815 Woodmont Avenue, Bethesda, Maryland	**20814**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, including area code:
(301) 986-1800

Securities registered pursuant to Section 12(b) of the Act:
Common Stock $.01 par value

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Section 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act Yes o No ý

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

Indicate by check mark if disclosure of delinquent filers in pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act. Yes o No ý

The aggregate market value of the outstanding Common Stock held by nonaffiliates as of June 30, 2007 was approximately $135 million.

As of March 11, 2008, the number of outstanding shares of the Common Stock, $.01 par value, of Eagle Bancorp, Inc. was 9,780,418

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 22, 2008 are incorporated by reference in part III hereof.

Form 10-K Cross Reference Sheet

The following shows the location in this Annual Report on Form 10-K or the Company's Proxy Statement for the Annual Meeting of Stockholders to be held on May 22, 2008, of the information required to be disclosed by the United States Securities and Exchange Commission Form 10-K. References to pages only are to pages in this report.

PART I	**Item 1.**	**Business.** See "Business" at Pages 65 through 69, "Employees" at Page 74, "Market Area and Competition" at Pages 75 through 76 and "Regulation" at Pages 76 through 81.
	Item 1A.	**Risk Factors.** See "Risk Factors" at Pages 69 through 74.
	Item 1B.	**Unresolved Staff Comments.** None.
	Item 2.	**Properties.** See "Properties" at Page 81 through 82.
	Item 3.	**Legal Proceedings.** From time to time the Company is a participant in various legal proceedings incidental to its business. In the opinion of management, the liabilities (if any) resulting from such legal proceedings will not have a material effect on the financial position of the Company.
	Item 4.	**Submission of Matters to a Vote of Security Holders.** No matter was submitted to a vote of the security holders of the Company during the fourth quarter of 2007.
PART II	**Item 5.**	**Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.** See "Market for Common Stock and Dividends" at Pages 32 though 34.
	Item 6.	**Selected Financial Data.** See "Six Year Summary of Financial Information" at Page 3.
	Item 7.	**Management's Discussion and Analysis of Financial Condition and Results of Operation.** See "Management's Discussion and Analysis of Financial Condition and Results of Operation" at Pages 4 through 32.
	Item 7A.	**Quantitative and Qualitative Disclosures About Market Risk.** See "Interest Rate Risk Management Asset/Liability Management and Quantitative and Qualitative Disclosure About Market Risk" at Page 28 through Page 31.
	Item 8.	**Financial Statements and Supplementary Data.** See Consolidated Financial Statements and Notes thereto at Pages 35 through 64.
	Item 9.	**Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.** None.
	Item 9A.	**Controls and Procedures.** See "Disclosure Controls and Procedures" at Page 82 and "Management Report on Internal Control Over Financial Reporting" at Page 83.
	Item 9B.	**Other Information.** None.
PART III	**Item 10.**	**Directors, Executive Officers and Corporate Governance.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors" and "Compliance with Section 16(a) of the Securities Exchange Act of 1934" in the Proxy Statement. The Company has adopted a code of ethics that applies to its Chief Executive Officer and Chief Financial Officer. A copy of the code of ethics will be provided to any person, without charge, upon written request directed to Zandra Nichols, Corporate Secretary, Eagle Bancorp, Inc., 7815 Woodmont Avenue, Bethesda, Maryland 20814. There have been no material changes in the procedures previously disclosed by which shareholders may recommend nominees to the Company's Board of Directors.
	Item 11.	**Executive Compensation.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors Director's Compensation" and "Executive Compensation" in the Proxy Statement.
	Item 12.	**Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.** See "Market for Common Stock and Dividends Securities Authorized for Issuance Under Equity Compensation Plans" at page. The remainder of the information required by this Item is incorporated by reference to the material appearing under the caption "Voting Securities and Principal Shareholders" in the Proxy Statement.
	Item 13.	**Certain Relationships and Related Transactions and Director Independence.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors" and "Certain Relationships and Related Transactions" in the Proxy Statement.
	Item 14.	**Principal Accountant Fees and Services.** The information required by this Item is incorporated by reference to the material appearing under the caption "Independent Registered Public Accounting Firm Fees Paid to Independent Accounting Firm" in the Proxy Statement.
PART IV	**Item 15.**	

Exhibits, Financial Statement Schedules. See "Exhibits and Financial Statements" at Page 85.

Six Year Summary of Selected Financial Data

The following table shows selected historical consolidated financial data for Eagle Bancorp (the "Company"). It should be read in conjunction with the Company's audited consolidated financial statements appearing elsewhere in this report.

	Year Ended December 31,						
	2007	2006	2005	2004	2003	2002	5 Year Compound Growth Rate
	(dollars in thousands except per share data)						
Selected Balances Period End							
Total assets	$ 846,400	$ 773,451	$ 672,252	$ 553,453	$ 442,997	$ 347,829	19%
Total stockholders' equity	81,166	72,916	64,964	58,534	53,012	20,028	32%
Total loans	716,677	625,773	549,212	415,509	317,533	236,860	25%
Total deposits	630,936	628,515	568,893	462,287	335,514	278,434	18%
Selected Balances Averages							
Total assets	$ 800,437	$ 712,297	$ 610,245	$ 487,853	$ 375,802	$ 292,921	22%
Total stockholders' equity	76,760	68,973	61,563	55,507	34,028	18,381	33%
Total loans	659,204	575,854	479,311	353,537	266,811	210,303	26%
Total deposits	634,332	585,621	512,416	397,788	292,953	237,910	22%
Results of Operations							
Interest income	$ 57,077	$ 50,318	$ 36,726	$ 24,195	$ 18,403	$ 16,661	28%
Interest expense	23,729	17,880	8,008	4,328	3,953	5,170	36%
Net interest income	33,348	32,438	28,718	19,867	14,450	11,491	24%
Provision for credit losses	1,643	1,745	1,843	675	1,175	843	14%
Net interest income after provision for credit losses	31,705	30,693	26,875	19,192	13,275	10,648	24%
Noninterest income	5,186	3,846	3,998	3,753	2,850	2,107	20%
Noninterest expense	24,921	21,824	18,960	14,952	11,007	8,530	24%
Income before taxes	11,970	12,715	11,913	7,993	5,118	4,225	23%
Income tax expense	4,269	4,690	4,369	2,906	1,903	1,558	22%
Net income	7,701	8,025	7,544	5,087	3,215	2,667	24%
Dividends declared	2,302	2,147	1,994				
Per Share Data(1)							
Net income, basic	$ 0.80	$ 0.85	$ 0.82	$ 0.56	$ 0.49	$ 0.54	8%
Net income, diluted	0.78	0.81	0.77	0.53	0.46	0.51	9%
Book value	8.35	7.69	6.95	6.38	5.85	4.09	15%
Dividends declared per share	0.24	0.23	0.22				
Dividend payout ratio(2)	29.89%	27.06%	26.42%				
Financial Ratios							
Return on average assets	0.96%	1.13%	1.24%	1.04%	0.86%	0.91%	
Return on average equity	10.03%	11.63%	12.25%	9.16%	9.45%	14.51%	
Average equity to average assets	9.59%	9.68%	10.09%	11.38%	9.05%	6.28%	
Net interest margin	4.37%	4.81%	4.99%	4.35%	4.14%	4.16%	
Efficiency ratio(3)	64.67%	60.15%	57.95%	63.30%	63.62%	62.73%	

(1)

Presented giving retroactive effect to stock splits in the form of 30% stock dividends paid on July 5, 2006 and February 28, 2005.

(2)

Computed by dividing dividends declared per share by net income per share.

(3) Computed by dividing noninterest expense by the sum of net interest income and noninterest income.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of Eagle Bancorp, Inc. (the "Company") and its subsidiaries, EagleBank (the "Bank") and Eagle Commercial Ventures ("ECV"). This discussion and analysis should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto, appearing elsewhere in this report.

This report contains forward looking statements within the meaning of the Securities Exchange Act of 1934, as amended, including statements of goals, intentions, and expectations as to future trends, plans, events or results of Company operations and policies and regarding general economic conditions. In some cases, forward looking statements can be identified by use of such words as "may", "will", "anticipate", "believes", "expects", "plans", "estimates", "potential", "continue", "should", and similar words or phases. These statements are based upon current and anticipated economic conditions, nationally and in the Company's market, interest rates and interest rate policy, competitive factors and other conditions which, by their nature, are not susceptible to accurate forecast, and are subject to significant uncertainty. Because of these uncertainties and the assumptions on which this discussion and the forward looking statements are based, actual future operations and results in the future may differ materially from those indicated herein. Readers are cautioned against placing undue reliance on any such forward looking statements.

GENERAL

The Company is a growth oriented, one-bank holding company headquartered in Bethesda, Maryland. We provide general commercial and consumer banking services through our wholly owned banking subsidiary EagleBank, a Maryland chartered bank which is a member of the Federal Reserve System. We were organized in October 1997, to be the holding company for the Bank. The Bank was organized as an independent, community oriented, and full-service banking alternative to the super regional financial institutions, which dominate our primary market area. Our philosophy is to provide superior, personalized service to our customers. We focus on relationship banking, providing each customer with a number of services, becoming familiar with and addressing customer needs in a proactive, personalized fashion.

The Company offers a broad range of commercial banking services to our business and professional clients as well as full service consumer banking services to individuals living and/or working primarily in our service area. We emphasize providing commercial banking services to sole proprietors, small and medium-sized businesses, partnerships, corporations, non-profit organizations and associations, and investors living and working in and near our primary service area. A full range of retail banking services are offered to accommodate the individual needs of both corporate customers as well as the community we serve. These services include the usual deposit functions of commercial banks, including business and personal checking accounts, "NOW" accounts and money market and savings accounts, business, construction, and commercial loans, equipment leasing, residential mortgages and consumer loans and cash management services. We have developed significant expertise and commitment as an SBA lender, have been designated a Preferred Lender by the Small Business Administration (SBA), and are a leading community bank SBA lender in the Washington D.C. district.

PENDING ACQUISITION

In December 2007, the Company announced the signing of a definitive agreement to acquire Fidelity & Trust Financial Corporation ("Fidelity & Trust"), parent of Fidelity & Trust Bank. At September 30, 2007, Fidelity & Trust had $452 million of assets. Fidelity & Trust Bank operates six locations, with one in Northern Virginia, three in Montgomery County, Maryland and two in the District of Columbia. The transaction is subject to regulatory and shareholder approvals and the satisfaction of other

conditions, as set forth in the merger agreement. The transaction is currently anticipated to be completed mid 2008. For further information about the proposed acquisition, please refer to "Business Pending Acquisition" at page 61.

Refer to "Note 16 of Notes to Consolidated Financial Statements" on page 54 for further information on this transaction.

CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and follow general practices within the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not 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 contingent upon 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 investment securities available for sale are based either on quoted market prices or are provided by other third-party sources, when available. As of December 31, 2007, the Company had not adopted the provisions of Statement on Financial Accounting Standards ("SFAS") 157, which establishes a common definition of fair value.

The allowance for credit losses is an estimate of the losses that may be sustained in our loan portfolio. The allowance is based on two principles of accounting: (a) Statement on Financial Accounting Standards ("SFAS") 5, "Accounting for Contingencies", which requires that losses be accrued when they are probable of occurring and are estimable and (b) SFAS No. 114, "Accounting by Creditors for Impairment of a Loan", which requires that losses be accrued when it is probable that the Company will not collect all principal and interest payments according to the contractual terms of the loan. The loss, if any, can be determined by the difference between the loan balance and the value of collateral, the present value of expected future cash flows, or values observable in the secondary markets.

Three components comprise our allowance for credit losses: a specific allowance, a formula allowance, and a nonspecific unallocated allowance. Each component of the allowance is based upon estimates that can and do change when actual events occur.

The specific allowance is used to individually allocate an allowance for loans identified as impaired. Impairment testing includes consideration of the borrower's overall financial condition, resources and payment history, support available from guarantors, and the fair market value of collateral. These factors are combined to estimate the probability and severity of inherent losses. When an impairment is identified, a specific reserve is established based upon the Company's assessment of the estimated loss embedded in the individual loan. Large groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Company does not individually evaluate consumer and residential loans for impairment.

The formula allowance is used to estimate the loss on internally risk rated loans, exclusive of those identified as impaired. Loans identified in the risk rating evaluation as meeting the criteria for substandard, doubtful, and loss classification, (classified loans), are segregated from non-classified loans within the portfolio. Unimpaired internally classified loans are stratified by loan type; with each loan type

assigned an allowance factor based upon management's estimate of the associated risk. Allowance factors increase with the worsening of internal risk ratings.

The unallocated formula allowance is used to estimate the loss associated with non-classified loans. These unclassified loans are also stratified by loan type and risk rating, and allowance factors are assigned by management based upon a number of factors, including delinquencies, loss history, changes in lending policy and procedures, changes in business and economic conditions, changes in the nature and volume of the portfolio, management expertise, concentrations within the portfolio, quality of loan review systems, competition, and legal and regulatory requirements. The factors assigned differ by loan type and internal risk rating. The unallocated allowance captures losses inherent in the portfolio which have not yet been recognized. Allowance factors and the overall size of the allowance may change from period to period based upon management's assessment of the above described factors and the relative weights given to each factor.

Management has significant discretion in making the judgments inherent in the determination of the provision and allowance for credit losses, including, in connection with the valuation of collateral, a borrower's prospects of repayment, and in establishing allowance factors on the formula allowance and nonspecific or environmental allowance components of the allowance. The establishment of allowance factors is a continuing evaluation, based on management's ongoing assessment of the global factors discussed above and their impact on the portfolio. The allowance factors may change from period to period, resulting in an increase or decrease in the amount of the provision or allowance, based upon the same volume and classification of loans. Changes in allowance factors have a direct impact on the amount of the provision, and a related, after tax effect on net income. Errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance not being adequate to cover losses in the portfolio, and may result in additional provisions or charge-offs. Alternatively, errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance being in excess of amounts necessary to cover losses in the portfolio, and may result in lower provision in the future. For additional information regarding the allowance for credit losses, refer to the discussion under the caption "Allowance for Credit Losses" below.

Beginning in January 2006, the Company adopted the provisions of SFAS No. 123R, which requires the expense recognition for the fair value of stock-based compensation awards, such as stock options, restricted stock units, and performance based shares and the like. This standard allows management to establish modeling assumptions as to expected stock price volatility, option terms, forfeiture rates and dividend rates which directly impact estimated fair value. The accounting standard also allows for the use of alternative option pricing models which may impact fair value as determined. The Company's practice is to utilize reasonable and supportable assumptions which are reviewed with the appropriate Board Committee.

RESULTS OF OPERATIONS

Overview

The Company reported net income of $7.7 million for the year ended December 31, 2007, a 4% decrease from net income of $8.0 million for the year ended December 31, 2006, as compared to $7.5 million for the year ended December 31, 2005.

The decrease in net income for the twelve months ended December 31, 2007 can be attributed substantially to an increase in interest expense of 33% while interest income increased by 13% as compared to the same period in 2006. Net interest income showed an increase of 3% on growth in average earning assets of 13%. For the twelve months ended December 31, 2007, the Company has experienced a 44 basis point decline in its net interest margin from 4.81% in 2006 to 4.37% in 2007. This change was primarily due to reliance on more expensive sources of funds which has increased interest expense at a faster rate than increases in interest income.

Earnings per basic share were $0.80 for the year ended December 31, 2007, as compared to $0.85 for 2006 and $0.82 for 2005. Earnings per diluted share were $0.78 for the year ended December 31, 2007, as compared to $0.81 for 2006 and $0.77 for 2005.

For the three months ended December 31, 2007, the Company reported net income of $2.3 million as compared to $2.2 million for the same period in 2006. Earnings per basic share was $0.24 and $0.23 per diluted share for the three months ended December 31, 2007, as compared to $0.23 per basic share and $0.22 per diluted share for the same period in 2006.

The Company had a return on average assets of .96% and a return on average equity of 10.03% for the year of 2007, as compared to returns on average assets and average equity of 1.13% and 11.63%, respectively, for the year of 2006 and 1.24% and 12.25% respectively, for the year of 2005.

For the twelve months ended December 31, 2007, average interest bearing liabilities funding average earning assets increased to 77% as compared to 73% for the first twelve months of 2006. Additionally, while the average rate on earning assets for the twelve month period ended December 31, 2007, as compared to 2006 has increased by 2 basis points from 7.46% to 7.48%, the cost of interest bearing liabilities has increased by 44 basis points from 3.62% to 4.06%, resulting in a decline in the net interest spread of 42 basis points from 3.84% for the twelve months ended December 31, 2006 to 3.42% for the twelve months ended December 31, 2007. The 44 basis point decline in the net interest margin (from 4.81% for the twelve months ended December 31, 2006 to 4.37% for the twelve months ended December 31, 2007) has been slightly greater than the decline in the net interest spread as the Company's benefit from average noninterest bearing funding sources in 2007 declined modestly as compared to 2006. For the twelve months ended December 31, 2007, average noninterest sources funding earning assets were $178 million as compared to $181 million for the same period in 2006. The slight decline in noninterest funding sources has resulted in a slight decrease in the value of noninterest sources funding earning assets from 97 basis points in 2006 to 95 basis points in 2007.

Due to the need to meet loan funding objectives in excess of deposit growth, the Bank has relied to a larger extent on alternative funding sources, such as FHLB Advances and brokered deposits, the higher costs of which have contributed to a narrowing of the net interest margin. If significant reliance on alternative funding sources continues, the Company's earnings could be adversely impacted.

Loans, which generally have higher yields than securities and other earning assets, increased to 86% of average earning assets in 2007 from 85% of average earning assets for 2006. Investment securities accounted for 11% of average earning assets for both 2007 and 2006. Federal funds sold averaged 2% and 3% of average earning assets for 2007 and 2006, respectively. This decline was directly related to average loan growth over the past twelve month period exceeding the growth of average deposits and other funding sources.

For the quarter ended December 31, 2007, average interest bearing liabilities funding average earning assets increased to 73% as compared to 72% for the same period in 2006. Additionally, while the average rate on earning assets for the quarter ended December 31, 2007, as compared to the same period in 2006, has declined by 33 basis points from 7.56% to 7.23%, the cost of interest bearing liabilities has decreased by 15 basis points from 3.98% to 3.83%, resulting in a decline in the net interest spread of 17 basis points from 3.58% for the quarter ended December 31, 2006 to 3.41% for the quarter ended December 31, 2007. The net interest margin decreased 25 basis points from 4.55% for the quarter ended December 31, 2006 to 4.30% for the quarter ended December 31, 2007, a higher decline than the net interest spread as the benefit of average noninterest sources funding earning assets declined from 97 basis points for the quarter ended December 31, 2006 to 89 basis points for the quarter ended December 31, 2007.

For the quarter ended December 31, 2007 average loans increased 13% over the same period in 2006, maintaining a constant level of approximately 84% of average earning assets. Investment securities for the quarter ended December 31, 2007 amounted to 13% of average earning assets, an increase of 2% from an

average of 11% for the same period in 2006. Federal funds sold averaged 3% and 4% of average earning assets for the quarters ended December 31, 2007 and 2006, respectively.

The provision for credit losses was $1.6 million for the year ended December 31, 2007 as compared to $1.7 million in 2006. For the full year 2007, the Company recorded net charge-offs of $979 thousand, as compared to $357 thousand for the same period in 2006. The ratio of net-charge offs to average loans was .15% for 2007 and .06% for 2006. The increase in net charge-offs in 2007 is associated with one large commercial loan relationship identified in prior periods.

At December 31, 2007, the allowance for credit losses was $8.0 million or 1.12% of total loans, as compared to $7.4 million or 1.18% of total loans at December 31, 2006.

The provision for credit losses was $883 thousand for the three months ended December 31, 2007 as compared to $327 thousand for the same period in 2006, the increase being attributable to increases in environmental reserve factors associated with current economic conditions and not to any specific problem loan. For the fourth quarter of 2007, the Company recorded net charge-offs of $250 thousand, as compared to no net charge-offs for the fourth quarter of 2006. The charge-offs in the fourth quarter of 2007 related to one problem loan relationship identified several quarters ago for which specific reserves had been established.

Total noninterest income was $5.2 million for the year 2007 as compared to $3.8 million for 2006, an increase of 35%. These amounts include net investment gains of $6 thousand for the year of 2007 and $124 thousand in 2006. Excluding securities gains, total noninterest income increased by 39%. The increase was attributed primarily to higher amounts of gains on the sale of residential mortgage loans ($416 thousand versus $301 thousand); higher deposit account activity fees ($1.5 million versus $1.4 million) and income from subordinated financing of a real estate project ($1.2 million versus $0). Income from subordinated financing activities can fluctuate greatly between periods, as it is based on the progress of a limited number of development projects. Refer to "Loan Portfolio" section below for further discussion of subordinated financing activity.

For the three months ended December 31, 2007, total noninterest income increased 107% to $2.0 million as compared to $945 thousand for the same period in 2006. Excluding securities losses of $1 thousand during the fourth quarter of 2007 and gains of $39 thousand for the same period in 2006, total noninterest income increased by 116%. The increase was attributed substantially to income ($1.0 million) from the subordinated financing transaction noted above.

Total noninterest expense increased from $21.8 million for 2006 to $24.9 million for 2007, an increase of 14%. The primary reasons for this increase were increases in staff levels over the past twelve months and related personnel cost, occupancy cost (due in part to a new banking office and an expanded lending center facility), higher software licensing costs and expense associated with a reinstated FDIC deposit insurance assessment. The efficiency ratio which measures the level of noninterest expense to total revenue was 64.67% for 2007 as compared to 60.15% for 2006. The higher efficiency ratio relates in part to a lower net interest margin in 2007 as compared to 2006.

The efficiency ratio, improved to 59.87% for the fourth quarter of 2007, as compared to 61.57% for the fourth quarter of 2006, owing to substantial noninterest income in the final three months of 2007. For the three months ended December 31, 2007, total noninterest expense was $6.5 million, as compared to $5.7 million for the same period in 2006, an increase of 13%. This increase was due substantially to the same factors mentioned above which affected the increase for the full year 2007 over 2006.

Net Interest Income and Net Interest Margin

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. Earning assets are composed primarily of loans and investment securities. The cost of funds represents interest expense on deposits, customer repurchase agreements and other borrowings,

which comprise federal funds purchased and advances from the Federal Home Loan Bank of Atlanta ("FHLBA"). Noninterest bearing deposits and capital are other components representing funding sources. Changes in the volume and mix of assets and funding sources, along with the changes in yields earned and rates paid, determine changes in net interest income. Net interest income in 2007 was $33.3 million compared to $32.4 million in 2006 and $28.7 million in 2005. For the three months ended December 31, 2007, net interest income was $8.8 million as compared to $8.4 million for the same period in 2006, a 5% increase.

The following table labeled "Average Balances, Interest Yields and Rates and Net Interest Margin" presents the average balances and rates of the various categories of the Company's assets and liabilities. Included in the table is a measurement of interest rate spread and margin. Interest spread is the difference (expressed as a percentage) between the interest rate earned on earning assets less the interest rate paid on interest bearing liabilities. While net interest spread provides a quick comparison of earnings rates versus cost of funds, management believes that the net interest margin provides a better measurement of performance, since the net interest margin includes the effect of noninterest bearing sources in its calculation, which are significant factors in the Company's financial performance. The net interest margin is net interest income (annualized) expressed as a percentage of average earning assets.

Average Balances, Interest Yields and Rates and Net Interest Margin

	Year Ended December 31,								
	2007			2006			2005		
	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate
	(dollars in thousands)								
ASSETS:									
Interest earning assets:									
Interest bearing deposits with other banks and other short-term investments	$ 4,565	$ 293	6.42%	$ 3,379	$ 212	6.27%	$ 12,168	$ 417	3.43%
Loans(1)(2)(3)	659,204	51,931	7.88%	575,854	45,814	7.96%	479,311	33,478	6.98%
Investment securities available for sale(3)	85,177	4,177	4.90%	75,181	3,277	4.36%	71,438	2,424	3.39%
Federal funds sold	13,682	676	4.94%	20,271	1,015	5.01%	12,281	407	3.31%
Total interest earning assets	762,628	57,077	7.48%	674,685	50,318	7.46%	575,198	36,726	6.38%
Noninterest earning assets	45,217			44,090			40,073		
Less: allowance for credit losses	7,408			6,478			5,026		
Total noninterest earning assets	37,809			37,612			35,047		
TOTAL ASSETS	$ 800,437			$ 712,297			$ 610,245		
LIABILITIES AND STOCKHOLDERS' EQUITY									
Interest bearing liabilities:									
Interest bearing transaction	$ 51,465	$ 305	0.59%	$ 58,675	$ 204	0.35%	$ 61,230	$ 122	0.20%
Savings and money market	177,312	6,044	3.41%	152,162	5,174	3.40%	138,844	2,504	1.80%
Time deposits	270,480	13,461	4.98%	229,719	10,225	4.45%	171,827	4,837	2.82%
Total interest bearing deposits	499,257	19,810	3.97%	440,556	15,603	3.54%	371,901	7,463	2.01%
Customer repurchase agreements and federal funds purchased	44,992	1,887	4.19%	32,968	1,199	3.64%	29,341	350	1.19%
Other short-term borrowings	11,093	611	5.51%	12,596	639	5.07%	3,964	195	4.92%
Long term borrowings	29,033	1,421	4.89%	7,888	439	5.57%			0.00%
Total interest bearing liabilities	584,375	23,729	4.06%	494,008	17,880	3.62%	405,206	8,008	1.98%
Noninterest bearing liabilities:									
Noninterest bearing demand	135,075			145,065			140,515		
Other liabilities	4,227			4,251			2,961		
Total noninterest bearing liabilities	139,302			149,316			143,476		
Stockholders' equity	76,760			68,973			61,563		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 800,437			$ 712,297			$ 610,245		

	Year Ended December 31,		
Net interest income	$ 33,348	$ 32,438	$ 28,718
Net interest spread	3.42%	3.84%	4.40%
Net interest margin	4.37%	4.81%	4.99%

(1) Includes loans held for sale.

(2) Loans placed on nonaccrual status are included in average balances. Net loan fees and late charges included in interest income on loans totaled $1 million, $2 million and $1.2 million respectively for 2007, 2006, 2005 respectively.

(3) Interest and fees on loans and investment securities available for sale exclude tax equivalent adjustments.

The rate/volume table below presents the composition of the change in net interest income for the periods indicated, as allocated between the change in net interest income due to changes in the volume of average earning assets and interest bearing liabilities, and the changes in net interest income due to changes in interest rates. As the table shows, the increase in net interest income in 2007 as compared to

2006 is due to growth in the volume of earning assets offset substantially by a decrease in the net interest margin on earning assets. For 2006 over 2005, the increase in net interest income was a function of increased volume of earning assets and a decrease in the net interest margin.

Rate/Volume Analysis of Net Interest Income

	2007 compared with 2006			2006 compared with 2005		
	Change Due to Volume	Change Due to Rate	Total Increase (Decrease)	Change Due to Volume	Change Due to Rate	Total Increase (Decrease)
			(dollars in thousands)			
Interest earned on:						
Loans	$ 6,631	$ (514)	$ 6,117	$ 6,743	$ 5,593	$ 12,336
Investment securities	436	464	900	127	726	853
Interest bearing bank deposits	74	7	81	(301)	96	(205)
Federal funds sold	(330)	(9)	(339)	265	343	608
Total interest income	6,811	(52)	6,759	6,834	6,758	13,592
Interest paid on:						
Interest bearing transaction	(25)	126	101	(5)	87	82
Savings and money market	855	15	870	240	2,430	2,670
Time	1,814	1,422	3,236	1,630	3,758	5,388
Customer repurchase agreements	437	251	688	43	806	849
Other borrowings	1,101	(147)	954	864	19	883
Total interest expense	4,182	1,667	5,849	2,772	7,100	9,872
Net interest income	$ 2,629	$ (1,719)	$ 910	$ 4,062	$ (342)	$ 3,720

Provision for Credit Losses

The provision for credit losses represents the amount of expense charged to earnings to fund the allowance for credit losses. The amount of the allowance for credit losses is based on many factors which reflect management's assessment of the risk in the loan portfolio. Those factors include economic conditions and trends, the value and adequacy of collateral, volume and mix of the portfolio, performance of the portfolio, and internal loan processes of the Company and Bank.

During the year of 2007, a provision for credit losses was made in the amount of $1.6 million and the allowance for credit losses increased $664 thousand, including the impact of net charge-offs of $979 thousand during the period. During the year of 2006, a provision for credit losses was made in the amount of $1.7 million and the allowance for credit losses increased $1.4 million, including the impact of net charge-offs of $357 thousand during the period. The provision for credit losses of $1.6 million for the year 2007 was similar to the provision for credit losses of $1.7 million for the year 2006, as the overall portfolio mix of loans at year-end 2007 and 2006 was similar and the amount of loan growth was also similar. The provision for credit losses was $1.8 million for the year 2005.

For the three months ended December 31, 2007, a provision for credit losses was made in the amount of $883 thousand, as compared to $327 thousand for the same period in 2006. The higher provision for the fourth quarter of 2007, relates primarily to increases in environmental reserve factors associated with current economic conditions and not to any specific problem loan. For the fourth quarter of 2007, net charge-offs amounted to $250 thousand as compared to no net charge-offs for the same period in 2006. The charge-offs in the fourth quarter of 2007 related to one problem loan relationship identified several quarters ago for which specific reserves had been established.

The maintenance of a high quality loan portfolio, with an adequate allowance for credit losses will continue to be a primary objective of the Company.

Noninterest Income

Total noninterest income includes service charges on deposits, gain on sale of loans, income from subordinated financing, other income and gain (loss) on investment securities.

Total noninterest income for the year ended December 31, 2007 was $5.2 million, compared to $3.8 million for the year ended December 31, 2006, an increase of 35%. Excluding securities gains of $6 thousand for year ended 2007 and $124 thousand during the same period in 2006, noninterest income increased by 39%. The increase was attributed primarily to higher amounts of gains on the sale of residential mortgage loans ($416 thousand versus $301 thousand), higher deposit account activity fees ($1.5 million versus $1.4 million) and income from subordinated financing of real estate projects ($1.2 million versus $0). Income from subordinated financing activities can fluctuate greatly between periods, as it is based on the progress of a limited number of development projects. Refer to "Loan Portfolio" section below for further discussion of subordinated financing activity.

Noninterest income for the fourth quarter of 2007 increased 107% to $2.0 million from $945 thousand for the fourth quarter of 2006. Excluding securities losses of $1 thousand during the fourth quarter of 2007 and gains of $39 thousand for the same period in 2006, noninterest income increased by 116%. The increase was attributed substantially to income ($1.0 million) from a subordinated financing transaction related to a real estate development project.

For the year ended December 31, 2007 service charges on deposit accounts increased to $1.5 million from $1.4 million, an increase of 8%. The increase in service charges for the year was primarily related to new relationships and a full year impact of changes made in 2006 to earning credit computations. For the three months ended December 31, 2007 service charges on deposit accounts increased from $350 thousand to $429 thousand compared to the same period in 2006, an increase of 22%. This increase relates in part to the impact of lower interest rates in fourth quarter of 2007 as compared to 2006 on commercial deposit account fees.

Gain on sale of loans consists of SBA and residential mortgage loans. For the year ended December 31, 2007 gain on sale of loans decreased from $1.1 million to $1.0 million compared to the same period in 2006 or 7.0%. For the three months ended December 31, 2007 gain on loan sales decreased from $255 thousand to $220 thousand compared to the same period in 2006.

The Company is an active originator of SBA loans and its current practice is to sell the insured portion of those loans at a premium. Income from this source was $620 thousand for the year ended December 31, 2007 compared to $813 thousand for the year ended December 31, 2006. For the three months ended December 31, 2007, gains on the sale of SBA loans amounted to $140 thousand as compared to $124 thousand for the same period in 2006. Activity in SBA loan sales to secondary markets can vary widely from quarter to quarter. The Bank has been recognized as the leading community bank SBA lender in its marketplace and continued emphasis is anticipated. A portion of the lower SBA gains is due to lower fee margins established by the SBA.

The Company originates residential mortgage loans on a pre-sold basis, servicing released. Sales of these mortgage loans yielded gains of $416 thousand for the year of 2007 compared to $301 thousand in the same period in 2006. For the three months ended December 31, 2007, gains on the sale of residential mortgage loans were $80 thousand as compared to $131 thousand for the same three months of 2006. The Company continues its efforts to expand residential mortgage lending and associated sale of these assets on a servicing released basis. Loans sold are subject to repurchase in circumstances where documentation is not accurate or the underlying loan becomes delinquent within a specified period following sale and loan funding. The Bank considers these potential recourse provisions to be a minimal risk and to date has not been required to repurchase any loans. The Bank does not originate so called "sub-prime" loans and has no exposure to this market segment.

Other income totaled $2.7 million, for year ended 2007 up from $1.2 million for the same period in 2006, an increase of 117%. The primary reason for the increase is due to subordinated financing transactions. The Company provides subordinated financing for the acquisition, development and construction of real estate projects. These subordinated financings which are held by its wholly owned subsidiary ECV, generally entail a higher risk profile (including lower priority and higher loan to value ratios) than other loans made by the Bank. A portion of the amount which the Company expects to receive for such loans will be payments based on the success, sale or completion of the underlying project, and as such the income from these loans may be volatile from period to period, based on the status of such projects. For the year ended December 31, 2007 the Company recognized $1.2 million as income from the settlement of its remaining interest in a subordinated financing transaction compared to $0 for the same period in 2006. Income from subordinated financing activities is subject to wide variances, as it is based on the sales progress of a limited number of development projects. Refer to "Loan Portfolio" below for additional information on outstanding subordinate financing transactions. Other income also increased due to income from increases in the cash surrender value of bank owned life insurance and to increases in loan commitment fees on terminated transactions, and loan prepayment fees.

Other income totaled $1.3 million for the fourth quarter of 2007 up from $300 thousand for the fourth quarter of 2006, an increase of $1.0 million. The primary reason for the increase was due to the realization of income from the subordinated financing transaction discussed above.

Net investment gains amounted to $6 thousand and a loss of $1 thousand for the year and quarter ended December 31, 2007, respectively, as compared to net investment gains of $124 thousand and $39 thousand for the year and quarter ended December 31, 2006, respectively. Investment gains and losses are typically recognized as part of the Company's asset and liability management to meet loan demand or to better manage the Bank's interest rate risk position.

Noninterest Expense

Noninterest expense consists of salaries and employee benefits, premises and equipment expenses, marketing and advertising, outside data processing, legal, accounting and professional fees and other expenses.

Total noninterest expense was $24.9 million for the year ended December 31, 2007 compared to $21.8 million for the year ended December 31, 2006, an increase of 14%. For the three months ended December 31, 2007, total noninterest expense was $6.5 million versus $5.7 million for the same period in 2006, a 13% increase.

Salaries and employee benefits were $14.2 million for the year ended 2007, as compared to $12.2 million for 2006, a 16% increase. For the three months ended December 31, 2007, salaries and employee benefits amounted to $3.8 million versus $3.2 million for the same period in 2006, a 19% increase. This increase was due to staff additions and related personnel costs, merit increases and increased benefit costs, offset by a decline in incentive based compensation. At December 31, 2007, the Company's staff numbered 175, as compared to 171 and 145 at December 31, 2006 and 2005, respectively.

Premises and equipment expenses amounted to $4.8 million for the year ended December 31, 2007 versus $3.8 million for the same period in 2006. This increase of 26% was due primarily to a new banking office opened in mid May 2006 and an expanded lending center facility opened in the first quarter of 2007. Additionally, ongoing operating expense increases associated with the Company's facilities, all of which are leased and increased equipment costs contributed to the overall increase in expense. For the three months ended December 31, 2007, premises and equipment expenses amounted to $1.2 million versus $1.0 million for the same period in 2006. The reason for the increase in expense for the three month period is the same as mentioned above for the year ended.

Advertising costs decreased from $587 thousand in the year ended December 31, 2006 to $465 thousand in the same period in 2007, a decrease of 21%. For the three months ended December 31, 2007, advertising expenses amounted to $109 thousand versus $221 thousand for the same period in 2006, a decrease of 51%. These declines were due primarily to shifting certain design work in-house, and lower levels of product advertising, including time deposit rate advertising.

Outside data processing costs were $793 thousand for the year ended 2007, as compared to $881 thousand in 2006, a decrease of 10%. For the three months ended December 31, 2007, outside data processing costs amounted to $146 thousand versus $225 thousand for the same period in 2006, a decrease of 35%. This decline in the three months and year ended December 31, 2007 as compared to 2006 was due to savings achieved from the renegotiation of the Bank's primary data processing vendor agreement.

Legal, accounting and professional fees were $611 thousand for the year ended 2007, as compared to $801 thousand for 2006, a 24% decrease. This decrease was due in part to consulting engagement work in 2006 related to an IT audit, and costs in 2006 related to a companywide initiative on relationship management. For the three months ended December 31, 2007, legal, accounting and professional fees amounted to $153 thousand versus $167 thousand for the same period in 2006, an 8% decrease. The costs related to the pending acquisition of Fidelity & Trust, which will be capitalized as of the consummation of the transaction, are not included in these expense totals.

Other expenses, increased to $4.1 million in the year ended 2007 from $3.5 million for the year ended December 31, 2006, or an increase of 16%. For the three months ended December 31, 2007, other expenses amounted to $1.1 million versus $913 thousand for the same period in 2006, an increase of 20%. The major components of costs in this category include ATM expenses, broker fees, telephone, courier, printing, business development, office supplies, charitable contributions, director fees, dues and FDIC insurance premiums. For the year ended of 2007, as compared to 2006, the significant increases in this category were primarily broker fees, internet and license agreements and the reinstituted requirement that the Bank pay deposit insurance premiums. The same factors which contributed to an increase in other expenses for 2007 over 2006 mentioned above also contributed substantially to the increase in other expenses for the three months ended December 31, 2007, as compared to the same period in 2006.

Income Tax Expense

The Company recorded income tax expense of $4.3 million in 2007 compared to $4.7 million in 2006 and $4.4 million in 2005, resulting in an effective tax rate of 35.7%, 36.9% and 36.7%, respectively. The lower effective tax rate for 2007 relates in part to a higher level of state tax exempt income.

BALANCE SHEET ANALYSIS

Overview

At December 31, 2007, the Company's total assets were $846.4 million, loans were $716.7 million, deposits were $630.9 million, other borrowings, including customer repurchase agreements were $128.4 million and stockholders' equity was $81.2 million. As compared to December 31, 2006, assets grew in 2007 by $72.9 million (9%), loans by $90.9 million (15%), deposits by $2.4 million (.4%), borrowings by $60.3 million (89%) and stockholders' equity by $8.3 million (11%).

The Company declared a cash dividend of $0.24 per share for the year 2007 and $0.23 per share for the year 2006.

Investment Securities Available-for-Sale (AFS) and Short-Term Investments

The AFS portfolio is comprised largely of U.S. Government agency securities (59% of AFS) with an average duration of 1.6 years. The remaining AFS securities consists of seasoned mortgage backed securities that are 100% agency issued (34% of AFS) which have an average expected lives of 2.9 years

with contractual maturities of the underlying mortgages of up to thirty years, a municipal bond issue ($357 thousand) and equity investments (7% of AFS), a portion of which are required by regulatory mandates (Federal Reserve and Federal Home Loan Bank stocks amounting to 6% of AFS). The remaining portion of equity investments are either preferred or common stocks of three community based banking companies.

At December 31, 2007, the investment portfolio amounted to $87.1 million as compared to a balance of $91.1 million at December 31, 2006, a decrease of 4%. The investment portfolio is managed to achieve goals related to income, liquidity, interest rate risk management and providing collateral for customer repurchase agreements and other borrowing relationships.

The Company also has a portfolio of short-term investments utilized for asset liability management needs which consists from time-to-time of discount notes, money market investments, and other bank certificates of deposit This portfolio amounted to $4.5 million at December 31, 2007 as compared to $4.9 million at December 31, 2006.

Federal funds sold amounted to $244 thousand at December 31, 2007 as compared to $9.7 million at December 31, 2006. These funds represent excess daily liquidity which is invested on an unsecured basis with well capitalized banks, in amounts generally limited both in the aggregate and to any one bank.

The tables below and Note 3 to the Consolidated Financial Statements provide additional information regarding the Company's investment securities available for sale. The Company classifies all its investment securities as AFS. This classification requires that investment securities be recorded at their fair value with any difference between the fair value and amortized cost (the purchase price adjusted by any accretion or amortization) reported as a component of stockholders' equity (accumulated other comprehensive income), net of deferred income taxes. At December 31, 2007, the Company had a net unrealized gain in AFS securities of $966 thousand as compared to a net unrealized loss in AFS securities of $420 thousand at December 31, 2006. The deferred income tax liability/benefit of these unrealized gains and losses was $382 thousand and $167 thousand, respectively.

The following table provides information regarding the composition of the Company's investment securities portfolio at the dates indicated. Amounts are reported at estimated fair value.

	December 31,					
	2007		2006		2005	
	Balance	Percent of Total	Balance	Percent of Total	Balance	Percent of Total
	(dollars in thousands)					
U. S. Government agency securities	$ 51,295	58.9%	$ 58,584	64.3%	$ 46,998	69.1%
Mortgage backed securities	29,303	33.6%	27,333	30.0%	17,240	25.3%
Municipal bonds	351	0.4%				
Federal Reserve and Federal Home Loan Bank stock	4,870	5.6%	3,829	4.2%	2,230	3.3%
Other equity investments	1,298	1.5%	1,394	1.5%	1,582	2.3%
	$ 87,117	100%	$ 91,140	100%	$ 68,050	100%

The following table provides information, on an amortized cost basis, regarding the contractual maturity and weighted average yield of the investment portfolio at December 31, 2007. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Yields on tax exempt securities have not been calculated on a tax equivalent basis.

At December 31, 2007, there were no issuers, other than the U.S. Government and its agencies, whose securities owned by the Company had a book or fair value exceeding ten percent of the Company's stockholders' equity.

	One Year or Less		After One Year Through Five Years		After Five Years Through Ten Years		After Ten Years		Total	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
	(dollars in thousands)									
U. S. Government agency securities	$ 7,999	3.89%	$ 20,898	5.17%	$ 21,531	5.29%	$		$ 50,428	5.00%
Mortgage backed securities			5,288	3.96%	8,677	4.91%	15,253	5.56%	29,218	5.08%
Muncipal bonds							357	5.69%	357	5.69%
Federal Reserve and Federal Home Loan Bank stock							4,870	5.98%	4,870	5.98%
Other equity investments							1,278	6.26%	1,278	6.26%
	$ 7,999	3.89%	$ 26,186	4.93%	$ 30,208	5.18%	$ 21,758	3.90%	$ 86,151	5.10%

Loan Portfolio

In its lending activities, the Company seeks to develop sound relationships with clients whose businesses and individual banking needs will grow with the Bank. There has been a significant effort to grow the loan portfolio and to be responsive to the lending needs in the markets served, while maintaining sound asset quality.

Loan growth over the past year has been favorable, with loans outstanding reaching $716.7 million at December 31, 2007, an increase of $90.9 million or 15% as compared to $625.8 million at December 31, 2006, and were $549.2 million at December 31, 2005, an increase of $76.6 million or 14% in 2006 over 2005. For the fourth quarter of 2007, the loan portfolio increased $37.2 million (5.5%) over $679.5 million at September 30, 2007.

The Bank is primarily commercial oriented and as can be seen in the chart below, has a large proportion of its loan portfolio related to real estate (70%) consisting of real estate-commercial, real estate-residential mortgage and construction-commercial and residential loans. Real estate also serves as collateral for loans made for other purposes, resulting in 80% of our loans being secured by real estate.

The following table shows the trends in the composition of the loan portfolio over the past five years.

	December 31,									
	2007		2006		2005		2004		2003	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)									
Commercial	$ 149,332	21%	$ 132,981	21%	$ 118,928	22%	$ 101,911	25%	$ 93,112	29%
Real estate commercial(1)	392,757	55%	349,044	56%	284,667	52%	189,708	47%	142,819	45%
Real estate residential mortgage	2,160		1,523		1,130		9,230	2%	6,964	2%
Construction commercial & residential(1)	110,115	15%	86,524	14%	90,035	16%	62,745	14%	35,644	11%
Home equity	57,515	8%	50,572	8%	50,776	9%	49,632	11%	34,092	11%
Other consumer	4,798	1%	5,129	1%	3,676	1%	2,283	1%	4,902	2%
Total loans	716,677	100%	625,773	100%	549,212	100%	415,509	100%	317,533	100%
Less: Allowance for Credit Losses	(8,037)		(7,373)		(5,985)		(4,240)		(3,680)	
Net loans	$ 708,640		$ 618,400		$ 543,227		$ 411,269		$ 313,853	

(1) Includes loans for land acquisition and owner occupied properties

As discussed under the caption "Business" and "Risk Factors", the Company has directly made higher risk loans that entail higher risks than loans made following normal underwriting practices ("higher risk loan transactions"). These higher risk loan transactions are currently made through the Company's subsidiary, ECV, which was formed in July 2006. This activity is limited as to individual transaction amount and total exposure amounts based on capital levels and is carefully monitored. Transactions are structured to provide ECV with returns commensurate to the risk through the requirement of additional interest following payoff of all loans:

For the year ended December 31, 2007, the Company recorded noninterest income from one subordinated financing transaction amounting to $1.2 million. At December 31, 2007, the Company has no further interests or risks from that project.

At December 31, 2007, ECV has a $1.9 million higher risk loan outstanding relating to a real estate project which is currently in a construction phase. The loan is expected to be outstanding throughout 2008, with sales completed in 2009.

Although the Company carefully underwrites each higher risk loan transaction and expects these transactions to provide additional revenues, there can be no assurance that any higher risk loan transaction, or the related loans made by the Bank, will prove profitable for the Company and Bank, that the Company and Bank will be able to receive any additional interest payments in respect of these loans, that any additional interest payments will be significant, or that the Company and Bank will not incur losses in respect of these transactions.

Loan Maturity

The following table sets forth the term to contractual maturity of the loan portfolio as of December 31, 2007.

	Due In				
	Total	One Year or Less	Over One to Five Years	Over Five to Ten Years	Over Ten Years
			(dollars in thousands)		
Commercial	$ 149,332	$ 66,482	$ 45,857	$ 32,796	$ 4,197
Real estate commercial	392,757	46,460	113,694	199,991	32,612
Real estate residential mortgage	2,160	688	1,321		151
Construction commercial and residential	110,115	54,447	24,549	23,397	7,722
Home equity	57,515	2	232	380	56,901
Other consumer	4,798	907	2,721	164	1,006
Total loans	$ 716,677	$ 168,986	$ 188,374	$ 256,728	$ 102,589
Loans with:					
Predetermined fixed interest rate	$ 249,717	$ 39,286	$ 119,822	$ 71,649	$ 18,960
Floating interest rate	466,960	129,700	68,552	185,079	83,629
Total loans	$ 716,677	$ 168,986	$ 188,374	$ 256,728	$ 102,589

Loans are shown in the period based on final contractual maturity. Demand loans, having no contractual maturity and overdrafts, are reported as due in one year or less.

As noted above, a significant portion of the loan portfolio consists of commercial, construction and commercial real estate loans, primarily made in the Washington, D.C. metropolitan area and secured by real estate or other collateral in that market. Although these loans are made to a diversified pool of unrelated borrowers across numerous businesses, adverse developments in the Washington D.C. metropolitan real estate market could have an adverse impact on this portfolio of loans and the Company's income and financial position. While our basic trading area is the Washington, D.C. metropolitan area, the Bank has made loans outside that market area where the nature and quality of such loans was consistent with the Bank's lending policies.

The federal banking regulators have issued guidance for those institutions which are deemed to have concentrations in commercial real estate lending. Pursuant to the supervisory criteria contained in the guidance for identifying institutions with a potential commercial real estate concentration risk, institutions which have (1) total reported loans for construction, land development, and other land which represent in total 100% or more of an institutions total risk-based capital; or (2) total commercial real estate loans representing 300% or more of the institutions total risk-based capital and the institution's commercial real estate loan portfolio has increased 50% or more during the prior 36 months are identified as having potential commercial real estate concentration risk. Institutions which are deemed to have concentrations in commercial real estate lending are expected to employ heightened levels of risk management with respect to their commercial real estate portfolios, and may be required to hold higher levels of capital. The Company, like many community banks, has a concentration in commercial real estate loans. Management has extensive experience in commercial real estate lending, and has implemented and continues to maintain heightened portfolio monitoring and reporting, and strong underwriting criteria with respect to its commercial real estate portfolio. The Company is well capitalized. Nevertheless, it is possible that the Company could be required to maintain higher levels of capital as a result of our commercial real estate concentration, which could require us to obtain additional capital, and may adversely affect shareholder returns

At December 31, 2007, the Company had no other concentrations of loans in any one industry exceeding 10% of its total loan portfolio. An industry for this purpose is defined as a group of businesses that are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

Allowance for Credit Losses

Management has developed a comprehensive review process to monitor the adequacy of the allowance for credit losses. The review process and guidelines were developed utilizing guidance from federal banking regulatory agencies. The results of this review process, in combination with conclusions of the Bank's outside loan review consultant, support management's view as to the adequacy of the allowance as of the balance sheet date. During 2007, a provision for credit losses was made in the amount of $1.6 million before net charge-offs of $979 thousand. A full discussion of the accounting for allowance for credit losses is contained in Note 1 to the Consolidated Financial Statements; activity in the allowance for credit losses is contained in Note 4 to the Consolidated Financial Statements. Also, please refer to the discussion under the caption, "Critical Accounting Policies" within Management's Discussion and Analysis of Financial Condition and Results of Operation for further discussion of the methodology which management employs to maintain an adequate allowance for credit losses, and the discussion under the caption "Provision for Credit Losses".

The allowance for credit losses represented 1.12% of total loans at December 31, 2007 as compared to 1.18% at December 31, 2006. This decrease in the ratio of the allowance for credit losses was due to the charge-off of a large commercial loan relationship during 2007 that had been partially reserved at December 31, 2006.

At December 31, 2007, the Company had $5.3 million of loans classified as nonperforming, and $1.9 million of potential problem loans, as compared to $2.0 million of nonperforming assets and $4.3 million of potential problem loans at December 31, 2006. Please refer to Note 1 of the notes to the Consolidated Financial Statements under the caption "Loans" for a discussion of the Company's policy regarding impairment of loans. Please refer to "Nonperforming Assets" below for a discussion of problem and potential problem assets.

As the loan portfolio and allowance for credit losses review process continues to evolve, there may be changes to elements of the allowance and this may have an effect on the overall level of the allowance maintained. To date, the Bank has enjoyed a high quality loan portfolio with relatively low levels of net charge-offs and low delinquency rates. The maintenance of a high quality portfolio will continue to be a high priority for both management and the Board of Directors.

Management, being aware of the significant loan growth experienced by the Company and the problems which could develop in an unmonitored environment, is intent on maintaining a strong credit review system and risk rating process. The Company established a formal Credit Department in 2003 to provide independent analysis of credit requests and to manage problem credits. The Credit Department has developed and implemented additional analytical procedures for evaluating credit requests, has further refined the Company's risk rating system, and has adopted enhanced monitoring of the loan portfolio and the allowance for credit losses. The loan portfolio analysis process is ongoing and proactive in order to maintain a portfolio of quality credits and to quickly identify any weaknesses before they become more severe.

The following table sets forth activity in the allowance for credit losses for the past five years.

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(dollars in thousands)				
Balance at beginning of year	$ 7,373	$ 5,985	$ 4,240	$ 3,680	$ 2,766
Charge-offs:					
Commercial	(1,005)	(369)	(122)	(257)	(319)
Home equity		(15)			
Other consumer	(26)	(5)	(17)	(35)	(14)
Total charge-offs	(1,031)	(389)	(139)	(292)	(333)
Recoveries:					
Commercial	37	27	41	175	68
Other consumer	15	5		2	4
Total recoveries	52	32	41	177	72
Net charge-offs	(979)	(357)	(98)	(115)	(261)
Additions charged to operations	1,643	1,745	1,843	675	1,175
Balance at end of year	$ 8,037	$ 7,373	$ 5,985	$ 4,240	$ 3,680
Ratio of net charge-offs during the year to average loans outstanding during the year	0.15%	0.06%	0.02%	0.03%	0.10%

The following table presents the allocation of the allowance by loan category and the percent of loans each category bears to total loans. The allocation of the allowance for the Commercial category includes a specific reserve of $220 thousand against impaired loans relating to two SBA loans which were identified as impaired during the fourth quarter of 2007. The allocation of the allowance to each category is not necessarily indicative of future losses or charge-offs and does not restrict the usage of the allowance for any specific loan or category.

	Year Ended December 31,									
	2007		2006		2005		2004		2003	
	Amount	% of Loans	Amount	% of Loans	Amount	% of Loans	Amount	% of Loans	Amount	% of Loans
	(dollars in thousands)									
Commercial	$ 3,300	21%	$ 3,379	21%	$ 2,594	22%	$ 1,963	25%	$ 1,689	29%
Real estate commercial	3,053	55%	2,800	56%	2,395	52%	1,426	47%	850	45%
Real estate residential mortgage	21		40		48		105	2%	38	2%
Construction commercial and residential	1,314	15%	854	14%	602	16%	431	14%	613	11%
Home equity	233	8%	176	8%	176	9%	223	11%	171	11%
Other consumer	116	1%	124	1%	84	1%	58	1%	72	2%
Unallocated					86		34		247	
Total Loans	$ 8,037	100%	$ 7,373	100%	$ 5,985	100%	$ 4,240	100%	$ 3,680	100%

Nonperforming Assets

The Company's nonperforming assets, which are comprised of loans delinquent 90 days or more, nonaccrual loans, restructured loans and other real estate owned, totaled $5.3 million at December 31, 2007 compared to $2.0 million at December 31, 2006. The percentage of nonperforming assets to total assets was 0.63% at December 31, 2007 compared to 0.26% at December 31, 2006.

The following table shows the amounts of nonperforming assets at December 31 for the past five years:

	2007	2006	2005	2004	2003
	(dollars in thousands)				
Nonaccrual Loans:					
Commercial	$ 1,174	$ 1,976	$ 362	$ 156	$ 554
Other consumer			129		100
Home equity	123				
Construction comercial and residential	3,386				
Real estate commercial	641				
Accrual loans-past due 90 days:					
Commercial		37			
Other consumer					
Real estate commercial					
Restructured loans					
Real estate owned					
Total non-performing assets	$ 5,324	$ 2,013	$ 491	$ 156	$ 654

(1) Gross interest income that would have been recorded in 2007 if nonaccrual loans and leases shown above had been current and in accordance with their original terms was $128 thousand, while interest actually recorded on such loans was $75 thousand. Please see Note 1 of the Notes to Consolidated financial Statements for a description of the Company's policy for placing loans on nonaccrual status.

Nonaccrual loans at December 31, 2007, include two related loans totaling $4.0 million, which were placed on nonaccrual in the third quarter of 2007 and which management believes are well secured. Interest on these two related loans is being recorded on a cash basis. Nonaccrual loans at December 31, 2006 consisted primarily of one large commercial relationship amounting to $1.9 million which had a specific reserve of $678 thousand at December 31, 2006 and which has been charged-off as of December 31, 2007 to an amount expected to be realized.

Significant variation in the amount of nonperforming loans may occur from period to period because the amount of nonperforming loans depends largely on the condition of a small number of individual credits and borrowers relative to the total loan portfolio. The Company had no Other Real Estate Owned (OREO) or restructured loans at either December 31, 2007 or 2006. The balance of impaired loans consisting of all nonaccrual loans only, was $5.3 million at December 31, 2007, with $220 thousand of specific reserves compared to $2.0 million of impaired loans at December 31, 2006 with $678 thousand of specific reserves.

At December 31, 2007, there were $1.9 million of performing loans considered potential problem loans, defined as loans which are not included in the 90 day past due, nonaccrual or restructured categories, but for which known information about possible credit problems causes management to be uncertain as to the ability of the borrowers to comply with the present loan repayment terms which may in the future result in disclosure in the past due, nonaccrual or restructured loan categories.

Other Earning Assets

Residential mortgage loans held for sale amounted to $2.2 million at both December 31, 2007 and December 31, 2006. Origination and sales of these loans during 2007 was emphasized by the Company in order to enhance noninterest income, which emphasis is expected to continue in 2008. The Bank did not engage in the origination of subprime or "exotic" mortgage loans. See "Business" at page 61 for a description of the Bank's mortgage lending and brokerage activities.

Bank owned life insurance is utilized by the Company in accordance with tax regulations as part of the Company's financing of its benefit programs. At December 31, 2007 this asset amounted to $12.0 million as compared to $11.5 million at December 31, 2006, which reflected an increase in cash surrender values, and not new investments.

Intangible Assets

In 2005, the Company began recognizing a servicing asset for the computed value of servicing fees on the sale of the guaranteed portion of SBA loans, which is in excess of a normal servicing fee. Assumptions related to loan term and amortization are made to arrive at the initial recorded value, which is included in other assets.

For 2007, excess servicing fees of $122 thousand were recorded, and $141 thousand was amortized as a reduction of actual service fees collected, which is a component of other income. At December 31, 2007, the balance of excess servicing fees was $236 thousand. For 2006, excess servicing fees of $167 thousand were recorded, of which $80 thousand was amortized as a reduction of actual service fees collected, which is a component of other income. At December 31, 2006, the balance of excess servicing fees was $255 thousand.

This asset is subject to impairment testing annually.

Deposits and Other Borrowings

The principal sources of funds for the Bank are core deposits, consisting of noninterest bearing demand, interest bearing transaction, money market and savings accounts and time deposits from the local market areas surrounding the Bank's offices. The deposit base includes transaction accounts, time and savings accounts and accounts which customers use for cash management and which provide the Bank with a source of fee income and cross-marketing opportunities as well as an attractive source of lower cost funds. Time and savings accounts, including money market deposit accounts, also provide a relatively stable and low-cost source of funding.

For the year ended December 31, 2007, deposits grew just $2.4 million, from $628.5 million to $630.9 million or 0.4%. Approximately 41% of the Bank's deposits at December 31, 2007 are made up of time deposits, which are generally the most expensive form of deposit because of their fixed rate and term, as compared to 42% at December 31, 2006. These deposits increased modestly, by $4.9 million, at December 31, 2007 as compared to December 31, 2006 as the Bank utilized alternative funding sources due to lower cost. Average time deposits amounted to $270.5 million in 2007, compared to $229.7 million in 2006, an increase of $40.8 million or 17%. Time deposits in denominations of $100 thousand or more increased $15.1 million, or 9.5%, to $173.6 million, or 28% of total deposits at December 31, 2007, as compared to 25% at December 31, 2006. These deposits can be more volatile and more expensive than time deposits of less than $100 thousand. However, because the Bank focuses on relationship banking, and its marketplace demographics are favorable, its historical experience has been that large time deposits have not been more volatile or significantly more expensive than smaller denomination certificates. From time to time, when appropriate in order to fund strong loan demand, the Bank accepts time deposits, generally in denominations of less than $100 thousand from bank and credit union subscribers to a wholesale deposit rate line and also acquires brokered deposits. Wholesale deposits amounted to approximately $10.2 million or 2% of total deposits at December 31, 2007, as compared to approximately $18.3 million or 3% of total deposits at December 31, 2006. On an average basis, wholesale deposits amounted to $25.9 million for 2007 (4% of average deposits) as compared to $9.1 million in 2006 (2% of average deposits).

The following table sets forth the maturities of time deposits with balances of $100,000 or more, which represent 28% of total time deposits as of December 31, 2007, compared to 25% at December 31, 2006.

See Note 6 to the Consolidated Financial Statements and the Average Balances Table above for additional information regarding the maturities of time deposits and average rates paid on interest- bearing deposits.

	December 31,		
	2007	**2006**	**2005**
	(dollars in thousands)		
Three months or less	$ 52,569	$ 39,730	$ 25,943
More than three months through six months	56,540	59,731	33,109
More than six months through twelve months	61,117	54,234	53,217
Over twelve months	3,359	4,800	10,302
Total	$ 173,585	$ 158,495	$ 122,571

At December 31, 2007, the Company had approximately $142.5 million in noninterest bearing demand deposits, representing 23% of total deposits. This compared to approximately $139.9 million of these deposits at December 31, 2006 or 22% of total deposits. These deposits are primarily business checking accounts on which the payment of interest is prohibited by regulations of the Federal Reserve. Proposed legislation has been introduced in each of the last several sessions of Congress which would permit banks to pay interest on checking and demand deposit accounts established by businesses. If legislation effectively permitting the payment of interest on business demand deposits is enacted, of which there can be no assurance, it is likely that we may be required to pay interest on some portion of our noninterest bearing deposits in order to compete with other banks. Payment of interest on these deposits could have a significant negative impact on our net interest income and net interest margin, net income, and the return on assets and equity.

As an enhancement to the basic noninterest bearing demand deposit account, the Company offers a sweep account, or "customer repurchase agreement", allowing qualifying businesses to earn interest on short-term excess funds which are not suited for either a certificate of deposit or a money market account. The balances in these accounts were $52.9 million at December 31, 2007 compared to $38.1 million at December 31, 2006. Customer repurchase agreements are not deposits and are not insured but are collateralized by U.S. government agency securities. These accounts are particularly suitable to businesses with significant fluctuation in the levels of cash flows. Attorney and title company escrow accounts are an example of accounts which can benefit from this product, as are customers who may require collateral for deposits in excess of $100 thousand but do not qualify for other pledging arrangements. This program requires the Company to maintain a sufficient investment securities level to accommodate the fluctuations in balances which may occur in these accounts.

At December 31, 2006 the Company had $23.5 million outstanding balances under its federal funds lines of credit provided by correspondent banks, as compared to no outstandings at December 31, 2006. This increase was due to funding loan growth late in 2007. The Bank had $52 million borrowings outstanding under its credit facility from the Federal Home Loan Bank of Atlanta, as compared to $30 million outstandings at December 31, 2006. Outstanding advances are secured by collateral consisting of a blanket lien on qualifying loans in the Bank's commercial mortgage loan portfolio. Please refer to Note 7 to the Consolidated Financial Statements for additional information regarding the Company's short-term borrowings.

COMPARISON OF 2006 VERSUS 2005

The Company reported net income of $8.0 million for the year ended December 31, 2006, a 6% increase over net income of $7.5 million for the year ended December 31, 2005.

Earnings per basic share were $0.85 for the year ended December 31, 2006, as compared to $0.82 for the year 2005 and $0.56 for the year 2004. Earnings per diluted share was $0.81 for the year ended December 31, 2006, as compared to $0.77 for the year 2005.

The Company had a return on average assets of 1.13% and a return on average equity of 11.63% for the year of 2006, as compared to returns on average assets and average equity of 1.24% and 12.25%, respectively, for the year of 2005.

The increase in net income for the twelve months ended December 31, 2006 as compared to the same period in 2005 can be attributed substantially to an increase of 13% in net interest income, resulting from an increase of 17% in average earning assets and a decline in the net interest margin of 18 basis points. For the twelve months ended December 31, 2006, the Company experienced a decline in its net interest margin as the funding mix shifted to more interest bearing deposits and borrowed funds and as the costs of those funds increased. For the twelve months ended December 31, 2006, average interest bearing liabilities funding average earning assets increased to 73% as compared to 70% for the twelve months of 2005. Additionally, while the average rate on earning assets for the twelve month period ended December 31, 2006 as compared to 2005 increased by 108 basis points from 6.38% to 7.46%, the cost of interest bearing liabilities increased by 164 basis points from 1.98% to 3.62%, resulting in a decline in the net interest spread from 4.40% for the twelve months ended December 31, 2005 to 3.84% for the twelve months ended December 31, 2006. The 18 basis point decline in the net interest margin during the same period was less than the decline in the net interest spread as the Company benefited from a significant amount of average noninterest bearing funding sources. For the twelve months ended December 31, 2006, average noninterest sources funding earning assets was $183 million as compared to $170 million for the same period in 2005. The combination of higher levels of market interest rates and the increase in noninterest funding sources resulted in an increase in the value of noninterest sources funding earning assets from 59 basis points for the twelve months in 2005 to 98 basis points for the twelve months ended December 31, 2006.

Net interest income in 2006 was $32.4 million compared to $28.7 million in 2005 and $19.9 million in 2004. The increase in 2006 as compared to 2005 is due to growth in the volume of earning assets offset in part by a decline in the net interest margin on earning assets.

Average loans increased to 85% of average earning assets in the year 2006 from 83% of average earning assets for the year of 2005. Average investment securities for the year of 2006 accounted for 11% of average earning assets as compared to 12% for the year of 2006.

The provision for credit losses was $1.7 million for the year of 2006 as compared to $1.8 million for the same period in 2005. This decline was largely attributable to a lesser amount of loan growth in the loan portfolio in 2006 as compared to 2005, offset by specific reserves being provided on a significant problem commercial loan relationship identified in August 2006. The Company had $357 thousand of net charge-offs in the year of 2006, as compared to net charge-offs of $98 thousand for the year of 2005.

Total noninterest income was $3.8 million for the year 2006 as compared to $4.0 million for 2005, a 4% decline. These amounts include net investment gains of $124 thousand for the year of 2006 and $279 thousand in 2005. Excluding gains on the sale of investment securities, noninterest income was $3.7 million in both 2006 and 2005. This result was due primarily to increased revenue on deposit service charges being effectively offset by lesser amounts of gains on the sale of SBA loans and SBA service fees.

Total noninterest expenses increased from $19.0 million for the year of 2005 to $21.8 million for the year of 2006, an increase of 15%. The increase was attributable primarily to increases in personnel and related benefit cost increases, the cost of share based compensation under new accounting rules effective January 1, 2006 ($345 thousand pre-tax), increased premises and equipment expenses, due in part to a new banking office and the relocation of another banking office, and to higher marketing and advertising costs, outside data processing costs and professional fees associated with a larger organization. For the year 2006, the efficiency ratio, which measures the ratio of noninterest expenses to the sum of net interest income and noninterest income (total revenue), was 60.15% as compared to 57.95% for the year of 2005.

The Company recorded income tax expense of $4.7 million in 2006 compared to $4.4 million in 2005, resulting in an effective tax rate of 36.9% for 2006 and 36.7% for 2005.

At December 31, 2006, the Company's total assets were $773.5 million, loans were $625.8 million, deposits were $628.5 million and stockholders' equity was $72.9 million. As compared to December 31, 2005, assets grew in 2006 by $101.2 million (15%), loans by $76.6 million (14%), deposits by $59.6 million (10%) and stockholders' equity by $8.0 million (12%).

The Company declared a cash dividend of $0.23 per share for the year 2006 and $0.22 per share for the year 2005.

At December 31, 2006, the investment portfolio amounted to $91.1 million as compared to a balance of $68.1 million at December 31, 2005, an increase of 34%. The investment portfolio is managed to achieve goals related to income, liquidity, interest rate risk management and providing collateral for customer repurchase agreements and other borrowing relationships.

The Company also has a portfolio of short-term investments utilized for asset liability management needs which consists of discount notes, money market investments, other bank certificates of deposit and similar instruments. This portfolio amounted to $4.9 million at December 31, 2006 as compared to $11.2 million at December 31, 2005.

Loans outstanding reached $625.8 million at December 31, 2006, an increase of $76.6 million or 14% as compared to $549.2 million at December 31, 2005.

The allowance for loan losses represented 1.18% of total loans at December 31, 2006 as compared to 1.09% at December 31, 2005. This increase in the ratio of the allowance was due to two factors as follows: additional reserves provided in the third quarter of 2006 for a large problem commercial loan relationship identified in August 2006 and to a slight increase in the environmental factors of the non-specific reserve component related to various factors including potential impacts of higher interest rates on debt service capacity and on real estate values.

At December 31, 2006, the Company had $2.0 million of loans classified as nonperforming, and $4.3 million of potential problem loans, as compared to $491 thousand of nonperforming assets and $2.9 million of potential problem loans at December 31, 2005. The percentage of nonperforming assets to total assets was 0.26% at December 31, 2006 compared to 0.07% at December 31, 2005. Non-accrual loans at December 31, 2006 consisted primarily of one large commercial relationship amounting to $1.9 million which has been assigned a specific reserve of $678. The Company had no Other Real Estate Owned (OREO) or restructured loans at either December 31, 2006 or 2005. The balance of impaired loans was $2.0 million at December 31, 2006, compared to $491 thousand of impaired loans at December 31, 2005 with specific reserves of $200 thousand.

Residential mortgage loans held for sale decreased to $2.2 million at December 31, 2006 from $2.9 million at December 31, 2005.

Bank owned life insurance is utilized by the Company in accordance with tax regulations as part of the Company's financing of its benefit programs. At December 31, 2006 this asset amounted to $11.5 million as compared to $11.1 million at December 31, 2005, which reflected an increase in cash surrender values, and not new investments.

For the year ending December 31, 2006 deposits grew $59.6 million, from $568.9 million to $628.5 million or 10%. Approximately 42% of the Bank's deposits at December 31, 2006 are made up of time deposits, which are generally the most expensive form of deposit because of their fixed rate and term as compared to 33% at December 31, 2005. These deposits had significant increases in the year ended December 31, 2006 as the Bank utilized these funding sources due to lesser growth in core non-interest and money market deposit accounts. From time to time, when appropriate in order to fund strong loan demand, the Bank accepts time deposits, generally in denominations of less than $100 thousand from bank and credit union subscribers to a wholesale deposit rate line and may also accept brokered deposits.

Wholesale deposits amounted to approximately $18 million or 3% of total deposits at December 31, 2006, as compared to approximately $11 million or 2% of total deposits at December 31, 2005.

As an enhancement to the basic noninterest bearing demand deposit account, the Company offers a sweep account, or "customer repurchase agreement", allowing qualifying businesses to earn interest on short-term excess funds which are not suited for either a certificate of deposit or a money market account. The balances in these accounts were $38 million at December 31, 2006 compared to $32 million at December 31, 2005. Customer repurchase agreements are not deposits and are not insured but are collateralized by U.S. government agency securities.

At December 31, 2006 and December 31, 2005, the Company had no outstanding balances under its lines of credit provided by correspondent banks. The Bank had $30 million borrowings outstanding under its credit facility from the Federal Home Loan Bank of Atlanta, as compared to no outstandings at December 31, 2005.

CONTRACTUAL OBLIGATIONS

The Company has various financial obligations, including contractual obligations and commitments that may require future cash payments. Except for its loan commitments, as shown in Note 13 to Notes to Consolidated Financial Statements Financial Instruments with Off-Balance Sheet Risk, the following table shows details on these fixed and determinable obligations in the time period indicated.

	Within One Year	One to Three Years	Three to Five Years	Over Five Years	Total
			(dollars in thousands)		
Deposits without a stated maturity(1)	$ 373,648	$	$	$	$ 373,648
Time deposits(1)	250,896	4,621	1,771		257,288
Borrowed funds(2)	98,408	20,000	10,000		128,408
Operating lease obligations(3)	2,350	4,851	3,999	4,979	16,179
Outside data processing(4)	904	1,596	1,376	287	4,163
Total	$ 726,206	$ 31,068	$ 17,146	$ 5,266	$ 779,686

(1) Excludes accrued interest payable at December 31, 2007

(2) Borrowed funds include customer repurchase agreements, federal funds purchased and other short-term and long-term borrowings.

(3) In September 2006, the Bank signed a lease for approximately 7,400 square feet in a "to be constructed" office building adjacent to its headquarters building in Bethesda. The minimum lease commitment is approximately $3.0 million and is subject to various approvals and other conditions. The table amounts include this obligation. In February 2008, the Company leased additional expansion space in its Operations Center amounting to approximately 2,000 square feet. This obligation is excluded in both the table above and the lease obligations shown in Note 5 of Notes to the Consolidated Financial Statements.

(4) The Bank has outstanding significant obligations under its current core data processing contract that expires in May 2013 and one other significant vendor arrangement that relates to data communications and data software that expires in December 2009.

OFF-BALANCE SHEET ARRANGEMENTS

The Company is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit and standby letters of credit. They involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheets.

The contract or notional 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 nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit 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. See Note 13 of the Notes to Consolidated Financial Statements for a summary list of loan commitments at December 31, 2007 and 2006.

Loan commitments represent agreements to lend to a customer as long as there is no violation of any condition established in the contract and which have been accepted in writing by the borrower. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments may 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 is based on management's credit evaluation of the borrower. Collateral obtained varies, and may include certificates of deposit, accounts receivable, inventory, property and equipment, residential and commercial real estate.

Standby letters of credit are conditional commitments issued by the Company which 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. Collateral held varies as specified above and is required in instances which the Company deems necessary. At December 31, 2007, approximately 91% of the dollar amount of standby letters of credit was collateralized.

With the exception of these off-balance sheet arrangements, the Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, capital expenditures or capital resources, that is material to investors.

LIQUIDITY MANAGEMENT

Liquidity is a measure of the Company and Bank's ability to meet loan demand and to satisfy depositor withdrawal requirements in an orderly manner. The Bank's primary sources of liquidity consist of cash and cash balances due from correspondent banks, loan repayments, federal funds sold and other short-term investments, maturities and sales of investment securities and income from operations. The Bank's investment portfolio of debt securities is held in an available-for-sale status, which allows it flexibility, subject to holdings held as collateral for customer repurchase agreements; to generate cash from sales as needed to meet ongoing loan demand. These sources of liquidity are considered primary and are supplemented by the ability of the Company and Bank to borrow funds, which are termed secondary sources. The Company maintains secondary sources of liquidity, which includes a $15 million line of credit with a correspondent bank, secured by the stock of the Bank, against which there were no amounts outstanding at December 31, 2007. Additionally, the Bank can purchase up to $76.5 million in federal funds on an unsecured basis and $5.5 million on a secured basis from its correspondents, against which there were $23.5 million outstanding at December 31, 2007. At December 31, 2007, the Bank was also eligible to make advances from the FHLB up to $97.1 million based on collateral at the FHLB, of which it had $52.0 million of advances outstanding at December 31, 2007. Also, the Bank may enter into repurchase agreements as well as obtaining additional borrowing capabilities from the FHLB provided adequate collateral exists to secure these lending relationships.

The loss of deposits, through disintermediation, is one of the greater risks to liquidity. Disintermediation occurs most commonly when rates rise and depositors withdraw deposits seeking higher rates in alternative savings and investment sources than the Bank may offer. The Bank was founded under a philosophy of relationship banking and, therefore, believes that it has less of an exposure to disintermediation and resultant liquidity concerns than do many banks. There is, however, a risk that some deposits would be lost if rates were to increase and the Bank elected not to remain competitive with its

deposit rates. Under those conditions, the Bank believes that it is well positioned to use other sources of funds such as FHLB borrowings, repurchase agreements and Bank lines of credit to offset a decline in deposits in the short run. Over the long-term, an adjustment in assets and change in business emphasis could compensate for a potential loss of deposits. The Bank also maintains a marketable investment portfolio to provide flexibility in the event of significant liquidity needs. The Bank Board's Asset Liability Board Committee has adopted policy guidelines which emphasize the importance of core deposits and their continued growth.

At December 31, 2007, under the Bank's liquidity formula, it had $236 million of primary and secondary liquidity sources, which was deemed adequate to meet current and projected funding needs.

INTEREST RATE RISK MANAGEMENT

Asset/Liability Management and Quantitative and Qualitative Disclosure about Market Risk

A fundamental risk in banking is exposure to market risk, or interest rate risk, since a bank's net income is largely dependent on net interest income. The Bank's Asset Liability Committee ("ALCO") of the Board of Directors formulates and monitors the management of interest rate risk through policies and guidelines established by it and the full Board of Directors. In its consideration of risk limits, the ALCO considers the impact on earnings and capital, the level and direction of interest rates, liquidity, local economic conditions, outside threats and other factors. Banking is generally a business of managing the maturity and re-pricing mismatch inherent in its asset and liability cash flows and to provide net interest income growth consistent with the Company's profit objectives.

The Company, through its ALCO, monitors the interest rate environment in which it operates and adjusts the rates and maturities of its assets and liabilities to remain competitive and to achieve its overall financial objectives subject to established risk limits. In the current interest rate environment, the Company has been extending the duration of its investment and loan portfolios and acquiring more variable and short-term liabilities, so as to mitigate the risk to earnings and capital should interest rates decline from current levels. There can be no assurance that the Company will be able to successfully achieve its optimal asset liability mix, as a result of competitive pressures, customer preferences and the inability to perfectly forecast future interest rates.

One of the tools used by the Company to manage its interest rate risk is a static GAP analysis presented below. The Company also uses an earnings simulation model (simulation analysis) on a quarterly basis to monitor its interest rate sensitivity and risk and to model its balance sheet cash flows and its income statement effects in different interest rate scenarios. The model utilizes current balance sheet data and attributes and is adjusted for assumptions as to investment maturities (calls), loan prepayments, interest rates, the level of noninterest income and noninterest expense. The data is then subjected to a "shock test" which assumes a simultaneous change in interest rate up 100 and 200 basis points or down 100 and 200 basis points, along the entire yield curve, but not below zero. The results are analyzed as to the impact on net interest income, and net income over the next twelve and twenty four month periods and to the market value of equity impact.

For the analysis presented below, the bank modified its assumption in the third quarter of 2007 (i.e. the September 30, 2007 analysis) for the re-pricing of money market deposit accounts to reflect a change of 50 basis points in money market interest rates for each 100 basis points in market interest rates in both a decreasing and increasing interest rate shock scenario. This assumption change was based on the bank's demand for funds and its recent experience with market interest rates in the third quarter of 2007. Prior analysis assumed that money market rates were changed 100 basis points for each 100 basis points movement in general interest rates.

As quantified in the table below, the Company's analysis at December 31, 2007 shows a moderate effect on net interest income and net income (over the next 12 months) as well as to the economic value of

equity when interest rates are shocked both down 100 and 200 basis points and up 100 and 200 basis points due to the significant level of variable rate and repriceable assets and liabilities. The re-pricing duration of the investment portfolio is 2.2 years, the loan portfolio 1.4 years; the interest bearing deposit portfolio 1.4 years and the borrowed funds portfolio 0.8 years.

Over the next twelve months, as denoted in the GAP table below, the Company has an excess of rate sensitive liabilities over rate sensitive assets of 6%. During the year 2007, the Company has recognized the probability of lower market interest rates and has kept its time deposit maturities short-term and its money market accounts at as low a rate as possible without incurring substantial deposit runoff. On the asset side, the duration of the loan portfolio was lengthened slightly during 2007 as more fixed and adjustable rate structures were emphasized as opposed to variable interest rate structures. Additionally, during 2007, in anticipation of lower market interest rates, investment purchases were made with longer duration to partially offset higher call risk embedded in the investment portfolio. As well, some callable investments were sold at modest gains in 2007 to mitigate call risk. At December 31, 2007 the investment portfolio's duration was 2.2 years, only slightly less than the 2.7 years at December 31, 2006.

The following table reflects the result of simulation analysis on the December 31, 2007 asset and liabilities balances:

Change in interest rates (basis points)	Percentage change in net interest income	Percentage change in net income	Percentage change in market value of portfolio equity
+200	-3.2%	-8.4%	-3.1%
+100	-1.5%	-3.9%	-1.3%
0			
-100	+1.0%	+2.6%	-2.5%
-200	+1.0%	+2.7%	-8.8%

The results of simulation are within the policy limits adopted by the Company. For net interest income, the Company has adopted a policy limit of 15% for a 100 basis point change and 20% for a 200 basis point change. For the market value of equity, the Company has adopted a policy limit of 20% for a 100 basis point change and 25% for a 200 basis point change. The change in the economic value of equity in a lower interest rate shock scenario at December 31, 2007 as compared to December 31, 2006 is due primarily to added call risk in the investment portfolio.

Certain shortcomings are inherent in the method of analysis presented in the foregoing table. For example, although certain assets and liabilities may have similar maturities or re-pricing periods, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. The effect of competition on loan and deposit pricing may vary from the assumptions used in performing the rate shock analysis. Additionally, certain assets, such as adjustable rate mortgage loans, have features that restrict changes in interest rates on a short-term basis and over the life of the loan. Further, in the event of a change in interest rates, prepayment and early withdrawal levels could deviate significantly from those assumed in calculating the tables. Finally, the ability of many borrowers to service their debt may decrease in the event of a significant interest rate increase.

GAP Analysis

Banks and other financial institutions earnings are significantly dependent upon net interest income, which is the difference between interest earned on earning assets and interest expense on interest bearing liabilities.

In falling interest rate environments, net interest income is maximized with longer term, higher yielding assets being funded by lower yielding short-term funds, or what is referred to as a negative mismatch or GAP. Conversely, in a rising interest rate environment, net interest income is maximized with shorter term, higher yielding assets being funded by longer-term liabilities or what is referred to as a positive mismatch or GAP.

Based on the current economic environment, management has been attempting to extend the duration of assets (both investments and loans) and emphasizing the acquisition of variable rate deposits and shorter-term time deposits. The Company has also acquired low cost FHLB callable advances to better manage the net interest margin. This strategy has mitigated the Company's exposure to lower interest rates as measured at December 31, 2007 and December 31, 2006 as compared to the position at December 31, 2005. While management believes that this overall position creates a reasonable balance in managing its interest rate risk and maximizing its net interest margin within plan objectives, there can be no assurance as to actual results.

The GAP position, which is a measure of the difference in maturity and re-pricing volume between assets and liabilities, is a means of monitoring the sensitivity of a financial institution to changes in interest rates. The chart below provides an indication of the sensitivity of the Company to changes in interest rates. A negative GAP indicates the degree to which the volume of repriceable liabilities exceeds repriceable assets in given time periods. At December 31, 2007, the Company had a slight positive GAP position of approximately 2% of total assets out to three months and a negative cumulative GAP position of 6% out to 12 months, as compared to a three month negative GAP of 1% and a negative cumulative GAP out to 12 months of 17% at December 31, 2006 and a three month positive GAP of 5% and a negative cumulative GAP out to 12 months of 8% at September 30, 2007.

The change in the negative cumulative GAP position at December 31, 2007 as compared to December 31, 2006 (minus 6% as compared to minus 17%) was due primarily to the assumption change mentioned above in the third quarter of 2007 related to the re-pricing of money market deposit accounts (to reflect a change of 50 basis points in money market interest rates for each 100 basis points in market interest rates in both a decreasing and increasing interest rate shock scenario). The current position is within guideline limits established by ALCO.

If interest rates decline, the Company's net interest income and margin over twelve months is expected to be relatively stable because of the present slight positive mismatch position out to 90 days (2%) combined with a more competitive business environment for both deposits and loans. Because competitive market behavior does not necessarily track the trend of interest rates but at times moves ahead of financial market influences, the change in the cost of liabilities may be different than anticipated by the GAP model. If this were to occur, any benefits of a declining interest rate environment may not be in accordance with management's expectations. If interest rates decline, the Company's interest rate sensitivity position at December 31, 2007 as compared to December 31, 2006 shows a similar risk position with regard to net interest income change, which is within established policy limits established by ALCO. Management has carefully considered its strategy to maximize interest income by reviewing interest rate levels, economic indicators and call features within its investment portfolio. These factors have been discussed with the ALCO and management believes that current strategies are appropriate to current economic and interest rate trends.

GAP Table

Repriceable in:	0-3 mos	4-12 mos	13-36 mos	37-60 mos	over 60 mos	Total Rate Sensitive	Non-sensitive	Total Assets
				(dollars in thousands)				
ASSETS:								
Investments	$ 7,104	$ 21,939	$ 43,261	$ 7,061	$ 7,752	$ 87,117		
Loans(1)	303,719	84,361	162,261	134,935	33,578	718,854		
Federal funds sold and other short-term investments	4,734					4,734		
Other earning assets		11,984				11,984		
Total	$ 315,557	$ 118,284	$ 205,522	$ 141,996	$ 41,330	$ 822,689	$ 23,711	$ 846,400
LIABILITIES:								
Noninterest bearing demand	$ 5,110	$ 15,922	$ 42,460	$ 42,460	$ 36,525	$ 142,477		
Interest bearing transaction	27,050		10,816	10,816	5,408	54,090		
Savings and money market	87,341		35,896	35,896	17,948	177,081		
Time deposits	77,969	172,926	4,620	1,773		257,288		
Customer repurchase agreements & federal funds purchased	76,408					76,408		
Other borrowings	22,000		20,000	10,000		52,000		
Total	$ 295,878	$ 188,848	$ 113,792	$ 100,945	$ 59,881	$ 759,344	$ 5,890	$ 765,234
GAP	$ 19,679	$ (70,564)	$ 91,730	$ 41,051	$ (18,551)	$ 63,345		
Cumulative GAP	$ 19,679	$ (50,885)	$ 40,845	$ 81,896	$ 63,345			
Cumulative GAP as percent of total assets	2.33%	-6.01%	4.83%	9.68%	7.48%			

(1) Includes loans held for sale and non-accrual loans.

Although interest bearing transaction accounts and money market accounts (which are administered rates) are subject to re-pricing as a whole category of deposits, the Bank's GAP model has incorporated a re-pricing schedule to account for the historical lag in effecting rate changes and the amount of those rate changes relative to the amount of rate change in assets. However, this measurement of interest rate risk sensitivity represents a static position as of a single day and is not necessarily indicative of the Company's position at any other point in time, does not take into account the differences in sensitivity of yields and costs on specific assets and liabilities to changes in market rates, and it does not take into account the specific timing of when changes to a specific asset or liability will occur.

CAPITAL RESOURCES AND ADEQUACY

The assessment of capital adequacy depends on a number of factors such as asset quality, liquidity, earnings performance, changing competitive conditions and economic forces, as well as the overall level of growth. The adequacy of the Company's current and future capital needs is monitored by management on an ongoing basis. Management seeks to maintain a capital structure that will assure an adequate level of capital to support anticipated asset growth and to absorb potential losses.

The capital position of the Company's wholly-owned subsidiary, the Bank, continues to meet regulatory requirements as a well-capitalized institution. The primary indicators relied on by bank regulators in measuring the capital position are the Tier 1 risk-based capital, total risk-based capital, and leverage ratios. Tier 1 capital consists of common and qualifying preferred stockholders' equity less goodwill and other intangibles of which the Bank has none, and for the Company a limited amount of certain other restricted core capital elements, such as qualifying trust preferred securities and minority interests in consolidated subsidiaries. Total risk-based capital consists of Tier 1 capital, qualifying subordinated

debt, and the qualifying portion of the allowance for credit losses, 100% of which qualifies at

December 31, 2007 and 2006, and for the Company, a limited extent excess amounts of restricted core capital elements. Risk-based capital ratios are calculated with reference to risk-weighted assets, which are prescribed by regulation. The Tier 1 capital to average assets ratio is often referred to as the leverage ratio.

The Company's capital ratios were all in excess of guidelines established by the Federal Reserve and the Bank's capital ratios as earlier mentioned were in excess of those required to be classified as a "well capitalized" institution under the prompt corrective action rule of the Federal Deposit Insurance Act. The Company and Bank's capital ratios at December 31, 2007 and 2006 are shown in Note 15 to the Consolidated Financial Statements.

The ability of the Company to continue to grow is dependent on its earnings and those of the Bank, the ability to obtain additional funds for contribution to the Bank's capital, through additional borrowings, through the sale of additional common stock or preferred stock, or through the issuance of additional qualifying equity equivalents, such as subordinated debt or trust preferred securities. The capital levels required to be maintained by the Company and Bank may be impacted as a result of the Bank's concentrations in commercial real estate loans. See "Regulation" and "Risk Factors".

IMPACT OF INFLATION AND CHANGING PRICES

The Consolidated Financial Statements and Notes thereto have been 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 due to inflation. The impact of inflation is reflected in the increased cost of operations. Unlike most industrial companies, nearly all of our assets and liabilities are monetary in nature. As a result, interest rates have a greater impact on our performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the price of goods or services.

NEW ACCOUNTING STANDARDS

Refer to Note 1 of the Notes to Consolidated Financial Statements for statements on New Accounting Standards.

MARKET FOR COMMON STOCK AND DIVIDENDS

Market for Common Stock. The Company's common stock is listed for trading on the NASDAQ Capital Market under the symbol "EGBN". Over the twelve month period ended December 31, 2007, the average daily trading amounted to approximately 5,000 shares. No assurance can be given that a very active trading market will develop in the foreseeable future or can be maintained. The following table sets forth the high and low sale prices for the common stock during each calendar quarter during the last two fiscal years, and dividends declared during such periods, as adjusted for the 1.3 for 1 stock split paid in the form of a 30% stock dividend on July 5, 2006. As of March 11, 2008, there were 9,780,418 shares of common stock outstanding, held by approximately 1,725 beneficial shareholders, including approximately 744 shareholders of record.

	2007			2006		
Quarter	**High**	**Low**	**Dividends Declared per Share**	**High**	**Low**	**Dividends Declared per Share**
First	$ 17.43	$ 15.75	$ 0.06	$ 18.58	$ 16.46	$ 0.05
Second	$ 17.00	$ 16.25	$ 0.06	$ 19.92	$ 16.95	$ 0.06
Third	$ 16.99	$ 12.75	$ 0.06	$ 21.19	$ 18.49	$ 0.06
Fourth	$ 13.95	$ 11.26	$ 0.06	$ 19.14	$ 16.78	$ 0.06

Dividends. The Company commenced paying a quarterly cash dividend in January 2005. While the Company has adequate liquidity at present, the payment of future cash dividends may depend upon the ability of the Bank, its principal operating business, to declare and pay dividends to the Company. Future dividends will depend primarily upon the Bank's earnings, financial condition, and need for funds, as well as governmental policies and regulations applicable to the Company and the Bank.

In June 2006, the Company declared a 1.3 for 1 stock split in the form of a 30% stock dividend, which was paid on July 5, 2006.

In January 2007, the Company established a Dividend Reinvestment Plan, pursuant to which stockholders may have dividends paid on their common stock automatically reinvested in additional shares of common stock. The price at which shares are reinvested may be at a discount of 5% from the market price, where the shares are newly issued shares purchased directly from the Company. Forty- seven thousand (47,000) shares were issued under this plan during 2007.

Regulations of the Federal Reserve Board and Maryland law place limits on the amount of dividends the Bank may pay to the Company without prior approval. Prior regulatory approval is required to pay dividends which exceed the Bank's net profits for the current year plus its retained net profits for the preceding two calendar years, less required transfers to surplus. Under Maryland law, dividends may only be paid out of retained earnings. State and federal bank regulatory agencies also have authority to prohibit a bank from paying dividends if such payment is deemed to be an unsafe or unsound practice, and the Federal Reserve Board has the same authority over bank holding companies.

The Federal Reserve Board has established guidelines with respect to the maintenance of appropriate levels of capital by registered bank holding companies. Compliance with such standards, as presently in effect, or as they may be amended from time to time, could possibly limit the amount of dividends that the Company may pay in the future. In 1985, the Federal Reserve Board issued a policy statement on the payment of cash dividends by bank holding companies. In the statement, the Federal Reserve Board expressed its view that a holding company experiencing earnings weaknesses should not pay cash dividends exceeding its net income, or which could only be funded in ways that weaken the holding company's financial health, such as by borrowing. As a depository institution, the deposits of which are insured by the FDIC, the Bank may not pay dividends or distribute any of its capital assets while it remains in default on any assessment due the FDIC. The Bank currently is not in default under any of its obligations to the FDIC.

Issuer Repurchase of Common Stock. No shares of the Company's Common Stock were repurchased by or on behalf of the Company during 2007.

Internet Access To Company Documents. The Company provides access to its SEC filings through the Bank's web site at www.eaglebankmd.com by linking to the SEC's web site. After accessing the web site, the filings are available upon selecting "Investor Relations SEC Filings." Reports available include the annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after the reports are electronically filed or furnished to the SEC.

Securities Authorized for Issuance Under Equity Compensation Plans. The following table sets forth information regarding outstanding options and other rights to purchase or acquire common stock granted under the Company's compensation plans as of December 31, 2007:

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights		Weighted average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in column (a)
	(a)		(b)	(c)
Equity compensation plans approved by security holders(1)	746,944	$	10.07	622,870(2)
Equity compensation plans not approved by security holders	0		0	0
Total	746,944	$	10.07	622,870

(1) Consists of the Company's 1998 Stock Option Plan, 2006 Stock Plan and the Employee Stock Purchase Plan. Outstanding options, warrants and rights includes nominal number of shares subject to awards of SARS and shares subject to unvested performance based restricted stock awards. For additional information, see Note 11 to the Consolidated Financial Statements.

(2) Shares include 497,776 available for issuance under the 2006 Stock Option Plan and 125,094 under the Employee Stock Purchase Plan.

Stock Price Performance. The following table compares the cumulative total return on a hypothetical investment of $100 in the Company's common stock on December 31, 2002 through December 31, 2007, with the hypothetical cumulative total return on the NASDAQ Stock Market Index (U.S. Companies) and the NASDAQ Bank Index for the comparable period, including reinvestment of dividends.

December 31,

	2002	2003	2004	2005	2006	2007
Eagle Bancorp, Inc.	$ 100.00	$ 129.36	$ 150.07	$ 222.96	$ 220.61	$ 155.91
Nasdaq Stock Market Index (U.S. Companies)	$ 100.00	$ 150.01	$ 162.89	$ 165.13	$ 180.85	$ 198.60
Nasdaq Bank Index	$ 100.00	$ 129.93	$ 144.21	$ 137.97	$ 153.15	$ 119.35

REPORT OF STEGMAN & COMPANY
INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and
Stockholders of Eagle Bancorp, Inc.

We have audited the accompanying consolidated balance sheets of Eagle Bancorp, Inc. (the "Company") and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these 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, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Eagle Bancorp Inc. as of December 31, 2007 and 2006, and the results of its operations and cash flows for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Eagle Bancorp Inc's. internal control over financial reporting as of December 31, 2007, 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 March 10, 2008 expressed an unqualified opinion.

/s/ Stegman & Company
Stegman & Company
Baltimore, Maryland
March 10, 2008

EAGLE BANCORP, INC.

Consolidated Balance Sheets

	December 31, 2007	December 31, 2006
	(dollars in thousands)	
ASSETS		
Cash and due from banks	$ 15,408	$ 19,250
Federal funds sold	244	9,727
Interest bearing deposits with banks and other short-term investments	4,490	4,855
Investment securities available for sale, at fair value	87,117	91,140
Loans held for sale	2,177	2,157
Loans	716,677	625,773
Less allowance for credit losses	(8,037)	(7,373)
Loans, net	708,640	618,400
Premises and equipment, net	6,701	6,954
Deferred income taxes	3,597	3,278
Bank Owned Life Insurance	11,984	11,529
Accrued interest, taxes and other assets	6,042	6,161
TOTAL ASSETS	$ 846,400	$ 773,451
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits:		
Noninterest bearing demand	$ 142,477	$ 139,917
Interest bearing transaction	54,090	66,596
Savings and money market	177,081	159,778
Time, $100,000 or more	173,586	158,495
Other time	83,702	103,729
Total deposits	630,936	628,515
Customer repurchase agreements and federal funds purchased	76,408	38,064
Other short-term borrowings	22,000	8,000
Long-term borrowings	30,000	22,000
Other liabilities	5,890	3,956
Total liabilities	765,234	700,535
STOCKHOLDERS' EQUITY		
Common stock, $.01 par value; shares authorized 20,000,000, shares issued and outstanding 9,721,315 (2007) and 9,478,064 (2006)	97	95
Additional paid in capital	52,290	50,278
Retained earnings	28,195	22,796
Accumulated other comprehensive income (loss)	584	(253)
Total stockholders' equity	81,166	72,916
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 846,400	$ 773,451

See notes to consolidated financial statements.

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EAGLE BANCORP, INC.

Consolidated Statements of Operations

Years Ended December 31,

	2007	2006	2005
	(dollars in thousands, except per share data)		
Interest Income			
Interest and fees on loans	$ 51,931	$ 45,814	$ 33,478
Taxable interest and dividends on investment securities	4,177	3,277	2,424
Interest on balances with other banks and short-term investments	293	212	417
Interest on federal funds sold	676	1,015	407
Total interest income	57,077	50,318	36,726
Interest Expense			
Interest on deposits	19,810	15,603	7,463
Interest on customer repurchase agreements and federal funds purchased	1,887	1,199	350
Interest on short-term borrowings	611	639	195
Interest on long-term borrowings	1,421	439	
Total interest expense	23,729	17,880	8,008
Net Interest Income	33,348	32,438	28,718
Provision for Credit Losses	1,643	1,745	1,843
Net Interest Income After Provision For Credit Losses	31,705	30,693	26,875
Noninterest Income			
Service charges on deposits	1,491	1,386	1,153
Gain on sale of loans	1,036	1,114	1,245
Gain on sale of investment securities	6	124	279
Increase in the cash surrender value of bank owned life insurance	455	406	401
Income from subordinated financing	1,252		
Other income	946	816	920
Total noninterest income	5,186	3,846	3,998
Noninterest Expense			
Salaries and employee benefits	14,167	12,230	10,503
Premises and equipment expenses	4,829	3,835	3,470
Marketing and advertising	465	587	473
Outside data processing	793	881	769
Legal, accounting and professional fees	611	801	759
Other expenses	4,056	3,490	2,986
Total noninterest expense	24,921	21,824	18,960
Income Before Income Tax Expense	11,970	12,715	11,913

	2007	2006	2005
Income Tax Expense	4,269	4,690	4,369
Net Income	$ 7,701	$ 8,025	$ 7,544
Earnings Per Share			
Basic	$ 0.80	$ 0.85	$ 0.82
Diluted	$ 0.78	$ 0.81	$ 0.77
Dividends Declared Per Share	$ 0.24	$ 0.23	$ 0.22

See notes to consolidated financial statements.

EAGLE BANCORP, INC.

Consolidated Statements of Changes in Stockholders' Equity

For The Years Ended December 31, 2007, 2006 and 2005

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
			(dollars in thousands)		
Balance January 1, 2005	$ 54	$ 47,014	$ 11,368	$ 98	$ 58,534
Comprehensive Income					
Net Income			7,544		7,544
Other comprehensive income:					
Unrealized loss on securities available for sale (net of taxes)				(549)	(549)
Less: reclassification adjustment for gains net of taxes of $110 included in net income				(169)	(169)
Total Comprehensive Income				(718)	6,826
Cash Dividends ($0.22 per share)			(1,994)		(1,994)
1.3 to one stock split in the form of a 30% stock dividend	17	(17)			
Cash paid in lieu of fractional shares		(4)			(4)
Exercise of options for 136,841 shares of common stock	1	1,133			1,134
Tax benefit on non-qualified options exercise		468			468
Balance December 31, 2005	**72**	**48,594**	**16,918**	**(620)**	**64,964**
Comprehensive Income					
Net Income			8,025		8,025
Other comprehensive income:					
Unrealized gain on securities available for sale (net of taxes)				442	442
Less: reclassification adjustment for gains net of taxes of $49 included in net income				(75)	(75)
Total Comprehensive Income				367	8,392
Cash Dividends ($0.23 per share)			(2,147)		(2,147)
Stock-based compensation		345			345
1.3 to one stock split in the form of a 30% stock dividend	22	(22)			
Cash paid in lieu of fractional shares		(5)			(5)
Exercise of options for 137,999 shares of common stock	1	935			936
Tax benefit on non-qualified options exercise		431			431
Balance December 31, 2006	**95**	**50,278**	**22,796**	**(253)**	**72,916**
Comprehensive Income					
Net Income			7,701		7,701
Other comprehensive income:					
Unrealized gain on securities available for sale (net of taxes)				841	841
Less: reclassification adjustment for gains net of taxes of $2 included in net income				(4)	(4)
Total Comprehensive Income				837	8,538
Cash Dividends ($0.24 per share)			(2,302)		(2,302)

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Stock-based compensation		224			224
Shares issued under dividend reinvestment plan 47,000 shares	0	689			689
Exercise of options for 196,251 shares of common stock	2	1,080			1,082
Excess tax benefits from stock-based compensation		19			19
Balance December 31, 2007	**$ 97**	**$ 52,290**	**$ 28,195**	**$ 584**	**$ 81,166**

See notes to consolidated financial statements.

EAGLE BANCORP, INC.

Consolidated Statements of Cash Flows

Years Ended December 31,

	2007	2006	2005
		(dollars in thousands)	
Cash Flows From Operating Activities:			
Net income	$ 7,701	$ 8,025	$ 7,544
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Decrease in deferred income taxes	(868)	(647)	(1,312)
Provision for credit losses	1,643	1,745	1,843
Depreciation and amortization	1,347	1,196	1,122
Gains on sale of loans	(1,036)	(1,114)	(1,245)
Origination of loans held for sale	(52,455)	(59,966)	(29,083)
Proceeds from sale of loans held for sale	53,471	61,847	29,612
Gain on sale of investment securities	(6)	(124)	(279)
Net increase in surrender value of Bank-owned life insurance	(455)	(406)	(402)
Stock-based compensation expense	224	345	
Excess tax benefit from stock-based compensation	(19)	(431)	(468)
Decrease (increase) in other assets	119	(1,857)	(1,700)
Increase (decrease) in other liabilities	1,953	(1,869)	4,408
Net cash provided by operating activities	11,619	6,744	10,040
Cash Flows From Investing Activities:			
Decrease (increase) in interest bearing deposits other banks	365	6,376	(1,637)
Purchases of available for sale investment securities	(33,695)	(48,632)	(48,336)
Proceeds from maturities of available for sale securities	9,784	20,979	31,230
Proceeds from sale/call of available for sale securities	29,326	5,277	12,275
Net increase in loans	(91,882)	(76,918)	(133,801)
Bank premises and equipment acquired	(1,094)	(2,376)	(1,170)
Net cash used in investing activities	(87,197)	(95,294)	(141,439)
Cash Flows From Financing Activities:			
Increase in deposits	2,421	59,622	106,606
Increase in customer repurchase agreements and Fed Funds	38,344	5,925	8,156
Increase (decrease) in other short-term borrowings	14,000	8,000	(6,333)
Increase in long-term borrowings	8,000	22,000	
Issuance of common stock	1,771	936	1,130
Excess tax benefit from stock-based compensation	19	431	468
Payment of dividends and payment in lieu of fractional shares	(2,302)	(2,152)	(1,998)
Net cash provided by financing activities	62,253	94,762	108,029
Net (decrease) increase in cash	(13,325)	6,212	(23,370)
Cash and cash equivalents at beginning of year	28,977	22,765	46,135
Cash and cash equivalents at end of year	$ 15,652	$ 28,977	$ 22,765
Supplemental cash flows information:			
Interest paid	$ 23,640	$ 16,906	$ 7,571

	2007	2006	2005
Income taxes paid	$ 4,052	$ 4,751	$ 5,083
Non-cash Financing Activities			
Reclassification of borrowings from long-term to short-term	$ 22,000	$	$
Non-cash Investing Activities			
Transfers from loans to other real estate owned	$	$ 257	$

See notes to consolidated financial statements.

Eagle Bancorp, Inc.

Notes to Consolidated Financial Statements for the Years Ended

December 31, 2007, 2006 and 2005

Note 1 Significant Accounting Policies

The consolidated financial statements include the accounts of Eagle Bancorp, Inc. (the "Company") and its subsidiaries, EagleBank (the "Bank") and Eagle Commercial Ventures LLC ("ECV") with all significant intercompany transactions eliminated. The investment in subsidiaries is recorded on the Company's books (Parent Only) on the basis of its equity in the net assets of the subsidiary. The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America and to general practices in the banking industry. Certain reclassifications have been made to amounts previously reported to conform to the classification made in 2007. The following is a summary of the more significant accounting policies.

Nature of Operations

The Company, through its bank subsidiary, conducts a full service community banking business, primarily in Montgomery County, Maryland and Washington, D.C. The primary financial services include real estate, commercial and consumer lending, as well as traditional deposit and repurchase agreement products. The Bank is also active in the origination and sale of residential mortgage loans and the origination of small business loans. The guaranteed portion of small business loans is typically sold through the Small Business Administration, in a transaction apart from the loan's origination. The Bank offers its products and services through nine banking offices and various electronic capabilities, including remote deposit services introduced in 2006. In July 2006, the Company formed Eagle Commercial Ventures, LLC as a direct subsidiary to provide subordinated financing for the acquisition, development and construction of real estate projects, whose primary financing would be done by the Bank.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, and federal funds sold (items with an original maturity of three months or less).

Loans Held for Sale

The Company engages in sales of residential mortgage loans and the guaranteed portion of Small Business Administration ("SBA") loans originated by the Bank. Loans held for sale are carried at the lower of aggregate cost or fair value. Fair value is derived from secondary market quotations for similar instruments. Gains and losses on sales of these loans are recorded as a component of noninterest income in the Consolidated Statements of Operations.

The Company's current practice is to sell residential mortgage loans on a servicing released basis, and, therefore, it has no intangible asset recorded for the value of such servicing as of December 31, 2007 or 2006. The sale of the guaranteed portion of SBA loans on a servicing retained basis gives rise to an Excess Servicing Asset, which is computed on a loan by loan basis and which unamortized amount is included in other assets. This asset is being amortized on a straight line basis (with adjustment for prepayments) as an offset of servicing fees collected and is included in other noninterest income.

Note 1 Significant Accounting Policies (Continued)

The Company enters into commitments to originate residential mortgage loans whereby the interest rate on the loan is determined prior to funding (i.e. rate lock commitments). Such rate lock commitments on mortgage loans to be sold in the secondary market are considered to be derivatives. The period of time between issuance of a loan commitment and closing and sale of the loan generally ranges from 15 to 60 days. The Company protects itself from changes in interest rates through the use of best efforts forward delivery commitments, whereby the Company commits to sell a loan at the time the borrower commits to an interest rate with the intent that the buyer has assumed interest rate risk on the loan. As a result, the Company is not exposed to losses nor will it realize gains related to its rate lock commitments due to changes in interest rates.

The market values of rate lock commitments and best efforts contracts are not readily ascertainable with precision because rate lock commitments and best efforts contracts are not actively traded. Because of the high correlation between rate lock commitments and best efforts contracts, no gain or loss occurs on the rate lock commitments.

Investment Securities

The Company has no securities classified as trading nor are any investment securities classified as held-to-maturity. Marketable equity securities and debt securities not classified as held-to-maturity or trading are classified as available-for-sale. Securities available-for-sale are acquired as part of the Company's asset/liability management strategy and may be sold in response to changes in interest rates, loan demand, changes in prepayment risk and other factors. Securities available-for-sale are carried at fair value, with unrealized gains or losses being reported as accumulated other comprehensive income, a separate component of stockholders' equity, net of deferred tax. Realized gains and losses, using the specific identification method, are included as a separate component of noninterest income. Declines in the fair value of individual available-for-sale securities below their cost that are other than temporary in nature result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether other-than-temporary impairment has occurred include a downgrading of the security by a rating agency, a significant deterioration in the financial condition of the issuer, or a change in management's intent and ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value.

Loans

Loans are stated at the principal amount outstanding, net of unamortized deferred costs and fees. Interest income on loans is accrued at the contractual rate on the principal amount outstanding. It is the Company's policy to discontinue the accrual of interest when circumstances indicate that collection is doubtful. Deferred fees and costs on loans originated through October 2005 are being amortized on the straight line method over the term of the loan. Deferred fees and costs on loans originated subsequent to October 2005 are being amortized on the interest method over the term of the loan. The difference between the straight line method and the interest method was considered immaterial.

Management considers loans impaired when, based on current information, it is probable that the Company will not collect all principal and interest payments according to contractual terms. Loans are evaluated for impairment in accordance with the Company's portfolio monitoring and ongoing risk assessment procedures. Management considers the financial condition of the borrower, cash flow of the borrower, payment status of the loan, and the value of the collateral, if any, securing the loan. Generally, impaired loans do not include large groups of smaller balance homogeneous loans such as residential real estate and consumer type loans which loans are evaluated collectively for impairment and are generally placed on non-accrual when the loan becomes 90 days past due as to principal or interest. Loans specifically reviewed for impairment are not considered impaired during periods of "minimal delay" in payment (ninety days or less) provided eventual collection of all amounts due is expected. The impairment

of a loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if repayment is expected to be provided solely by the collateral. In appropriate circumstances, interest income on impaired loans may be recognized on the cash basis.

Allowance for Credit Losses

The allowance for credit losses represents an amount which, in management's judgment, is adequate to absorb probable losses on existing loans and other extensions of credit that may become uncollectible. The adequacy of the allowance for credit losses is determined through careful and continuous review and evaluation of the loan portfolio and involves the balancing of a number of factors to establish a prudent level of allowance. Among the factors considered in evaluating the adequacy of the allowance for credit losses are lending risks associated with growth and entry into new markets, loss allocations for specific nonperforming credits, the level of the allowance to nonperforming loans, historical loss experience, economic conditions, portfolio trends and credit concentrations, changes in the size and character of the loan portfolio, and management's judgment with respect to current and expected economic conditions and their impact on the existing loan portfolio. Allowances for collateral impaired loans are generally determined based on collateral values. Loans or any portion thereof deemed uncollectible are charged against the allowance, while recoveries are credited to the allowance. Management adjusts the level of the allowance through the provision for credit losses, which is recorded as a current period operating expense. The allowance for credit losses consists of allocated and unallocated components.

The components of the allowance for credit losses represent an estimation done pursuant to either Statement of Financial Accounting Standards ("SFAS") No. 5, "*Accounting for Contingencies*," or SFAS No. 114, "*Accounting by Creditors for Impairment of a Loan.*" Specific allowances are established in cases where management has identified significant conditions or circumstances related to a specific credit that management believes indicate the probability that a loss may be incurred. For potential problem credits for which specific allowance amounts have not been determined, the Company establishes allowances according to the application of credit risk factors. These factors are set by management to reflect its assessment of the relative level of risk inherent in each risk grade. A third component of the allowance computation, termed a nonspecific or environmental factors allowance, is based upon management's evaluation of various environmental conditions that are not directly measured in the determination of either the specific allowance or formula allowance. Such conditions include general economic and business conditions affecting key lending areas, credit quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes and concentrations, specific industry conditions within portfolio categories, recent loss experience in particular loan categories, duration of the current business cycle, bank regulatory examination results, findings of outside review consultants, and management's judgment with respect to various other conditions including credit administration and management and the quality of risk identification systems. Executive management reviews these environmental conditions quarterly, and documents the rationale for all changes.

Management believes that the allowance for credit losses is adequate; however, determination of the allowance is inherently subjective and requires significant estimates. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. Evaluation of the potential effects of these factors on estimated losses involves a high degree of uncertainty, including the strength and timing of economic cycles and concerns over the effects of a prolonged economic downturn in the current cycle. In addition, various regulatory agencies, as an integral part of their examination process, and independent consultants engaged by the Bank periodically review the Bank's loan portfolio and allowance for credit losses. Such review may result in recognition of additions to the allowance based on their judgments of information available to them at the time of their examination.

Note 1 Significant Accounting Policies (Continued)

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization computed using the straight-line method for financial reporting purposes. Premises and equipment are depreciated over the useful lives of the assets, which generally range from seven years for furniture, fixtures and equipment, three to five years for computer software and hardware, and ten to forty years for buildings and building improvements. Leasehold improvements are amortized over the terms of the respective leases, which may include renewal options where management has the positive intent to exercise such options, or the estimated useful lives of the improvements, whichever is shorter. The costs of major renewals and betterments are capitalized, while the costs of ordinary maintenance and repairs are expensed as incurred. These costs are included as a component of premises and equipment expenses on the Consolidated Statement of Operations.

Marketing and Advertising

Marketing and advertising costs are generally expensed as incurred.

Income Taxes

Income tax expense on the Statements of Operations is based on the results of operations, adjusted for any permanent differences between items of income and deduction recognized for financial reporting purposes differently than for income tax accounting purposes. The Company has adopted the liability method of accounting for income taxes and has recorded deferred tax assets and liabilities determined based on differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities (i.e., temporary differences). Such temporary differences are measured at the enacted rates that are expected to be in effect when these timing differences reverse.

Transfer of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtain the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. In certain cases, the recourse to the Bank to repurchase assets may exist but be deemed immaterial based on the specific facts and circumstances.

Earnings per Common Share

Basic net income per common share is derived by dividing net income available to common stockholders by the weighted-average number of common shares outstanding during the period measured. Diluted earnings per common share is computed by dividing net income available to common stockholders by the weighted-average number of common shares outstanding during the period measured including the potential dilutive effects of common stock equivalents. Earnings per common share has been adjusted to give retroactive reflect to all stock splits.

Stock-Based Compensation

Effective January 2006, in accordance with a new accounting standard (SFAS 123R), the Company records as compensation expense an amount equal to the amortization (over the remaining service period) of the fair value (computed at the date of option grant) of any outstanding stock option grants which vest subsequent to December 31, 2005. Refer to Note 11 for a description of stock-based compensation expense for the years ended December 31, 2007 and 2006.

Note 1 Significant Accounting Policies (Continued)

Through December 31, 2005, the Company adopted the disclosure-only provisions of SFAS No. 123, "*Accounting for Stock-Based Compensation"* ("SFAS 123R") and SFAS 148 "*Accounting for Stock-Based Compensation-Transition and Disclosure"* ("SFAS 148"), but applied Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its stock-based compensation plans. No compensation expense related to the stock- based compensation plans was recorded during the year ended December 31, 2005.

New Accounting Pronouncements

In March 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 156, *"Accounting for Servicing of Financial Assets"*. This Statement amends SFAS No. 140, *"Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities"*, and requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, and permits the entities to elect either fair value measurement with changes in fair value reflected in earnings or the amortization and impairment requirements of SFAS No. 140 for subsequent measurement. The subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value eliminates the necessity for entities that manage the risks inherent in servicing assets and servicing liabilities with derivatives to qualify for hedge accounting treatment and eliminates the characterization of declines in fair value as impairments or direct write-downs. This Statement is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company's servicing asset was for the computed value of servicing fees on the sale of the guaranteed portion of SBA loans. Assumptions related to loan term and amortization is made to arrive at the initial recorded value. This asset is subject to impairment testing annually. The Company does not elect to measure this asset at fair value and believes this new accounting standard had no impact on its financial condition or results of operations.

In June 2006, the FASB issued FASB Interpretation No. 48, "*Accounting for Uncertainty in Income Taxes"* ("FIN 48"). FIN 48 clarifies when tax benefits should be recorded in financial statements, requires certain disclosures of uncertain tax matters and indicates how any tax reserves should be classified in a balance sheet. FIN 48 was effective for the Company in the first quarter of fiscal 2007. The Company does not have any uncertain tax positions and this new accounting standard did not have any impact on its financial condition or results of operation.

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements"* ("SFAS 157"). This statement provides a single definition of fair value, a framework for measuring fair value, and expanded disclosures concerning fair value. Previously, different definitions of fair value were contained in various accounting pronouncements creating inconsistencies in measurement and disclosures. SFAS 157 applies under those previously issued pronouncements that prescribe fair value as the relevant measure of value, except SFAS 123R and related interpretations and pronouncements that require or permit measurement similar to fair value but are not intended to measure fair value. This pronouncement is effective for fiscal years beginning after November 15, 2007. The Company is evaluating the impact of this new standard, but currently believes that adoption will not have a material impact on its financial position, results of operations, or cash flows.

In September 2006, the SEC's Office of the Chief Accountant and Divisions of Corporation Finance and Investment Management released SAB No. 108, "*Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements"* ("SAB 108"), that provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. This pronouncement is effective for fiscal years ending after November 15,

Note 1 Significant Accounting Policies (Continued)

2006. The adoption of SAB 108 had no material impact on the Company's financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, *"The Fair Value Option for Financial Assets and Financial Liabilities"* ("SFAS 159"). SFAS 159 allows entities the option to measure eligible financial instruments at fair value as of specified dates. Such election, which may be applied on an instrument by instrument basis, is typically irrevocable once elected. Statement 159 is effective for fiscal years beginning after November 15, 2007, and early application is allowed under certain circumstances. The Company is evaluating the impact of this new standard, but currently believes that adoption will not have a material impact on its financial position, results of operations, or cash flows.

In December 2007, the FASB issued SFAS 141(R), "*Business Combinations (Revised 2007) (".SFAS 141R").* SFAS 141R replaces SFAS 141, "Business Combinations," and applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost-allocation process required under SFAS 141 whereby the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their estimated fair value. SFAS 141R requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed, as was previously the case under SFAS 141. Under SFAS 141R, the requirements of SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities," would have to be met in order to accrue for a restructuring plan in purchase accounting. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting and, instead, that contingency would be subject to the probable and estimable recognition criteria of SFAS 5, "Accounting for Contingencies." SFAS 141R is expected to have a significant impact on the Company's accounting for business combinations closing on or after January 1, 2009.

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

Note 2 Cash and Due from Banks

Regulation D of the Federal Reserve Act requires that banks maintain reserve balances with the Federal Reserve Bank based principally on the type and amount of their deposits. During 2007, the Bank maintained balances at the Federal Reserve (in addition to vault cash) to meet the reserve requirements as well as balances to partially compensate for services. Additionally, the Bank maintained balances with the Federal Home Loan Bank and five domestic correspondents as compensation for services they provide to the Bank.

Note 3 Investment Securities Available-for-Sale

The amortized cost and estimated fair values of investments available for sale at December 31, 2007 and 2006 are as follows:

December 31, 2007	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	$ 50,428	$ 885	$ 18	$ 51,295
Mortgage backed securities	29,218	220	135	29,303
Municipal bonds	357		6	351
Federal Reserve and Federal Home Loan Bank stock	4,870			4,870
Other equity investments	1,278	20		1,298
	$ 86,151	$ 1,125	$ 159	$ 87,117

December 31, 2006	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	$ 58,803	$ 161	$ 380	$ 58,584
Mortgage backed securities	27,650	69	386	27,333
Federal Reserve and Federal Home Loan Bank stock	3,829			3,829
Other equity investments	1,278	116		1,394
	$ 91,560	$ 346	$ 766	$ 91,140

Gross unrealized losses and fair value by length of time that the individual available-for-sale securities have been in a continuous unrealized loss position as of December 31, 2007 are as follows:

December 31, 2007	Estimated Fair Value	Less than 12 months	More than 12 months	Gross Unrealized Losses
		(dollars in thousands)		
U. S. Government agency securities	$ 5,982	$	$ 18	$ 18
Mortgage backed securities	11,032	6	129	135
Municipal bonds	351	6		6
	$ 17,365	$ 12	$ 147	$ 159

All of the bonds reflected in the above table (the debt instruments) are rated AAA. The debt instruments comprise 100% of the gross unrealized losses at December 31, 2007. The debt instruments have a weighted average duration of 2.2 years, low credit risk, and modest loss (approximately .2%) when compared to amortized cost. The gross unrealized gain on other equity investments represents two banking company stocks owned by the Company (parent only), one of which is not traded on an exchange. The estimated fair value is determined by broker quotes. The unrealized losses that exist on the debt securities are the result of market changes in interest rates since the original purchase. These factors coupled with the fact that the Company has both the intent and ability to hold these investments for the period of time sufficient to allow for any anticipated recovery in fair value substantiates that the unrealized losses in the available-for-sale portfolio are temporary. In addition, at December 31, 2007, the Company held $4.9 million in equity securities in Federal Reserve Bank ("FRB") and Federal Home Loan Bank ("FHLB") stocks which are held for regulatory purposes and are not marketable.

The amortized cost and estimated fair values of investments available-for-sale at December 31, 2007 and 2006 by contractual maturity are shown below. Expected maturities will differ from contractual

Note 3 Investment Securities Available-for-Sale (Continued)

maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	2007		2006	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(dollars in thousands)			
Amounts maturing:				
One year or less	$ 7,999	$ 7,985	$ 6,305	$ 6,284
After one year through five years	20,898	21,310	33,484	33,402
After five years through ten years	21,531	22,000	19,014	18,898
Mortgage backed securities	29,218	29,303	27,650	27,333
Municipal bonds maturing after ten years	357	351		
FRB, FHLB and other equity securities	6,148	6,168	5,107	5,223
	$ 86,151	$ 87,117	$ 91,560	$ 91,140

Realized gains on sales of investment securities were $49 thousand and realized losses on sales of investment securities were $43 thousand in 2007. Realized gains on sales of investment securities were $195 thousand and realized losses on sales of investment securities were $71 thousand in 2006. Realized gains on sales of investment securities were $344 thousand and realized losses on sales of investment securities were $65 thousand in 2005.

Proceeds from sales and calls of investment securities in 2007 were $29.3 million, in 2006 were $5.3 million, and in 2005 were $12.3 million.

At December 31, 2007, $55.5 million (fair value) of securities were pledged as collateral for certain government deposits, and securities sold under agreement to repurchase. The outstanding balance of no single issuer, except for U.S. Government and U.S. Government agency securities, exceeded ten percent of stockholders' equity at December 31, 2007 or 2006.

Note 4 Loans and Allowance for Credit Losses

The Bank makes loans to customers primarily in the Washington, D.C. metropolitan statistical area and surrounding communities. A substantial portion of the Bank's loan portfolio consists of loans to businesses secured by real estate and other business assets.

Note 4 Loans and Allowance for Credit Losses (Continued)

Loans, net of unamortized net deferred fees, at December 31, 2007 and 2006 are summarized by type as follows:

	2007	2006
	(dollars in thousands)	
Commercial	$ 149,332	$ 132,981
Real estate commercial(1)	392,757	349,044
Real estate residential mortgage	2,160	1,523
Construction commercial & residential(1)	110,115	86,524
Home equity	57,515	50,572
Other consumer	4,798	5,129
Total loans	716,677	625,773
Less: Allowance for Credit Losses	(8,037)	(7,373)
Loans net	$ 708,640	$ 618,400

(1) Includes loans for land acquisition and owner occupied properties

Unamortized net deferred fees amounted to $1.5 million and $1.1 million at December 31, 2007 and 2006, respectively, of which $509 thousand and $512 thousand, respectively at December 31, 2007 and 2006 represented net deferred costs on home equity loans.

As of December 31, 2007 and 2006, the Bank serviced $25.8 million and $26.9 million, respectively, of SBA loans participations which are not reflected as loan balances on the on the Consolidated Balance Sheet.

Activity in the allowance for credit losses for the past three years is shown below.

	2007	2006	2005
	(dollars in thousands)		
Balance at beginning of year	$ 7,373	$ 5,985	$ 4,240
Provision for credit losses	1,643	1,745	1,843
Loan charge-offs	(1,031)	(389)	(139)
Loan recoveries	52	32	41
Balance at end of year	$ 8,037	$ 7,373	$ 5,985

Information regarding impaired loans at December 31, 2007 and 2006 is as follows:

	2007	2006
	(dollars in thousands)	
Impaired loans with a valuation allowance	$ 348	$ 1,856
Impaired loans without a valuation allowance	4,975	120
Total impaired loans	$ 5,323	$ 1,976
Allowance for credit losses related to impaired loans	$ 220	$ 678
Allowance for credit losses related to other than impaired loans	7,817	6,695

	2007		2006	
Total allowance for credit losses	$	8,037	$	7,373
Average impaired loans for the year	$	2,903	$	3,267
Interest income on impaired loans recognized on a cash basis	$	75	$	125

Note 5 Premises and Equipment

Premises and equipment include the following at December 31:

	2007	2006
	(dollars in thousands)	
Leasehold improvements	$ 5,738	$ 5,409
Furniture and equipment	7,507	6,877
Less accumulated depreciation and amortization	(6,544)	(5,332)
Total premises and equipment, net	$ 6,701	$ 6,954

The Company leases banking and office space in thirteen locations under non-cancelable lease arrangements accounted for as operating leases. The initial lease periods range from 5 to 10 years and provide for one or more five year renewal options. The leases in some cases provide for scheduled annual rent escalations and require that the Bank (lessee) pay certain operating expenses applicable to the leased space. Rent expense applicable to operating leases amounted to $2.6 million in 2007, $1.9 million in 2006, and $1.7 million in 2005. At December 31, 2007, future minimum lease payments under non-cancelable operating leases having an initial term in excess of one year are as follows. The Company subleases two leased premises and has recorded $63 thousand as a reduction of rent expense during 2007:

	(dollars in thousands)
Years ending December 31:	
2008	$ 2,350
2009	2,383
2010	2,468
2011	2,162
2012	1,837
Thereafter	4,979
Total minimum lease payments	$ 16,179

Note 6 Deposits

The following table provides information regarding the Bank's deposit composition at December 31, of the years indicated and shows the average rate being paid on the interest bearing deposits in December of each year.

	2007		2006		2005	
	Balance	Average Rate	Balance	Average Rate	Balance	Average Rate
	(dollars in thousands)					
Noninterest bearing demand	$ 142,477		$ 139,917		$ 165,103	
Interest bearing transaction	54,090	0.73%	66,596	0.44%	73,666	0.26%
Savings and money market	177,081	2.96%	159,778	3.74%	142,879	2.88%
Time, $100,000 or more	173,586	4.63%	158,495	4.81%	122,571	3.36%
Other time	83,702	5.66%	103,729	5.20%	64,674	3.38%
Total	$ 630,936		$ 628,515		$ 568,893	

Note 6 Deposits (Continued)

The remaining maturity of time deposits at December 31, 2007 and 2006 are as follows:

	2007	2006
	(dollars in thousands)	
Three months or less	$ 82,289	$ 70,408
More than three months through six months	89,737	91,540
More than six months through twelve months	78,870	91,991
Over twelve months	6,392	&nbs