1ST COLONIAL BANCORP INC
Form 424B4
April 22, 2004

PROSPECTUS

720,000 SHARES OF COMMON STOCK

OFFERING PRICE $10.00 PER SHARE

(1ST COLONIAL LOGO)

1st Colonial Bancorp, Inc. is the holding company for 1st Colonial National Bank, Collingswood, New Jersey, a nationally chartered commercial bank that opened for business in June 2000.

We are offering for sale 720,000 shares of our common stock in an underwritten public offering. The offering price is $10.00 per share.

Our common stock is currently traded on the OTC Bulletin Board under the symbol "FCOB." However, the trading market is not active. The last reported sale price for our common stock was $10.25 per share on April 14, 2004. As of April 20, 2004, the bid and asked prices for our common stock were $10.25 and $11.25 per share, respectively.

The shares covered by this prospectus have been registered under the Securities Act of 1933. Concurrently with that registration, we have also registered, on behalf of selling shareholders, 97,024 shares of common stock issuable by us upon the exercise of outstanding warrants. We have agreed to bear all expenses of registration of these shares under federal and state securities laws. The holders of these warrants have agreed not to sell or otherwise dispose of, for a period of 180 days from the conclusion of this offering, any shares of our common stock that they own or acquire. Please also see the Risk Factor pertaining to these shares on page 10.

INVESTING IN THE COMMON STOCK INVOLVES RISKS. YOU SHOULD CAREFULLY CONSIDER THE INFORMATION CONTAINED UNDER THE HEADING "RISK FACTORS" BEGINNING ON PAGE 7 BEFORE MAKING YOUR INVESTMENT DECISION.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THE SECURITIES OFFERED BY THIS PROSPECTUS ARE NOT SAVINGS ACCOUNTS OR DEPOSITS AND ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER GOVERNMENTAL AGENCY.

| | PER SHARE | TOTAL |
|---|---|---|

| | | |
|---|---|---|
| Public offering price | $10.00 | $7,200,000 |
| Underwriting commissions we will pay | $ .69 | $ 494,000 |
| Net proceeds to 1st Colonial Bancorp, Inc., before our expenses | $ 9.31 | $6,706,000 |

This is a firm commitment underwriting. We will pay underwriting commissions for the sale of the shares of common stock to the public. The underwriting commission assumes all shares are sold to the public; however, we will pay a reduced commission on shares sold to our officers and directors. The underwriter has been granted a 30-day option to purchase up to an additional 108,000 shares to cover over-allotments, if any. See "Underwriting."

RYAN BECK & CO.

April 20, 2004

(COLONIAL LOGO)

(MAP)

## SUMMARY

The following summary contains all of the material terms of the offering, but is qualified in its entirety by, and should be read in conjunction with, the more detailed information and the financial statements (including the notes thereto) appearing in this prospectus. In this prospectus, the term "1st Colonial" refers to 1st Colonial Bancorp, Inc., the term the "bank" refers to 1st Colonial National Bank, and the terms "us," "we" and "our" refer to 1st Colonial or the bank, as the context may require.

## 1ST COLONIAL BANCORP, INC.

### WHO WE ARE

1st Colonial Bancorp, Inc. is a bank holding company headquartered in Collingswood, New Jersey, and the parent company of 1st Colonial National Bank. We became the holding company for the bank on June 30, 2002. The bank is a national bank that opened for business on June 30, 2000, and provides a wide range of business and consumer financial services through its main office located in Collingswood, New Jersey and a branch office located in Westville, New Jersey.

Emphasizing customer service, access to decision makers and responsive turnaround time on credit applications, we have grown quickly, achieving profitability during our seventh month of existence. At December 31, 2003, we had $118.1 million in assets, $66.6 million in loans, and $104.3 million in deposits. These amounts reflect increases of $19.8 million or 20.1%, $12.4 million or 22.8% and $21.4 million or 25.8%, respectively, from our assets, loans and deposits of $98.3 million, $54.2 million and $82.9 million, respectively, at December 31, 2002. For the year ended December 31, 2003, we had net income of $500,000, or $0.35 per share.

Our goal is to further increase our assets, deposits and net income by continuing to stress customer service and our identity as a locally operated community bank. We compete with many existing and larger financial institutions in our geographic market by emphasizing personalized service and responsive decision making. We strive to maintain a stable employee base, which leads to customer loyalty and retention. Our management team is led by Gerard M. Banmiller, our president and chief executive officer, and James E. Strangfeld, our executive vice president and senior loan officer. Each of these gentlemen has over 30 years of banking experience, most of which has been in the markets that we serve.

As a bank holding company registered under the Bank Holding Company Act of 1956, we are subject to the supervision and regulation of the Board of Governors of the Federal Reserve System. The bank is chartered as a national bank by Office of the Comptroller of the Currency (OCC), and its deposits are insured by the Bank Insurance Fund of the Federal Deposit Insurance Corporation (FDIC). The bank's operations are subject to supervision and regulation by the FDIC and the OCC. For more information, please see the section of this prospectus entitled "Supervision and Regulation."

Since opening in June 2000, we have accomplished the following:

- Reported 12 consecutive quarters of profitability after becoming profitable in the first quarter of 2001, our third quarter of operations, and achieved earnings of $500,000 for the year ended December 31, 2003;

- Implemented a strong credit culture which has resulted in no non-performing loans and no non-performing assets as of December 31, 2003;

- Assembled a management and lending team of six people who collectively have more than 215 years of banking experience;

- Opened our second full service banking office in Westville, New Jersey;

- Established our local identity in the communities we serve through an extensive marketing campaign that includes sponsoring a wide variety of civic and charitable events; and

- Assembled a board of directors consisting of recognized local business people and civic leaders.



Our principal executive offices are located at 1040 Haddon Avenue, Collingswood, NJ 08108, and our telephone number is (856) 858-1100.

OUR MARKET AREA

We are located in the southwestern part of New Jersey, approximately five miles east of the City of Philadelphia, Pennsylvania, which is the fifth largest city in the United States. Our market area consists of the greater Cherry Hill, New Jersey area and the Borough of Westville, New Jersey. Our target market includes the towns of Collingswood, Cherry Hill, Haddonfield and Westville.

BUSINESS STRATEGY

Our mission is to become the leading community bank in our market area by meeting the credit needs of local businesses and residents, providing relationship banking and customer service that is superior to the larger banks in our market area, and offering products and services responsive to local needs. We intend to increase our market share and presence by opening additional branch offices at convenient and strategic locations and through growth at our existing offices.

We target small and mid-sized businesses as well as professional practices such as lawyers, medical doctors and accountants in our market area. In addition, we have had success marketing our deposit account services to local government entities such as municipalities, school districts and public authorities. This success is largely due to the experience and reputation of our management in serving municipal and local government entities in our marketplace. These deposit relationships are typically operating accounts and longer-term certificates of deposit, which we believe are a stable source of funding for us.

We actively pursue business relationships with our targeted clientele through diligent calling efforts and by capitalizing on our knowledge of the market and pre-existing business relationships. Our goal is to establish deposit and lending relationships that are based on service, will result in long-standing relationships and will lead to referrals from our satisfied customers.

As an added convenience for our government and business customers, we began offering courier pick-up and delivery services to these customers in 2003. We also are planning to add up to two full-service branches by the first quarter of 2006, although we have no definitive arrangements to establish any branches at this time.

An important element of our strategy is to capitalize on the prior experience of our management team in our market, as well as their pre-existing business relationships. Prior to organizing the bank, our president, Gerard M. Banmiller, helped organize Community National Bank of New Jersey located in Camden County, New Jersey, and served as its president from 1987 until its sale in 1998. James E. Strangfeld, the bank's executive vice president, directed various business and consumer banking operations for the southern New Jersey divisions of two large regional banks from 1986 to 2000. Many of the bank's customers, including governmental entities and local businesses, were customers of Mr. Banmiller and Mr. Strangfeld in their prior positions. It is a fundamental belief of management that having knowledge of our local markets facilitates a bank's deposit gathering capabilities and its ability to make sound credit decisions. This extensive knowledge of our local markets has allowed us to develop and implement a highly focused and disciplined approach to deposit and lending relationships with the customers in our market area.

We believe that our knowledge of the local banking market and our emphasis on service, when combined with the application of sound lending practices, will create value for our shareholders.

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THE OFFERING

| | |
|---|---|
| Common stock offered for sale.......................... | 720,000 shares |
| Shares of common stock outstanding after the offering(1).................. | 2,138,540 shares |

| | |
|---|---|
| Offering price................ | $10.00 per share |
| Market for the common stock... | The common stock is not listed on any securities exchange or on the NASDAQ National or SmallCap Markets. The common stock is traded on the OTC Bulletin Board under the symbol "FCOB" and we believe that it will continue to trade on the OTC Bulletin Board after the completion of the offering. |
| Dividend policy.............. | We have not paid cash dividends in the past, and we do not intend to pay cash dividends for the foreseeable future. We paid a 10% stock dividend in December 2001, a 5% stock dividend in April 2003, and a 5% stock dividend on April 15, 2004. We will review whether to pay additional stock dividends in the future. |
| Use of proceeds.............. | We will contribute most of the proceeds to the bank to enable it to continue to grow its loan portfolio and deposits while complying with its regulatory capital requirements. The bank may use a portion of these proceeds to finance the establishment of additional branches if we find locations that we believe will be successful and will provide growth opportunities for the bank. |
| Purchases by directors and officers..................... | Certain officers and directors have indicated an intent to participate in the offering through the purchase of approximately 62,600 total shares of common stock. See "Underwriting." |
| Risk factors................. | An investment in 1st Colonial and the common stock involves certain risks. Prospective purchasers of the common stock should consider the information discussed under the heading "Risk Factors." |

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(1) Does not include or reflect the following:

- up to 108,000 shares that may be purchased by the underwriter from us to cover over-allotments;

- 127,638 shares of common stock issuable upon the exercise of outstanding stock options;

- 369,752 shares of common stock issuable upon the exercise of outstanding warrants; and

- an aggregate of 75,075 shares of common stock reserved for future issuance upon the exercise of additional stock options that may be granted under our stock option plans.



SUMMARY FINANCIAL AND OTHER DATA

The summary financial data presented below is derived from, and should be read in conjunction with, our audited financial statements for the years ended December 31, 2003, 2002 and 2001, including the related notes, included in this prospectus beginning on page F-1. The selected financial data for the periods ended December 31, 2003, 2002, 2001 and 2000 were derived from our audited consolidated financial statements for the respective periods. Effective June 30, 2002, the bank became a wholly owned subsidiary of 1st Colonial which has no material operations other than ownership of the bank. Therefore, the financial statements of 1st Colonial prior to June 30, 2002 are the historical statements of the bank. All per share data has been restated for the effect of the 10% stock dividend paid on January 15, 2002 to shareholders of record as of January 2, 2002, the 5% stock dividend paid on April 15, 2003 to shareholders of record as of April 1, 2003 and the 5% stock dividend paid on April 15, 2004 to shareholders of record as of April 1, 2004.

SUMMARY OF OPERATIONS

| | FOR THE YEARS ENDED DECEMBER 31, 2003 | 2002 | 2001 | FOR THE PERIOD FROM JUNE 30, 2000 (INCEPTION) TO DECEMBER 31, 2000 |
|---|---|---|---|---|
| | (DOLLARS IN THOUSANDS) | | | |
| Interest income | $4,764 | $4,085 | $3,188 | $ 757 |
| Interest expense | 1,244 | 1,165 | 1,264 | 262 |
| Net interest income | 3,520 | 2,920 | 1,924 | 495 |
| Provision for loan losses | 225 | 275 | 225 | 110 |
| Net interest income after provision for loan losses | 3,295 | 2,645 | 1,699 | 385 |
| Other income | 299 | 202 | 169 | 13 |
| Other expense | 2,759 | 2,023 | 1,601 | 995 |
| Income (loss) before income taxes | 835 | 824 | 267 | (597) |
| Income tax expense (benefit) | 335 | 329 | (94) | -- |
| Net income (loss) | $ 500 | $ 495 | $ 361 | $(597) |

PER SHARE DATA

| | FOR THE YEARS ENDED DECEMBER 31, 2003 | 2002 | 2001 | FOR THE PERIOD FROM JUNE 30, 2000 (INCEPTION) TO DECEMBER 31, 2000 |
|---|---|---|---|---|
| Net income (loss) | | | | |

| | | | | |
|---|---|---|---|---|
| Basic | $ 0.35 | $ 0.44 | $ 0.35 | $ (0.61) |
| Diluted | 0.35 | 0.43 | 0.35 | $ (0.61) |
| Book value | $ 6.75 | $ 6.52 | $ 5.99 | $ 5.39 |
| Actual period end shares outstanding | 1,414,487 | 1,410,770 | 1,129,607 | 984,086 |

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BALANCE SHEET DATA

| | AT DECEMBER 31, | | | |
|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 |
| | (DOLLARS IN THOUSANDS) | | | |
| Total Assets | $118,072 | $98,320 | $79,773 | $30,728 |
| Investment securities(1) | 33,793 | 31,154 | 18,413 | 9,964 |
| Total loans(2) | 66,831 | 54,261 | 36,778 | 14,293 |
| Allowance for loan losses | (768) | (576) | (335) | (110) |
| Deposits | 104,323 | 82,948 | 67,265 | 23,294 |
| Shareholders' equity | $ 9,551 | $ 9,202 | $ 6,769 | $ 5,302 |

PERFORMANCE RATIOS

| | FOR THE YEARS ENDED DECEMBER 31, | | | FOR THE PERIOD FROM JUNE 30, 2000 (INCEPTION) TO DECEMBER 31, |
|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 |
| Return on average assets | 0.48% | 0.64% | 0.68% | (5.32)% |
| Return on average shareholders' equity | 5.39% | 7.16% | 6.37% | (22.34)% |
| Net interest spread(3) | 3.18% | 3.45% | 3.10% | 3.28% |
| Net interest margin(4) | 3.55% | 3.97% | 3.85% | 4.79% |
| Other income as a percentage of total revenue(5) | 7.83% | 6.47% | 8.07% | 2.56% |
| Other income as a percentage of average assets | 0.28% | 0.26% | 0.32% | 0.12% |
| Other expense to average assets | 2.62% | 2.61% | 3.03% | 8.87% |
| Efficiency ratio(6) | 72.24% | 64.80% | 76.49% | 195.87% |

ASSET QUALITY DATA

| | AT OR FOR THE YEARS ENDED DECEMBER 31 | | | AT OR FOR THE PERIOD FROM JUNE 30, 2000 (INCEPTION) TO DECEMBER 31, |
|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 |

| | | | | |
|---|---|---|---|---|
| Nonperforming loans | 0 | 0 | 0 | 0 |
| Nonperforming assets | 0 | 0 | 0 | 0 |
| Allowance for loan losses to period-end loans(2) | 1.15% | 1.06% | 0.91% | 0.77% |
| Net loan charge-offs to average total loans | 0.05% | 0.07% | 0.00% | 0.00% |

SELECTED CAPITAL RATIOS(7)

| | AT DECEMBER 31, | | | |
|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 |
| Total risk-based capital | 14.60% | 16.38% | 15.76% | 33.08% |
| Total tier 1 risk-based capital | 13.52% | 15.40% | 15.00% | 32.36% |
| Leverage ratio | 8.73% | 10.18% | 9.84% | 18.74% |
| Equity to assets ratio(8) | 8.09% | 9.36% | 8.49% | 17.25% |

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(1) Includes securities held to maturity and securities available for sale.

(2) Includes mortgage loans held for sale.

(3) Net interest spread is the difference between the average yield on interest earning assets and the average cost of interest bearing liabilities.

(4) The net interest margin is calculated by dividing net interest income by average interest earning assets.

(5) Total revenue consists of net interest income and total other income.

(6) Efficiency ratio is total other expense divided by the sum of net interest income and total other income.

(7) The ratios in this table are the capital ratios of the bank. The bank's capital ratios must meet the minimum requirements of the OCC. As long as the consolidated assets of 1st Colonial are less than $150 million, its sole business is serving as the holding company for the bank, and it has no publicly held debt, 1st Colonial is exempt from the consolidated capital requirements of the Federal Reserve Board.

(8) Equity to assets ratio is period-end total equity to period-end total assets.

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RISK FACTORS

You should review and consider carefully the following factors, together with the other information contained in this prospectus, in deciding whether you should make an investment in our common stock.

RISKS RELATED TO OUR BUSINESS

ESTABLISHING NEW BRANCHES INVOLVES START UP COSTS THAT WILL DECREASE NET INCOME IN THE SHORT TERM.

We are planning to establish up to two new breaches by the first quarter of 2006, and we may establish additional branch offices in 2006 and beyond. Growth through the establishment of new branches involves certain risks and costs that might not be incurred if we acquired an existing branch along with its associated deposits and loans. A bank must fund the majority of a branch's start up costs prior to the time the branch opens for business and attracts deposits. In our experience, it typically takes at least 12 months for a branch to contribute to a bank's profitability, and a branch may never become profitable. Moreover, in establishing new branches, we are required to enter into a market which may already be served by existing institutions and compete without the benefit of existing customer relationships. Notwithstanding our plans, we currently do not have any definitive arrangements to establish additional branches.

A LARGE PERCENTAGE OF OUR DEPOSITS ARE ATTRIBUTABLE TO A RELATIVELY SMALL NUMBER OF CUSTOMERS, AND THE LOSS OF EVEN A FEW OF THESE CUSTOMERS MAY HAVE A MATERIAL ADVERSE EFFECT ON OUR RESULTS OF OPERATIONS.

At December 31, 2003, 36.3% of our deposits were attributable to our 10 largest depositors. Although we believe that we have adequate liquidity to manage the loss of one or more of these customers, we would need to raise deposit rates to attract new deposits, sell investment securities, purchase federal funds, or borrow funds on a short term basis to replace such deposits. All of these actions would decrease our net interest income and our net income.

OUR LOAN PORTFOLIO IS UNSEASONED.

All of our loans have been originated since we commenced operations in June 2000. Although we believe we have underwriting standards to manage normal lending risks, it is difficult to assess the future performance of our loan portfolio due to the recent origination of most of our loans. Although as of December 31, 2003, we did not have any non-performing loans, we can give you no assurance that this absence of non-performing loans will continue or that future non-performing or delinquent loans will not adversely affect our future performance.

WE MAY NOT BE ABLE TO CONTINUE TO GROW.

We have experienced significant growth, and our future business strategy is to continue to expand. Our ability to continue to grow depends, in part, upon our ability to expand our market share, successfully attract core deposits, and identify loan and investment opportunities as well as opportunities to generate fee-based income. Our ability to manage growth successfully will also depend on whether we can continue to efficiently fund asset growth and maintain asset quality and cost controls, as well as on factors beyond our control, such as economic conditions and interest rate trends. The growth of our loans and deposits has been the principal factor in our increase in net interest income. In the event that we are unable to execute our business strategy of continued growth, our earnings could be adversely impacted.

WE MAY HAVE DIFFICULTY MANAGING OUR GROWTH.

We expect to continue to experience significant growth in the number of our employees and customers and the scope of our operations. This growth may place a significant strain on our management and operations. Our ability to manage this growth will depend upon our ability to continue to attract, hire and retain skilled employees. Our success will also depend on the ability of our officers and key employees to continue to implement and improve our operational and other systems, to manage multiple, concurrent customer relationships and to hire, train and manage our employees.



WE DEPEND ON OUR EXECUTIVE OFFICERS AND KEY PERSONNEL TO IMPLEMENT OUR BUSINESS STRATEGY AND COULD BE HARMED BY THE LOSS OF THEIR SERVICES.

We believe that our growth and future success will depend in large part upon the skills of our management team, Gerard M. Banmiller, the President and Chief Executive Officer, James E. Strangfeld, the Executive Vice President and Senior Loan Officer, and Robert Faix, the Chief Financial Officer. The competition for qualified personnel in the financial services industry is intense, and the loss of our key personnel or an inability to continue to attract, retain and motivate key personnel could adversely affect our business. We cannot assure you that we will be able to retain our existing key personnel or to attract additional qualified personnel. Although we have obtained key man life insurance on our president and chief executive officer and have employment agreements with all of our executive officers which contain noncompete provisions, the loss of the services of one or more of our executive officers could impair our ability to continue to develop our business strategy.

OUR FUTURE SUCCESS WILL DEPEND, IN PART, ON OUR ABILITY TO ADAPT TO TECHNOLOGICAL CHANGES AND USE TECHNOLOGY TO PROVIDE PRODUCTS AND SERVICES THAT ARE DESIRED BY CUSTOMERS.

Many of the bank's competitors have substantially greater resources to invest in technological improvements and have more experience in managing technological change. Adoption of rapid technological changes by the banking industry or the bank's customers could put the bank at a competitive disadvantage if we do not have the capital or personnel necessary to implement such changes.

We anticipate that we will begin to offer Internet banking services to our customers commencing in the third quarter of 2004. We will incur significant expense in doing so, and customer acceptance of these services is uncertain. Therefore, our total other expenses will increase and there may not be a corresponding increase in revenue. Further, if our Internet banking system does not function in the manner we expect, we could incur claims and liabilities related to customer privacy and security issues, account errors and other malfunctions, in addition to a resulting loss of business.

SETTLEMENT AGREEMENT MAY LIMIT OUR ABILITY TO BRANCH AND MAY DISSUADE OTHERS FROM MAKING AN OFFER TO ACQUIRE US IN THE FUTURE.

In February 2000, Colonial Bank, a federal mutual savings bank located in Gloucester County, New Jersey, filed an action in the Superior Court of New Jersey, Chancery Division, Gloucester County against us alleging that our use of the name "1st Colonial National Bank" constituted a violation of Colonial Bank's rights to its name, unfair competition, a violation of New Jersey trademark law and tortious interference with its business. In October 2001, this litigation was settled by written agreement between us and Colonial Bank.

Under terms of the settlement agreement, Colonial Bank released us from all claims relating to this matter, and the litigation was dismissed with prejudice. In exchange, we agreed that, with the exception of any branch we open in the Borough of Westville, New Jersey, we would not open a branch in any other part of Gloucester County, New Jersey under a name that included the word "Colonial." The agreement does not prohibit us from opening a branch in any other area of Gloucester County, as long as the name of that branch does not include the word

"Colonial." In addition, we are not precluded from conducting business in any other area of Gloucester County under the name "1st Colonial National Bank," as long as we do not do so from a branch in that area that is operated under a name that includes the word "Colonial."

Although federal banking regulations permit the bank, under certain conditions, to operate a branch under a name other than "1st Colonial National Bank," the regulatory requirements relating to operations, signage, and documentation, in addition to the lack of name recognition by customers and the increased marketing costs related to such a branch may cause us to refrain from branching into areas of Gloucester County, other than Westville. This may impact our growth, as Gloucester County is one of the fastest growing counties in New Jersey.

The settlement agreement also provides that, in the event we enter into a transaction pursuant to which we are acquired by another organization, we will require, as a material term of such acquisition, that the



name "1st Colonial National Bank" not be utilized by the successor organization. This provision may cause prospective acquirers to refrain from pursuing an acquisition of us that you may deem to be in your best interest as a shareholder. In a sale situation, this provision could limit the number of bidders for us, which could adversely affect the price offered. It could also cause bidders to offer less because the prospective acquirer would be unable to use the goodwill generated by our name.

## RISKS RELATED TO THE OFFERING

### THERE IS A LIMITED TRADING MARKET FOR OUR COMMON STOCK.

Our common stock trades from time to time on the OTC Bulletin Board and we believe that it will continue to do so after the completion of the offering. However, whether or not a stock trades on the OTC Bulletin Board is within the sole discretion of the market makers for the stock, and we cannot assure that the common stock will continue to trade on the OTC Bulletin Board. Further, the OTC Bulletin Board does not provide a liquid market for trading, and it may be more difficult for shareholders to sell large blocks of the common stock. There is no assurance that you will be able to resell your common stock for an aggregate amount per share that is equal to or more than the price in the offering should you need to liquidate your investment. Before purchasing, you should consider the limited trading market for the shares and be financially prepared and able to hold your shares for an indefinite period. See "Market for Our Common Stock" on page 13.

### WE DO NOT INTEND TO PAY CASH DIVIDENDS ON THE COMMON STOCK FOR THE FORESEEABLE FUTURE.

We intend to retain all earnings within 1st Colonial and the bank to provide capital for future growth. Accordingly, we do not intend to pay cash dividends on the common stock in the foreseeable future. Moreover, we are a legal entity separate and distinct from the bank. We have no material assets other than our ownership of the bank. 1st Colonial's earnings are wholly dependent on the earnings of the bank, as we have no significant operations of our own. Accordingly, 1st Colonial's earnings and our ability to pay dividends are dependent on our receipt of the earnings of the bank in the form of dividends. Any restriction on the ability of the bank to pay dividends would significantly and adversely affect our ability to pay dividends on our common stock.

The bank's ability to pay dividends or make other capital distributions to us is governed by regulations imposed by the FDIC and the OCC, the bank's primary regulators. See "Supervision and Regulation."

IN THE FUTURE, WE MAY NEED TO ISSUE ADDITIONAL SHARES OF COMMON STOCK OR SECURITIES CONVERTIBLE INTO COMMON STOCK TO RAISE ADDITIONAL CAPITAL. IF WE ARE ABLE TO SELL SUCH SHARES, THEY MAY BE ISSUED AT A PRICE THAT DILUTES THE BOOK VALUE OF SHARES OUTSTANDING AT THAT TIME.

Although this offering will increase the book value per share of our outstanding common stock, future offerings may be at a price that dilutes the book value of shares outstanding at that time. Any need to raise additional capital would most likely be caused by our regulatory capital requirements. Our future capital requirements will depend on many factors including:

- the growth in the bank's interest-earning assets;

- loan quality;

- the cost of deposits and any necessary borrowings; and

- the costs associated with our growth, such as increased salaries and employee benefits expense and office and occupancy costs.

If these or other factors cause the bank's capital levels to fall below the minimum regulatory requirements, or if the bank's existing sources of cash from operations are insufficient to fund its activities or future growth plans, we may need to raise additional capital. If such needs arises and we are unable to raise capital, we may not be able to our continue our growth strategy and management will be required to reorient its long term strategy for 1st Colonial. There can be no assurance that we will be able to generate or attract



additional capital in the future on favorable terms. In addition, future issuances of stock may cause dilution in our earnings per share and will dilute your ownership interest.

OUR STOCK IS THINLY TRADED, AND FUTURE SALES BY OUR CURRENT SHAREHOLDERS MAY ADVERSELY AFFECT OUR STOCK PRICE.

As of April 1, 2004, there were warrants outstanding to purchase 369,752 shares of our common stock, including warrants to purchase the 97,024 shares registered with the Securities and Exchange Commission concurrently with the shares covered by this prospectus. In addition, stock options to purchase 127,638 shares were outstanding. The sale of the common stock issued upon the exercise of these warrants and stock options, as well as future sales of common stock by us or by existing shareholders, or the perception that sales could occur, could adversely affect the market price of our common stock.

MANAGEMENT HAS DISCRETIONARY USE OF THE PROCEEDS OF THIS OFFERING.

Management will have broad discretion with respect to the expenditures of the net proceeds of this offering and, accordingly, there is no assurance that you will agree with the uses that we choose to make of these funds. See "Use of Proceeds."

PROVISIONS UNDER PENNSYLVANIA LAW, IN OUR CHARTER DOCUMENTS AND OTHER LAWS AND REGULATIONS APPLICABLE TO US MAY MAKE IT HARDER FOR OTHERS TO OBTAIN CONTROL OF 1ST COLONIAL EVEN THOUGH SOME SHAREHOLDERS MIGHT CONSIDER SUCH A DEVELOPMENT FAVORABLE.

Provisions of our articles of incorporation and applicable provisions of Pennsylvania law and federal law may delay, inhibit or prevent someone from gaining control of 1st Colonial through a tender offer, business combination, proxy contest or some other method even though some of our shareholders might believe a change in control is desirable. See "Description of Our Securities" on page 60.

Our articles of incorporation and bylaws contain provisions that may discourage a change in control of 1st Colonial. These provisions include:

- the prohibition of ownership and voting of shares having in excess of 10% of the total voting power of the outstanding stock of 1st Colonial;

- a classified board of directors divided into three classes serving for successive terms of three years each;

- the prohibition of cumulative voting in the election of directors;

- the requirement that nominations for the election of directors made by shareholders and any shareholder proposals for the agenda at any annual meeting generally must be made by notice (in writing) delivered or mailed to us not less than 90 days prior to the meeting;

- the requirement that any merger, consolidation, sale of assets or similar transaction involving 1st Colonial requires the affirmative vote of shareholders entitled to cast at least 80% of the votes which all shareholders are entitled to cast, unless the transaction is approved in advance by 66 2/3% of the members of the board of directors;

- the requirement that a person must be a shareholder of 1st Colonial or the bank for at least three years before he or she can be elected to the board of directors;

- the requirement that any person or entity that acquires shares of our stock having a combined voting power of 25% or more of the total voting power of our outstanding capital stock, must offer to purchase, for cash, all outstanding shares of our voting stock at a price equal to the highest price paid for that stock within the preceding twelve months by that person or entity;

- the prohibition of shareholder action without a meeting and the prohibition of shareholders being able to call a special meeting;



- the provision that certain provisions of our articles of incorporation can only be amended by an affirmative vote of shareholders entitled to cast at least 80% of all votes which shareholders are entitled to cast, unless approved by an affirmative vote of at least 80% of the members of our board of directors; and

- the provision that certain sections of our bylaws can only be amended by an affirmative vote of shareholders entitled to cast at least 66 2/3% or 80% of all votes that shareholders are entitled to cast, unless approved by affirmative vote of at least 80% of the members of our board of directors.

These provisions may serve to entrench management and may discourage a takeover attempt that you may consider to be in your best interest or in which you would receive a substantial premium over the current market price. These provisions may make it extremely difficult for any one person or group of affiliated persons to acquire voting control of 1st Colonial, with the result that it may be extremely difficult to bring about a change in the board of directors or management. Some of these provisions also may tend to perpetuate present management because of the additional time required to cause a change in the control of the board. Other provisions render it difficult for shareholders owning less than a majority of the voting stock to be able to elect even a single director. See "Description of Our Securities -- Certain Restrictions on Acquisition of 1st Colonial" on page 62.

## RISKS RELATED TO THE BANKING INDUSTRY

### WE FACE SUBSTANTIAL COMPETITION FOR CUSTOMERS, AND MANY OF OUR COMPETITORS HAVE MUCH GREATER RESOURCES IN TERMS OF CAPITAL AND PRODUCTS.

The banking business in southern New Jersey is extremely competitive. The region has experienced a large number of bank mergers and acquisitions in the last several years and the resulting institutions have significant resources. The bank currently operates from only two branches and competes for customers with New Jersey-based and out-of-state financial institutions that have longer operating histories, more capital, extensive branch and automated teller machine networks and established customer bases. In addition, the bank's market area may be served in the future by new, locally-based institutions. The bank's competition also includes Internet-based banks, securities firms, insurance companies, credit unions, mortgage companies, mutual funds and other entities, in addition to traditional banking institutions such as savings and loan associations, savings banks, and commercial banks. Most of the bank's competitors are larger than the bank and, accordingly, have higher lending limits and resources. Banks compete for customers based on the convenience of customer access, interest rates paid on deposits and charged on loans, the level of bank fees and other factors. As a bank with only two branches, we are at a competitive disadvantage to many of our competitors that have more than two branches. The bank is not currently able to offer certain products and services that its competitors provide, such as trust and certain investment and insurance products and services, and may not be able to develop those services in the future.

### IF WE EXPERIENCE GREATER LOAN LOSSES THAN ANTICIPATED, IT WILL HAVE AN ADVERSE EFFECT ON OUR NET INCOME AND OUR ABILITY TO FUND OUR GROWTH STRATEGY.

The risk of nonpayment of loans is inherent in banking. If we experience greater nonpayment levels than anticipated, our earnings and overall financial condition, as well as the value of our common stock, could be adversely affected.

We cannot assure you that our monitoring, procedures and policies will reduce certain lending risks or that our allowance for loan losses will be adequate to cover actual losses. Loan losses can cause insolvency and failure of a financial institution and, in such an event, our shareholders could lose their entire investment. In addition, future provisions for loan losses could materially and adversely affect our results of operations. Any loan losses will reduce the loan loss reserve. A reduction in the loan loss reserve will be restored by an increase in our provision for loan losses. This will cause our earnings to be reduced and reduced earnings could have an adverse effect on our stock price.



### OUR NET INCOME IS DIRECTLY AFFECTED BY CHANGES IN MONETARY POLICY AND INTEREST RATES OVER WHICH WE HAVE NO CONTROL.

Our operating results may be significantly affected (favorably or unfavorably) by market rates of interest which, in turn, are affected by prevailing economic conditions, by the fiscal and monetary policies of the United States Government and by the policies of various regulatory agencies. Our earnings depend primarily upon the difference between income earned on our loans and investments and the interest paid on our deposits and borrowings. Like many financial institutions, we may be subject to the risk of fluctuations in interest rates, which, if significant, may have a material adverse effect on our net income. See "Supervision and Regulation" commencing on page 44.

THE LAWS AND REGULATIONS GOVERNING OUR BUSINESS ARE SUBJECT TO CHANGE AT ANY TIME.

The Federal and state laws and regulations applicable to us give regulatory authorities extensive discretion in connection with their supervisory and enforcement responsibilities, and generally have been promulgated to protect depositors and the deposit insurance funds and not for the purpose of protecting shareholders. These laws and regulations can materially affect our future business. Laws and regulations may be changed at any time, and the interpretation of such laws and regulations by bank regulatory authorities is also subject to change. We can give no assurance that future changes in laws and regulations or changes in their interpretation will not adversely affect our business. See "Supervision and Regulation" commencing on page 44.

RECENT LEGISLATION TO ADDRESS CORPORATE ACCOUNTING IRREGULARITIES COULD CAUSE US TO INCUR SIGNIFICANT EXPENSE.

In response to highly publicized accounting restatements and alleged improprieties by some corporate officers of certain large publicly-held companies, in July 2002, President Bush signed into law the Sarbanes-Oxley Act of 2002. Additional regulations have been promulgated by the Securities and Exchange Commission (SEC) and were effective beginning August 29, 2002. Under this law and the regulations adopted by the SEC to implement various provisions of the law, publicly-traded companies are subject to significant additional and accelerated reporting regulations and disclosure. These regulations also impose significant new responsibilities on officers, auditors, boards of directors and in particular, audit committees. Compliance with the new laws and regulations has begun to increase our expenses; this could have a material adverse effect on our financial results in the future. See "Supervision and Regulation -- Sarbanes-Oxley Act" on page 45.



USE OF PROCEEDS

The net proceeds from the sale of the common stock in the offering are estimated to be approximately $6.3 million, after deducting offering expenses and assuming that the underwriter does not purchase any additional shares from us to cover over-allotments. We intend to contribute $5.5 million, or 87.3%, of these net proceeds to the bank to fund its ongoing expansion. 1st Colonial will retain the remainder of the proceeds for general corporate purposes.

The ability of any bank to accept deposits and otherwise increase its asset size is limited by regulatory requirements mandating that the bank maintain certain minimum amounts and types of capital when compared to the amounts and types of its assets. The bank will use a portion of the proceeds to enable it to increase its legal lending limit and to provide the capital necessary, in light of such regulatory requirements, to support the bank's growth. A portion of the proceeds also may be used to fund the establishment or acquisition of additional branches, if we find locations that we believe will be successful and will provide growth opportunities for the bank. Although we desire to open two additional branches by the first quarter of 2006, we currently have no definitive plans or arrangements to establish or acquire any branches.

## MARKET FOR OUR COMMON STOCK

Our common stock is traded on the OTC Bulletin Board under the symbol FCOB and we believe that it will continue to be traded on the OTC Bulletin Board after the completion of the offering. An active trading market does not currently exist for our common stock. As of April 20, 2004, the bid price for the common stock was $10.25, and the asked price was $11.25. The following table sets forth the high and low last sale information, as reported by the OTC Bulletin Board, as of the most recent practicable date and for the periods indicated.

### SALE PRICE INFORMATION FOR COMMON STOCK

| | SALE PRICE(1) | |
|---|---|---|
| | HIGH | LOW |
| | 2002 | |
| First Quarter | $ 9.30 | $ 8.39 |
| Second Quarter | 8.85 | 8.16 |
| Third Quarter | 8.62 | 6.57 |
| Fourth Quarter | 8.17 | 6.14 |
| | 2003 | |
| First Quarter | $ 9.34 | $ 7.49 |
| Second Quarter | 10.48 | 8.30 |
| Third Quarter | 10.48 | 9.52 |
| Fourth Quarter | 10.57 | 9.57 |
| | 2004 | |
| First Quarter | $10.71 | $ 9.80 |
| Second Quarter (Through 4/20/04) | 10.25 | 10.25 |

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(1) Prices are adjusted to reflect the 5% stock dividend paid by 1st Colonial on April 15, 2003 to shareholders of record as of April 1, 2003 and the 5% stock dividend paid by 1st Colonial on April 15, 2004 to shareholders of record as of April 1, 2004.

As of April 1, 2004, there were options outstanding to purchase 127,638 shares of common stock and warrants outstanding to purchase 369,752 shares of common stock. These amounts reflect the 5% stock dividend paid on April 15, 2004 to shareholders of record as of April 1, 2004.

As of April 1, 2004, there were 296 holders of record of our common stock.



Ryan Beck & Co.; Midwest Research Securities Corp., a subsidiary of First

Tennessee National Bank; and Janney Montgomery Scott, LLC make a market in our common stock. Ryan Beck has advised us that it intends to make a market in the common stock following the completion of the offering and to encourage other securities firms to do so, but it has no obligation to do so. Making a market involves maintaining bid and ask quotations and being able, as principal, to effect transactions in reasonable quantities at those prices, subject to securities laws and regulatory constraints. Additionally, the development of a liquid public market depends on the existence of willing buyers and sellers, the presence of which is not within our control. An active and liquid market may not develop for the common stock.

StockTrans, Inc. serves as transfer agent and registrar for our common stock.

## DIVIDEND POLICY

Since our inception in June 2000, we have not paid a cash dividend, and we do not intend to pay cash dividends for the foreseeable future. We desire to retain our net income to support the growth of the bank. Any payment of cash dividends to our shareholders would be dependent on the payment of a cash dividend from the bank to us. The payment of cash dividends by the bank to us is limited under federal banking law. See "Supervision and Regulation -- Limits on Dividends" and "Description of Capital Stock -- Common Stock -- Dividends."

On January 15, 2002, we effected a 10% stock split in the form of a stock dividend to shareholders of record on January 2, 2002. On April 15, 2003, we paid a 5% stock dividend to shareholders of record on April 1, 2003. On April 15, 2004, we paid a 5% stock dividend to shareholders of record on April 1, 2004. We will continually review whether to pay additional stock dividends in the future.



## CAPITALIZATION

The following table sets forth our capitalization as of December 31, 2003, and as adjusted to give effect to this offering. As adjusted numbers assume net proceeds of approximately $6.3 million from the sale of the common stock offered by this prospectus (not including the over allotment option), after deducting estimated offering expenses.

| | AT DECEMBER 31, 2003 | |
| --- | --- | --- |
| | ACTUAL | AS ADJUSTED |
| | (DOLLARS IN THOUSANDS) | |
| Shareholders' equity:(1) | | |
| Common stock, no par value 5,000,000 shares authorized, 1,414,487 shares issued and 2,134,487 shares issued as adjusted | $ -- | $ -- |
| Preferred stock, 1,000,000 shares authorized; no shares issued | -- | -- |
| Additional paid in capital | 9,238 | 15,579 |
| Retained earnings | 386 | 386 |
| Accumulated other comprehensive (loss) income | (73) | (73) |

| | | |
|---|---|---|
| Total shareholders' equity | $9,551 | $15,892 |
| Book value per share | $ 6.75 | $ 7.45 |

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(1) Does not include a total of 453,419 shares of common stock reserved for issuance under options and warrants to purchase common stock outstanding at December 31, 2003. Does include the shares issuable pursuant to the 5% stock dividend paid on April 15, 2004 to shareholders of record as of April 1, 2004.

The bank is subject to minimum capital requirements of the OCC, our primary regulator. See "Supervision and Regulation -- Capital Requirements." The tables below reflect the capital ratios of the bank at December 31, 2003, and as adjusted to give effect to the proceeds of the offering and the contribution of a portion of the proceeds to the bank. The ratios in this table are the capital ratios of the bank. As long as 1st Colonial's consolidated assets are less than $150 million, its sole business is serving as the holding company for the bank, and it has no publicly held debt, 1st Colonial is exempt from the consolidated capital requirements of the Federal Reserve Board.

| | AT DECEMBER 31, 2003 | | |
|---|---|---|---|
| | ACTUAL | AS ADJUSTED | REGULATORY MINIMUM TO BE WELL CAPITALIZED |
| Risk based capital: | | | |
| Total Capital | 14.60% | 21.63% | 8.00% |
| Tier 1 capital | 13.52% | 20.63% | 8.00% |
| Leverage ratio | 8.73% | 13.72% | 4.00% |

## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements. You can find many of these statements before and after words such as "may," "could," "should," "will," "would," "believe," "expect," "anticipate," "estimate," "project," "intend," "plan," "seek," "assume" or similar expressions.

These forward-looking statements, implicitly and explicitly, include the assumptions underlying the statements and other information with respect to our beliefs, plans, objectives, goals, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance and business, including our

- plans for the use of the proceeds of this offering;

- expectations for continued acceptance and success in the banking and business communities in our market area;

- expectations as to the amount, mix, yield and other characteristics of the deposits and loans we expect to acquire and make; and

- expectations and estimates with respect to our revenues, expenses, earnings, return on equity, return on assets, efficiency ratio, asset quality and other financial data and capital and performance ratios.

Although we believe that the expectations reflected in our forward-looking statements are reasonable, these statements involve risks and uncertainties that are subject to change based on various important factors (some of which are beyond our control). The following factors, among others, could cause our financial performance to differ materially from our goals, plans, objectives, intentions, expectations, and other forward-looking statements:

- the strength of the United States economy in general and the strength of the regional and local economies in which we conduct operations;

- the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System;

- inflation, interest rate, market and monetary fluctuations;

- our ability to raise the capital necessary on a timely basis to support our continued asset growth and geographic expansion;

- our ability to maintain and continue to obtain the desired customers and employees;

- our timely development of new products and services in a changing environment, including the features, pricing and quality compared to the products and services of our competitors;

- the willingness of prospective customers to substitute our products and services for the bank products and services they currently use, and the impact of competition from banks, thrifts and others in our market;

- changes in the timing and structure of our growth and related transactions and other changed facts and circumstances resulting from the passage of time;

- the impact of changes in financial services policies, laws and regulations, including laws, regulations and policies concerning taxes, banking, securities and insurance, and the application thereof by regulatory bodies;

- technological changes;

- change in consumer spending and savings habits;

- regulatory or judicial proceedings; and

- the other risks set forth under "Risk Factors" beginning on page 7.

If one or more of the factors affecting our forward-looking information and statements proves incorrect, then our actual results, performance or achievements could differ materially from those expressed in, or implied by, forward-looking information and statements contained in this prospectus. Therefore, we caution you not to place undue reliance on our forward-looking information and statements.

We do not intend to update our forward-looking information and statements, whether written or oral, to reflect change. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.



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

The following presents management's discussion and analysis of our financial condition and results of operations and should be read in conjunction with the financial statements and related notes included elsewhere in this prospectus beginning on page F-1. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ significantly from those anticipated in these forward-looking statements as a result of various factors, including those discussed in "Risk Factors" beginning on page 7 and "Special Note Regarding Forward-Looking Statements" beginning on page 15 in this prospectus.

### OVERVIEW

Effective June 30, 2002, the bank became a wholly owned subsidiary of 1st Colonial, which has no material operations other than ownership of the bank. Therefore, the financial statements of 1st Colonial prior to June 30, 2002 are the historical statements of the bank. All per share data has been restated for the effect of the 10% stock dividend paid on January 15, 2002 to shareholders of record as of January 2, 2002, the 5% stock dividend paid on April 15, 2003 to shareholders of record as of April 1, 2003 and the 5% stock dividend paid on April 15, 2004 to shareholders of record as of April 1, 2004.

The bank conducts community banking activities by accepting deposits from the public and investing the proceeds in loans and investment securities. The bank's lending products include commercial loans and lines of credit, consumer and home equity loans, and multi-family residential and non-residential real estate loans. In order to manage its liquidity and interest rate risk, the bank maintains an investment portfolio consisting of municipal, U.S. government and mortgage-backed securities, most of which are investment grade. The bank's loan and investment portfolios are funded with deposits as well as collateralized borrowings secured by the bank's investment securities.

Our earnings are largely dependent upon net interest income (the difference between what we earn on our loans and investments and what we pay on deposits and borrowings). In addition to net interest income, our net income is impacted by our loan loss provision, other income (mostly deposit fees and income from sale of loans held for sale) and other expense (such as salaries and benefits, professional fees, occupancy cost and data processing expenses).

### CRITICAL ACCOUNTING MATTERS

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses and the valuation of the deferred tax assets.

The allowance for loan losses is established through a provision for loan losses charged to operations. The allowance is maintained at a level that management believes will be adequate to absorb estimated losses on existing loans based on the collectibility of the loans and prior loss experience. Management uses significant estimates to determine the allowance for loan losses. Management's evaluations consider such factors as changes in the nature and volume of the portfolio, overall portfolio quality, concentrations of credit risk, review of specific problem loans, current economic conditions and trends that may affect the borrowers' ability to pay, and prior loss experience within various categories of the portfolio. Loans are charged against the allowance when they are determined to be uncollectible.

In addition, regulatory authorities, as an integral part of their examinations, periodically review the allowance for loan losses. They may require additions to the allowance based upon their judgments about information available to them at the time of examination.



Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established against deferred tax assets when, in the judgment of management, it is more likely that not that such deferred tax assets will not become available.

The realizability of deferred tax assets is dependent upon various factors, including the generation of future taxable income, the existence of taxes paid and recoverable, the reversal of deferred tax liabilities, and tax planning strategies. Based upon these and other factors, management determined during 2001 that it is more likely than not that the bank will realize the benefits of these deferred tax assets and, as a result, removed the previously established valuation allowance.

## COMPARISON OF FINANCIAL CONDITION

### YEAR ENDED DECEMBER 31, 2003 VERSUS YEAR ENDED DECEMBER 31, 2002

Our assets totaled $118.1 million at December 31, 2003, as compared to $98.3 million at December 31, 2002, an increase of $19.8 million or 20.1%. Our assets at December 31, 2003, consisted primarily of cash and cash equivalents, including federal funds sold, which totaled $16.5 million, investment securities, which totaled $33.8 million and loans, including loans held for sale, which totaled $66.8 million. Premises and equipment totaled $935,000 at December 31, 2003, and consisted primarily of our Westville branch and leasehold improvements. Our assets at December 31, 2002 consisted primarily of cash and cash equivalents, including federal funds sold of $12.2 million, investment securities of $31.2 million, and loans of $54.3 million. The $19.8 million increase in total assets was primarily due to an increase in loans of $12.4 million, an increase in investment securities of $2.6 million, and an increase in short-term investments, such as Federal Funds sold and interest bearing deposits of $4.2 million. This increase in assets was funded by an increase in deposits of $21.4 million, as partially offset by a decrease in short-term borrowings of $1.9 million. The increase in loans was due to general growth in our loan portfolio resulting from the continued execution of our business plan.

Our deposits totaled $104.3 million at December 31, 2003, as compared to $82.9 million at December 31, 2002, an increase of $21.4 million or 25.8%. This increase was the direct result of the establishment of new business relationships with municipalities and other commercial accounts and the opening of our branch office in Westville, New Jersey on January 16, 2003. The Westville branch location was purchased in August 2002, renovated and equipped at a total cost of $480,000 at December 31, 2003.

Non-interest bearing demand deposits totaled $20.4 million and interest-bearing demand deposits totaled $37.3 million at December 31, 2003, increases of 22.6% and 25.5% as compared to balances of $16.6 million and $29.7 million, respectively, at December 31, 2002. This increase in demand deposits was the result of the new Westville office and new relationships established with municipal entities and commercial accounts. Savings and money market deposits totaled $20.4 million and certificates of deposit totaled $26.2 million at December 31, 2003, increases of 3.6% and 55.2%, respectively, as compared to balances of $19.7 and $16.9 million, respectively, at December 31, 2002.

NET INTEREST INCOME

The principal source of our revenue is net interest income. Net interest income is the difference between income earned on loans and securities and the interest paid on deposits and borrowed funds. Interest-earning assets are comprised primarily of loans and securities, while deposits represent the major portion of interest bearing liabilities. Changes in the volume and mix of interest-earning assets and interest-bearing liabilities, as well as their respective yields and rates, have a significant impact on the level of net interest income. Net interest margin is calculated as net interest income divided by average earning assets and represents our net yield on our earning assets.



Interest on loans is included in interest income on the accrual method over the terms of the loans based upon the principal balances outstanding. During the fiscal years ended December 31, 2003, 2002 and 2001, average interest-earning assets were $99.9 million, $73.7 million and $50.2 million, respectively. During these same periods, our net yields on average interest-earning assets (net interest margin) were 3.55%, 3.97%, and 3.85%, respectively.

AVERAGE BALANCE, INTEREST INCOME AND EXPENSE, AVERAGE YIELD AND RATES

The following table illustrates the average balances of total interest-earning assets and total interest-bearing liabilities for the periods indicated, showing the average distribution of assets, liabilities, shareholders' equity, and the related income, expense, and corresponding weighted average yields and costs. The average balances used for the purposes of these tables and other statistical disclosures were calculated by using the daily average balances. Non-accruing loans, if any, are included in the average balances of loans.



| | YEAR ENDED DECEMBER 31, 2003 | | | YEAR ENDED DECEMBER 31, 2002 | | |
|---|---|---|---|---|---|---|
| | AVERAGE BALANCE | INTEREST INCOME/ EXPENSE | AVERAGE YIELD/ RATE | AVERAGE BALANCE | INTEREST INCOME/ EXPENSE | AVERAGE YIELD/ RATE |

(DOLLARS IN THOUSANDS)

| | | | | | | |
|---|---|---|---|---|---|---|
| ASSETS | | | | | | |
| Interest earning assets: | | | | | | |
| Federal funds sold.............. | $ 6,953 | $ 78 | 1.12% | $11,006 | $ 176 | 1.60% |
| Investment Securities: | | | | | | |
| Taxable(1)...................... | 28,945 | 870 | 3.01% | 14,683 | 647 | 4.41% |
| Tax-exempt(2)................... | 3,826 | 71 | 1.86% | 604 | 17 | 2.81% |
| Total Securities.............. | 32,771 | 941 | 2.87% | 15,287 | 664 | 4.34% |
| Loans, net of deferred fees/costs(3)................... | 60,183 | 3,769 | 6.26% | 47,430 | 3,251 | 6.85% |
| Total interest earning assets... | 99,907 | 4,788 | 4.79% | 73,723 | 4,091 | 5.55% |
| Non-interest earning assets: | | | | | | |
| Cash and due from banks......... | 4,258 | | | 3,017 | | |
| Other assets(4)................. | 1,629 | | | 1,107 | | |
| Less: allowance for loan losses........................ | (681) | | | (472) | | |
| Total non-interest earning assets...................... | 5,206 | | | 3,652 | | |
| Total assets................ | $105,113 | | | $77,375 | | |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | | |
| Interest bearing liabilities | | | | | | |
| Deposits: | | | | | | |
| Interest bearing demand....... | $ 31,344 | $ 531 | 1.69% | $19,772 | $ 427 | 2.16% |
| Money market.................. | 15,109 | 97 | 0.64% | 12,231 | 192 | 1.57% |
| Savings....................... | 5,293 | 31 | 0.59% | 3,873 | 38 | 0.98% |
| Time deposits................. | 20,296 | 544 | 2.68% | 14,342 | 425 | 2.96% |
| Total interest bearing deposits...................... | 72,042 | 1,203 | 1.67% | 50,218 | 1,082 | 2.15% |
| Short-term borrowings......... | 5,284 | 41 | 0.78% | 5,217 | 83 | 1.59% |
| Total interest bearing liabilities.................. | 77,326 | 1,244 | 1.61% | 55,435 | 1,165 | 2.10% |
| Non-interest bearing liabilities: | | | | | | |
| Demand deposits................. | 18,320 | | | 14,786 | | |
| Other liabilities............... | 186 | | | 237 | | |
| Total non-interest bearing liabilities..................... | 18,506 | | | 15,023 | | |
| Total liabilities................ | 95,832 | | | 70,458 | | |
| Shareholders' equity............. | 9,281 | | | 6,917 | | |
| Total liabilities and shareholders' equity.......... | $105,113 | | | $77,375 | | |
| Net interest spread............... | | | 3.18% | | | 3.45% |
| Net interest income/net interest margin.......................... | | $3,544 | 3.55% | | $2,926 | 3.97% |
| Average interest earning assets as a percentage of interest bearing | | | | | | |

| | | |
|---|---|---|
| liabilities.................... | 129.20% | 132.99% |

---------------

(1) All taxable investment securities are classified as available for sale. The average balance for taxable securities excludes the SFAS 115 valuation allowance.

(2) All tax-exempt investment securities are classified as held to maturity. Interest income on tax-exempt investment securities is presented on a tax-equivalent basis. Tax exempt yields were adjusted to a tax-equivalent basis using a 34% rate.

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(3) Includes average balance of loans held for sale of $382 in 2003, $156 in 2002 and $160 in 2001. Interest income on loans held for sale was $23 in 2003, $13 in 2002 and $14 in 2001.

(4) Excludes the average balance of deferred tax assets related to the SFAS 115 valuation allowance on investment securities available for sale.

RATE/VOLUME ANALYSIS

Future net interest income will be affected by changes in both average interest rates and average volumes of interest-earning assets and interest-bearing liabilities. The following tables set forth certain information regarding changes in interest income and interest expense for the periods indicated for each category of interest-earning assets and interest-bearing liabilities. Information is provided on changes attributable to (i) changes in volume (changes in average volume multiplied by prior rate), (ii) changes in rate (changes in average rate multiplied by prior average volume), and (iii) total change. Changes due to the combination of rate and volume changes (change in average volume multiplied by change in average rate) have been allocated on a consistent basis between rate and volume variances based on the percentage of the rate or volume variance to the sum of the two absolute variances.

| | YEAR ENDED DECEMBER 31, 2003 VERSUS YEAR ENDED DECEMBER 31, 2002 | | |
|---|---|---|---|
| | INCREASE (DECREASE) DUE TO | | |
| | VOLUME | RATE | TOTAL |
| | (DOLLARS IN THOUSANDS) | | |
| Interest Income: | | | |
| Federal funds sold...................................... | $ (54) | $ (44) | $(98) |
| Investment securities -- taxable........................ | 478 | (255) | 223 |
| Investment securities -- tax exempt(1).................. | 62 | (8) | 54 |
| Loans................................................... | 817 | (299) | 518 |
| Total change in interest income...................... | $1,303 | $(606) | $697 |
| Interest Expense: | | | |
| Interest bearing checking............................... | $ 211 | $(107) | $104 |

| | | | |
|---|---|---|---|
| Money market deposits | 37 | (132) | (95) |
| Savings deposits | 11 | (18) | (7) |
| Time deposits | 163 | (44) | 119 |
| Short-term borrowings | 1 | (43) | (42) |
| Total change in interest expense | 423 | (344) | 79 |
| Total change in net interest income | $ 880 | $(262) | $618 |

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| | YEAR ENDED DECEMBER 31, 2002 VERSUS YEAR ENDED DECEMBER 31, 2001 | | |
|---|---|---|---|
| | INCREASE (DECREASE) DUE TO | | |
| | VOLUME | RATE | TOTAL |
| | (DOLLARS IN THOUSANDS) | | |
| Interest Income: | | | |
| Federal funds sold | $ (25) | $(217) | $(242) |
| Investment securities -- taxable | 96 | (259) | (163) |
| Investment securities -- tax exempt(1) | 2 | (11) | (9) |
| Loans | 1,568 | (260) | 1,308 |
| Total change in interest income | $1,641 | $(747) | $ 894 |
| Interest Expense: | | | |
| Interest bearing checking | $ 239 | $ (90) | $ 149 |
| Money market deposits | (43) | (168) | (211) |
| Savings deposits | 22 | (11) | 11 |
| Time deposits | 165 | (163) | 2 |
| Short-term borrowings | 36 | (86) | (50) |
| Total change in interest expense | 419 | (518) | (99) |
| Total change in net interest income | $1,222 | $(229) | $ 993 |

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(1) Tax-exempt yields were adjusted to a tax-equivalent basis using a 34% rate.

COMPARISON OF RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2003 VERSUS YEAR ENDED DECEMBER 31, 2002

General. Net income increased 1.0% to $500,000 for the year ended December 31, 2003, as compared to net income of $495,000 for the period ended December 31, 2002. This increase was due to a $697,000 increase in net interest and total other income, coupled with a $50,000 reduction in the provision for loan losses, which were only partially offset by a $736,000 increase in total other expense and a $6,000 increase in income tax expense.

Basic earnings per share decreased to $0.35 for the year ended December 31, 2003 (basic and diluted) from $0.44 for the year ended December 31, 2002 ($0.43 on a fully diluted basis). This decrease was due to the issuance of additional shares of common stock in our public offering of units completed in December 2002, which shares had only a marginal effect on the weighted average number of shares outstanding for 2002. In the offering, we sold 254,399 units and each unit consisted of one share of common stock and one warrant to purchase an additional share of common stock. After giving effect to the 5% stock dividend paid in April 2003 and the 5% stock dividend paid in April 2004, the total number of shares of common stock issued in the unit offering was 280,475.

Total interest income increased 16.6% to $4.8 million from $4.1 million primarily due to the growth and mix of earning assets. Total other income increased 48.0% or by $97,000 to $299,000 from $202,000, due to increased deposit fees, gains on sale of mortgage loans and other fees as partially offset by an 83.3% decline in gains on sale of investments to $4,000 from $24,000 in the previous year. Total other expenses increased 36.4% or $736,000 to $2.8 million from $2.0 million due to growth related expenses from staffing increases, new marketing initiatives, increased regulatory compliance costs and more customer volume and activity, as well as increased expenses related to the opening of our new Westville office.

Net Interest Income. Interest income increased by $679,000 to $4.8 million from $4.1 million, primarily due to a $26.2 million increase in average earning assets. Interest and fees on loans increased by $518,000 for

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the year ended December 31, 2003, due to an increase in average loans and loans available for sale outstanding of $12.8 million or 26.9% from the prior period, which more than offset the decline in the average yield on the loan portfolio. The average yield on our loan portfolio declined from 6.85% in 2002 to 6.26% in 2003 due to the declining interest rate environment. Interest on federal funds sold decreased by $98,000 due to a decrease of $4.1 million in average balances and lower yields caused by market rate declines. Interest and dividends on investments increased by $259,000 for the period due to an increase of $17.5 million in average outstanding balances. The increase was partially offset by an overall decline in the yield on investment securities caused by a decline in market interest rates. The average yield on investment securities declined to 2.87% in 2003 from 4.34% in 2002.

Total interest expense increased $79,000 from the prior period, due principally to a $21.9 million increase in average interest bearing liabilities. The increase in the average balance of deposits was ameliorated by the lower rates paid on deposit accounts and short term borrowings, as the cost of interest bearing liabilities declined from 2.10% in 2002 to 1.61% in 2003. Our net interest margin was 3.55% for the year ended December 31, 2003 as compared to 3.97% for the prior period ended December 31, 2002, as our interest earning assets repriced downward to a greater degree than our interest bearing liabilities.

Provision for Loan Losses. The provision for loan losses decreased to $225,000 for year ended December 31, 2003 compared to $275,000 for the prior period. Factors such as changes in the nature and volume of the portfolio, overall portfolio quality, concentrations of credit risk, review of specific problem loans, current economic conditions and trends that may affect the ability of borrowers to pay, and prior loss experience within the various categories of the portfolio are considered when reviewing the risks in the portfolio. The allowance for loan losses was $768,000 at December 31, 2003, or 1.15% of total outstanding loans. See "Business -- Allowance for Loan Losses"

for more information.

The bank's loan portfolio is relatively unseasoned due to the fact that we commenced operations in 2000. Therefore, our historical charge-off and non-performing loan statistics may not be indicative of future trends.

Total Other Income. Other income, primarily service charges on deposit accounts and gains on sale of mortgages held for sale, increased $97,000 to $299,000 for the year ended December 31, 2003. Fees from deposit account holders for the year ended December 31, 2003 were approximately $139,000 compared to $85,000 in the prior period. This 63.5% increase was principally due to deposit growth. For the year ended December 31, 2003, we recorded gains on the sale of residential mortgage loans held for sale of $103,000 compared to $62,000 in the prior period. This was primarily due to increased refinancing activity due to lower interest rates during the year. In general, we sell all newly originated fixed-rate residential mortgage loans into the secondary market on a servicing released basis. The increase of $22,000 to $53,000 in 2003 from $31,000 in 2002, in other fees and charges was primarily volume related. Gains on sale of investments available for sale for the year ended December 31, 2003 declined to $4,000 compared to $24,000 in the year ended December 31, 2002.

Total Other Expense. Total other expenses for the year ended December 31, 2003 increased $736,000 or 36.4% to $2.8 million compared to $2.0 million in the prior period. Most of the increases were due to growth related factors:

- Employee related expenses were $1.2 million for the year compared to $842,000 for the year ended December 31, 2002, reflecting additions to our staff as well as normal compensation increases.

- Occupancy and equipment expenses increased $117,000 to $335,000 for the year ended December 31, 2003, compared to $218,000 in the prior period. The opening of our Westville branch office in January 2003 accounted for $72,000 of these increases.

- Advertising expenses increased $70,000 to $145,000 for the year ended December 31, 2003 compared to $75,000 in the prior period. This was due to increased activity relating to our Westville opening and other marketing campaigns designed to increase community awareness of our presence, products and capabilities.



- Due to increased business volume, data processing expenses increased 23.3% to $275,000 for the year ended December 31, 2003 compared to $223,000 for the year ended December 31, 2002.

- Professional services, including audit, loan review, and legal expenses increased $27,000 to $222,000 during the year ended December 31, 2003 compared to $195,000 for the comparable prior period. This increase was primarily related to our growth.

- Other operating expenses included postage, ATM charges, telephone expenses, business development costs and other miscellaneous expenses. These expenses also included a loss of $19,000 on the replacement of equipment during the year ended December 31, 2003. Due to growth and increased activity, other operating expenses increased $137,000 or 29.2% to $607,000 for the year ended December 31, 2003, compared to $470,000 for the year ended December 31, 2002.

Income Taxes. Our recorded income tax expense for the year ended December 31, 2003 was $335,000 compared to $329,000 in the prior period. The increase in income tax expense is due to higher pre-tax income for the year ended December 31, 2003 as compared to the prior period. The effective rates for the year ended December 31, 2003 and 2002 were 40.1% and 39.9%, respectively.

YEAR ENDED DECEMBER 31, 2002 VERSUS YEAR ENDED DECEMBER 31, 2001

General. Net income increased 37.1% to $495,000 for the year ended December 31, 2002 as compared to net income of $361,000 for the period ended December 31, 2001. Basic earnings per share increased to $0.44 for the year ended December 31, 2002 ($0.43 on a diluted basis) from $0.35 (basic and diluted) for the year ended December 31, 2001. This increase in net income was due to a $1.0 million increase in net interest and other income, which was partially offset by a $423,000 increase in income tax expense, a $422,000 increase in total other expense, and a $50,000 increase in the provision for loan losses.

Total interest income increased 28.1% to $4.1 million from $3.2 million primarily due to the growth and mix of earning assets. Total other income increased 19.5% or by $33,000 due to increased deposit fees, gains on sale of residential mortgage loans and other fees, as partially offset by a 63.1% decline in gains on sale of investments to $24,000 from $65,000 in the previous year. Total other expenses increased $422,000 to $2.0 million from $1.6 million, or 26.4%, due to increased staff, additional occupancy expenses and volume related charges.

Net Interest Income. Total interest income increased 28.1% to $4.1 million from $3.2 million primarily due to the growth and mix of earning assets. Interest and fees on loans increased by $1.3 million for the year ended December 31, 2002, due to an increase in average loans and loans available for sale outstanding of $22.5 million or 90.3% from the prior period. Interest on federal funds sold decreased by $242,000 due to lower yields caused by market rate declines and a decrease of $770,000 in average balances. Interest and dividends on investments decreased by $169,000 for the period due to a general decline in market interest rates.

Total interest expense decreased $99,000 from the prior period, due principally to a decrease in the average rate paid on deposits and short-term borrowings from 3.26% to 2.10%. Our net interest margin was 3.97% for the year ended December 31, 2002 as compared to 3.85% for the prior period ended December 31, 2001.

Provision for Loan Losses. Our provision for loan losses for 2002 was $275,000, representing a $50,000, or 22.2%, increase over the $225,000 recorded for 2001. Provisions for loan losses are charged to income to bring the allowance for loan losses to a level deemed appropriate by management based on factors discussed under "Business -- Allowance for Loan Losses." The increase in the 2002 provision was principally due to the substantial growth in our loan portfolio combined with management's view of the appropriate level of reserves given the state of the economy in 2002. The allowance for loan losses was $576,000 at December 31, 2002, representing 1.06% of total outstanding loans. The allowance for loan losses at December 31, 2001 was $335,000 or 0.91% of total outstanding loans at that date.

Total Other Income. We derive a significant portion of our other income from fees assessed on retail and business deposit account holders. Fees from deposit account holders for the year ended December 31,



2002 were approximately $85,000 compared to $47,000 for the year ended December 31, 2001. This increase is primarily the result of deposit growth. In addition, during 2002 we recorded income from the sale of residential mortgages held-for-sale in the amount of $62,000 and gains on the sale of available-for-sale securities in the amount of $24,000. For the year ended December 31, 2001, we recorded gains on sale of mortgages held-for-sale in the amount of $46,000 and gains on sale of available-for-sale securities of $65,000.

Total Other Expenses. Total other expenses for the year ended December 31, 2002 increased 26.4% to $2.0 million as compared to $1.6 million for the year ended December 31, 2001. Most of the increases were due to the following growth related factors:

- Salaries, wages and employee benefit expenses were $842,000 for the year ended December 31, 2002 as compared to $770,000 in the prior period, reflecting additions to our staff as well as normal compensation increases.

- In the second quarter of 2002, the bank moved its accounting and operations department to a new location. This coupled with additional equipment for the added staff resulted in 29.8% increase in occupancy and equipment expenses to $218,000 from $168,000 in the prior year.

- As the volume of our business increased due to our growth, data processing expenses for the year ended December 31, 2002 were $223,000, a 54.9% increase from the previous period.

- Professional services increased $77,000 to $195,000 in 2002 from $118,000 in 2001, as audit and loan review fees increased 75.9% from $58,000 in 2001 to $102,000 in 2002. Legal expenses also increased during the period from $41,000 in 2001 to $68,000 in 2002.

- Other operating expense increased $127,000 to $470,000 in 2002 from $343,000 in 2001, as the growth in deposits and assets caused FDIC/OCC premiums and assessments to increase from $25,000 in 2001 to $45,000 in 2002, an increase of 80.0%. In addition, during 2002 we increased our dependence on outside couriers used for pick-up and delivery services to our customers. (The bank's internal courier service did not commence operations until 2003.) As a result of this and general growth, postage and courier related expenses increased to $77,000 in 2002, a 108.1% increase from the prior period.

Income Taxes. During 2002, we recorded an income tax expense of $329,000, compared to a net tax benefit of $94,000 for 2001. This net tax benefit was due to the reversal of the valuation allowance on our deferred tax assets in the amount of $194,000, which offset our current tax expense of $125,000. We have deferred tax assets because of differences that arise between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

## LIQUIDITY

Liquidity represents an institution's ability to meet present and future financial obligations through either the sale or maturity of existing assets or the acquisition of additional funding through liability management. Liquid assets include cash, interest-bearing deposits with banks, federal funds sold, securities classified as available-for-sale, and loans maturing within one year. As a result of our management of liquid assets and the ability to generate liquidity through additional deposits or borrowings, we are able to maintain overall liquidity sufficient to satisfy our deposit withdrawal requirements and meet our customers' borrowing needs.

At December 31, 2003 cash, cash equivalents, securities classified as securities available for sale, and federal funds sold totaled $44.5 million and were 37.7% of total assets. However, we have pledged $26.1 of our securities available for sale as collateral for uninsured municipal deposits held by us and uninsured deposits that underlie retail repurchase agreements, which adversely impacts our liquidity position. Asset liquidity is also provided by managing loan maturities. At December 31, 2003, approximately $29.6 million or 44.3% of loans would mature or reprice within a one-year period. To the extent possible, loans are funded with deposits or other funding with coinciding maturity or repricing dates.



Net cash provided by operating activities for the year ended December 31, 2003 was $721,000 compared to $838,000 for the previous period. The difference can be attributed to an increase in mortgage loans available for sale offset by increased accretion of discounts on securities. An increase in other assets also contributed to the change.

Net cash used in investing activities was $15.8 million for the year ended December 31, 2003 compared with $30.8 million for the previous year. Proceeds from prepayments and redemptions of securities in excess of the prior year, as well as a slower pace of loan growth, accounted for the majority of this change.

Cash provided by financing activities was $19.5 million in fiscal year 2003 compared with $18.2 million in fiscal year 2002. Deposit growth was partially offset by a decline in short-term borrowings. In addition, in December 2002, we completed a public offering of units of common stock and warrants. 1st Colonial raised net proceeds of $1.9 million in that offering, and these proceeds were included in cash provided by financing activities in fiscal year 2002.

CAPITAL RESOURCES

The assessment of capital adequacy depends on a number of factors such as asset quality, liquidity, earnings performance, changing competitive conditions, economic forces and growth and expansion activities. We seek to maintain a capital base to support our growth and expansion activities, to provide stability to current operations and to promote public confidence.

The bank's capital position exceeds regulatory minimums. The primary indicators relied on by the OCC and other bank regulators in measuring strength of capital position are the Tier 1 risk-based capital ratio, total risk-based capital ratio and leverage ratio. Tier 1 capital consists of common and qualifying preferred shareholders' equity less goodwill. Total capital consists of Tier 1 capital, qualifying subordinated debt and a portion of the allowance for possible loan losses. Risk-based capital ratios are calculated with reference to risk weighted assets, which consist of both on and off balance sheet risks (such as letters of credit, lines of credit and home equity lines).

We manage capital ratios to exceed regulatory minimums. The bank's Tier 1 risk-based capital ratio was 13.52% at December 31, 2003. The bank's total risk-based capital ratio was 14.60% at December 31, 2003. These ratios are in excess of the mandated minimum requirements of 4.00% and 8.00%, respectively. The leverage ratio consists of Tier 1 capital divided by quarterly average assets. At December 31, 2003, the bank's leverage ratio was 8.73%, which exceeded the required minimum leverage ratio of 4.00%. Management anticipates these ratios to decline as capital is leveraged in support of deposit and asset growth.

The following table shows our regulatory capital ratios and shareholders' equity to total assets as of December 31, 2003:

| | AT DECEMBER 31, 2003 | |
|---|---|---|
| | REGULATORY MINIMUM | ACTUAL RATIO |
| Total risk-based capital ratio | 8.0% | 14.60% |
| Tier 1 risk-based capital ratio | 4.0% | 13.52% |
| Tier 1 leverage ratio | 4.0% | 8.73% |
| Shareholders' equity to total assets | None | 8.09% |

CONTRACTUAL OBLIGATIONS

We enter into contractual obligations in the normal course of business as a source of funds for its asset growth and its asset/liability management, to fund acquisitions, and to meet required capital needs. These



obligations require us to make cash payments over time as detailed in the table below (For further information regarding our contractual obligations refer to Notes 9, 10, 15 and 16 of our Consolidated Financial Statements included in this prospectus.):

PAYMENTS DUE BY PERIOD

| CONTRACTUAL OBLIGATIONS AT DECEMBER 31, 2003 | TOTAL | LESS THAN 1 YEAR | 1-3 YEARS | 4-5 YEARS | AFTER 5 YEARS |
|---|---|---|---|---|---|
| | | (DOLLARS IN THOUSANDS) | | | |
| Borrowings | $ 4,087 | $ 4,087 | $ 0 | $ 0 | $0 |
| Certificates of deposit | 26,232 | 20,577 | 2,251 | 3,404 | 0 |
| Operating leases | 363 | 78 | 185 | 100 | 0 |
| Capital leases | 0 | 0 | 0 | 0 | 0 |
| Total contractual cash obligations | $30,682 | $24,742 | $2,436 | $3,504 | $0 |

OFF-BALANCE SHEET INSTRUMENTS

We do not have any off-balance sheet arrangements as that term is defined in Item 303 of SEC Regulation S-B (such as guarantee contracts, credit or liquidity support arrangements, derivative instruments or variable interests in other entities). We are, however, a 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 manage its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit. These financial instruments involve elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of these financial instruments reflect the extent of our involvement in particular classes of financial instruments.

Our exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments. Unless noted otherwise, we do not require and are not required to pledge collateral or other security to support financial instruments with credit risk.

AMOUNT OF COMMITMENT EXPIRATION PER PERIOD

| OTHER COMMERCIAL COMMITMENTS AT DECEMBER 31, 2003 | TOTAL AMOUNTS COMMITTED | LESS THAN 1 YEAR | 1-3 YEARS | 4-5 YEARS | AFTER 5 YEARS |
|---|---|---|---|---|---|
| | (DOLLARS IN THOUSANDS) | | | | |
| Commitments to extend credit: | | | | | |
| Lines of Credit | $3,666 | $3,274 | $392 | $0 | $ 0 |
| Unfunded residential mortgages | 4,653 | 522 | 0 | 0 | 4,131 |
| Total commercial commitments | $8,319 | $3,796 | $392 | $0 | $4,131 |

For further information regarding our commitments, refer to Note 16 of our Consolidated Financial Statements included in this prospectus.

INTEREST SENSITIVITY

An important element of both earnings performance and the maintenance of sufficient liquidity is management of the interest sensitivity gap. The interest sensitivity gap is the difference between interest-rate sensitive assets and interest-rate sensitive liabilities in a specific time period. Interest rate "gap analysis" is a common, though imperfect, measure of interest rate risk, which measures the relative dollar amounts of interest-earning assets and interest-bearing liabilities which re-price within these specific time periods, either through maturity or rate adjustment. A "positive gap" for a given period means that the amount of interest-



earning assets maturing or otherwise repricing within that period exceeds the amount of interest-bearing liabilities maturing or otherwise repricing within the same period. Accordingly, in a declining interest rate environment, an institution with a "positive gap" would generally be expected, absent the effects of other factors, to experience a decrease in the yield on its assets greater than the decrease in the cost of its liabilities and its net interest income should be negatively affected. Conversely, the cost of funds for an institution with a "positive gap" would generally be expected to increase more slowly than the yield on its assets in a rising interest rate environment, and such institution's net interest income generally would be expected to be positively affected by rising interest rates. If we had a "negative gap" position with respect to a given time period, it would indicate that more liabilities may reprice within that time period than assets, with the result that rising rates may have a negative impact on interest rate spread and therefore on earnings.

The gap can be managed by repricing assets or liabilities, by selling securities or loans held-for-sale, by replacing an asset or liability at maturity or by adjusting the interest rate during the life of an asset or liability. Matching the amounts of assets and liabilities repricing in the same time interval contributes to preserving net interest margins and minimizing the impact on net interest income in periods of rising or falling interest rates. We evaluate interest sensitivity risk and then formulate guidelines regarding asset generation and pricing, funding sources and pricing, and off-balance sheet commitments (such as letters of credit, lines of credit and credit card lines) in order to manage sensitivity risk. These guidelines are based on management's outlook regarding future interest rate movements, the state of the regional and national economy, and other financial and business risk factors.

The following table illustrates our interest sensitivity gap position at December 31, 2003. It summarizes the contractual repayment terms or nearest repricing dates of our interest earning assets and interest-bearing liabilities. This table presents a position that existed at one particular day (December 31, 2003) and therefore is not necessarily indicative of our position at any other time.

INTEREST SENSITIVITY ANALYSIS

| | MATURING OR REPRICING IN: | | | | |
|---|---|---|---|---|---|
| | WITHIN 3 MONTHS | 4-12 MONTHS | 1-5 YEARS | OVER 5 YEARS | TOTAL |
| | (DOLLARS IN THOUSANDS) | | | | |
| Interest earning assets: | | | | | |
| Federal funds sold | $ 9,735 | $ -- | $ -- | $ -- | $ 9,735 |
| Interest bearing deposits | 500 | -- | -- | -- | 500 |
| Investment securities held to maturity | 387 | 5,421 | -- | -- | 5,808 |
| Investment securities available-for-sale | 8,812 | 8,169 | 10,493 | 511 | 27,985 |
| Loans and mortgages available for sale | 20,579 | 9,005 | 36,536 | 711 | 66,831 |
| Total interest earning assets | $40,013 | $22,595 | $47,029 | $ 1,222 | $110,859 |
| Interest bearing liabilities: | | | | | |
| Deposits: | | | | | |
| Interest bearing demand | $ 6,612 | $18,680 | $ 9,014 | $ 3,005 | $ 37,311 |
| Money market | 2,646 | 3,402 | 9,073 | -- | 15,121 |
| Savings | 762 | 709 | 2,836 | 946 | 5,253 |
| Time deposits $100,000 and over | 9,737 | 5,591 | 1,556 | -- | 16,884 |
| Time deposits less than $100,000 | 2,277 | 2,972 | 4,099 | -- | 9,348 |
| Other borrowed money | 4,087 | -- | -- | -- | 4,087 |
| Total interest bearing liabilities | $26,121 | $31,354 | $26,578 | $ 3,951 | $ 88,004 |
| Period gap | $13,892 | $(8,759) | $20,451 | $(2,729) | $ 22,855 |
| Cumulative gap | $13,892 | $ 5,133 | $25,584 | $22,855 | |
| Ratio of cumulative gap to total interest earning assets | 12.53% | 4.63% | 23.08% | 20.62% | |

======= ======= ======= =======



While securities available-for-sale are presented in the foregoing table according to the earlier of their stated maturities or call dates, such investments can, if necessary, be sold at any time in reaction to interest rate changes or funding demands.

We manage our interest rate sensitivity gap to, among other things, control the exposure of our net interest margin such that a 200 basis point increase or decrease in market rates will impact net interest income by no more than approximately 15% in any one year period. At December 31, 2003, we estimate that if interest rates increased by 200 basis points, projected net interest income for 2003 would decrease by 3.4% despite the fact that we had a positive gap. This is due to the fact that callable agency securities would not be called and we would not be able to reinvest these funds into higher yielding investments. Given the current interest rate levels, all interest rates could not decline 200 basis points. We estimate that a 100 basis point decrease would cause net interest income to decrease approximately 7.4%. This is due to callable agency securities being called, necessitating reinvestment into lower yielding investments.

As noted previously, securities available for sale, while presented in the table at their stated maturities or possible call date whichever is shorter, can be sold any time and are an active interest sensitivity gap management tool. Further, the magnitude and timing of changes to deposit rate changes can be managed to further minimize the exposure of net interest margin. For example, savings deposits and certain interest bearing demand deposits, while recorded at their first possible repricing opportunity, would not likely react as quickly to a market rate change as their first recorded repricing opportunity would indicate.

RECENT ACCOUNTING PRONOUNCEMENTS

TECHNICAL CORRECTIONS TO FASB STATEMENTS.

In April 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections. This Statement rescinds FASB Statement No. 4, Reporting Gains and Losses from Extinguishment of Debt, and an amendment of that Statement, FASB Statement No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements. This Statement also rescinds FASB Statement No. 44, Accounting for Intangible Assets of Motor Carriers. This Statement amends FASB Statement No. 13, Accounting for Leases, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. This Statement also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions.

The provisions of this Statement related to the rescission of Statement 4 shall be applied in fiscal years beginning after May 15, 2002. Any gain or loss on extinguishment of debt that was classified as an extraordinary item in prior periods presented that does not meet the criteria in Opinion 30 for classification as an extraordinary item shall be reclassified.

The provisions in paragraphs 8 and 9(c) of this Statement related to Statement 13 shall be effective for transactions occurring after May 15, 2002, with early application encouraged. All other provisions of this Statement shall be effective for financial statements issued on or after May 15, 2002, with early application encouraged.

The adoption of this Statement did not have an impact on 1st Colonial's earnings, financial condition or equity.

COSTS ASSOCIATED WITH EXIT OR DISPOSAL ACTIVITIES

In June 2002, the FASB issued SFAS No. 146 Accounting for Costs Associated with Exit or Disposal Activities. This Statement requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. The standard nullifies Emerging Issues Task Force (EITF) Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring).



The provisions of this Statement are to be applied prospectively for exit or disposal activities that are initiated after December 31, 2003, with early application encouraged. 1st Colonial does not expect the adoption of this Statement to have an impact on its earnings, financial condition, or equity.

ACQUISITIONS OF CERTAIN FINANCIAL INSTITUTIONS

In October 2002, the FASB issued Statement No. 147, Acquisitions of Certain Financial Institutions, which amends SFAS No. 72, Accounting for Certain Acquisitions of Banking or Thrift Institutions, SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, and FASB Interpretation No. 9. Except for transactions between two or more mutual enterprises, this Statement removes acquisitions of financial institutions from the scope of both Statement No. 72 and Interpretation 9 and requires that those transactions be accounted for in accordance with FASB Statements No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets. Thus, the requirement in paragraph 5 of Statement No. 72 to recognize any excess of the fair value of liabilities assumed over the fair value of tangible and identifiable intangible assets acquired as an unidentifiable intangible asset no longer applies to acquisitions within the scope of this Statement. In addition, this Statement amends Statement No. 144 to include in its scope long-term customer-relationship intangible assets of financial institutions such as depositor- and borrower-relationship intangible assets and credit cardholder intangible assets. Consequently, those intangible assets are subject to the same undiscounted cash flow recoverability test and impairment loss recognition and measurement provisions that Statement No. 144 requires for other long-lived assets that are held and used. With some exceptions, the requirements of Statement No. 147 are effective October 1, 2002. The adoption of this Statement did not have an impact on 1st Colonial's earnings, financial condition, or equity.

ACCOUNTING FOR STOCK-BASED COMPENSATION

In December 2002, FASB issued SFAS No. 148, Accounting for Stock-Based Compensation -- Transition and Disclosure -- an amendment of FASB Statement No. 123. SFAS No. 148 amends FASB Statement No. 123, Accounting for Stock-Based Compensation, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 amends the disclosure requirements of Statement 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The provisions of SFAS No. 148 are effective for fiscal years ending after December 15, 2002, except for financial reports containing condensed financial statements for interim periods for which disclosure is effective for periods beginning after December 15, 2002. Adoption of SFAS No. 148 did not impact 1st Colonial's earnings, financial condition, or equity. However, 1st Colonial did modify its disclosures related to the method of accounting for stock-based employee compensation in accordance with SFAS No. 148.

GRANTOR'S ACCOUNTING AND DISCLOSURE REQUIREMENTS FOR GUARANTEES

During 2002, FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees Including Indirect Guarantees of Indebtedness of Others, was issued. FASB Interpretation No. 45 requires a guarantor to include disclosure of certain obligations, and if applicable, at the inception of the guarantee, recognize a liability for the fair value of other certain obligations undertaken in issuing a guarantee. The recognition requirement is effective for guarantees issued or modified after December 31, 2003. Adoption of FASB Interpretation No. 45 did not have an impact on 1st Colonial's earnings, financial condition, or equity.

CONSOLIDATION OF VARIABLE INTEREST ENTITIES

During 2002, FASB Interpretation No. 46, Consolidation of Variable Interest Entities, was issued. FASB Interpretation No. 46 clarifies the application of Accounting Research Bulletin No. 51 and applies immediately to any variable interest entities created after January 31, 2003 and to variable interest entities in which an interest is obtained after that date. Adoption of FASB Interpretation No. 46 did not have an impact on 1st Colonial's earnings, financial condition, or equity.



DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

In April 2003, the FASB issued Statement No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities. This Statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities. With some exceptions, this Statement is effective for contracts entered into or modified after June 30, 2003. The adoption of this Statement did not have an impact on 1st Colonial's earnings, financial condition, or equity.

FINANCIAL INSTRUMENTS WITH DEBT AND EQUITY CHARACTERISTICS

In May 2003, the FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003, except for mandatorily redeemable financial instruments of nonpublic entities. The adoption of this Statement did not have an impact on 1st Colonial's earnings, financial condition, or equity.



BUSINESS

GENERAL

We are a Pennsylvania business corporation and bank holding company registered under the Bank Holding Company Act of 1956. 1st Colonial was incorporated on February 26, 2002 for the purpose of acquiring the bank, thereby enabling the bank to operate within a holding company structure. On June 30, 2002, 1st Colonial acquired 100% of the outstanding shares of the bank.

The principal activities of 1st Colonial are owning and supervising the bank. The bank is a community-oriented, full-service commercial bank providing commercial and consumer financial services to businesses and individuals in Camden County, New Jersey and surrounding areas. We believe that we will continue to gain market share in our geographic market. We compete with the many existing and larger financial institutions in our geographic market by emphasizing personalized service, responsive decision making and an overall commitment to excellence.

The bank offers commercial and consumer loans of all types, including real estate loans, residential mortgage loans, home equity loans and lines of credit, auto loans and other credit products. The bank's deposit services include business and individual demand and time deposit accounts, NOW accounts, money market accounts, Individual Retirement Accounts and holiday accounts. Our strategy for deposit acquisition and development has been to attract and retain core deposits, and we traditionally have not priced our deposits to attract short-term relationships. We do not accept brokered deposits. The bank is not authorized to offer trust services and does not presently offer the sale of investment products such as mutual funds to its customers.

We provide a number of convenience-oriented services and products to our customers, including direct payroll and social security deposit services, bank-by-mail services, letters of credit, access to a national automated teller machine network, safe deposit boxes, night depository facilities, notary services, courier services and travelers checks. We also offer telephone banking services that enable our customers to obtain account information, effectuate transfers between accounts, order new checks and make stop payment requests. In addition, we intend to begin offering Internet-banking services to our customers in the third quarter of 2004, using a third party service provider.

We have outsourced virtually all of our data processing operations to a third party service provider with respect to deposit accounts, checking accounts, loan accounts and other matters, as well as ATM processing services. We also use third parties to provide certain credit card processing services and escrow deposit processing services.

As of December 31, 2003, we employed 23 full-time and three part-time employees.

BUSINESS STRATEGY

Our mission is to become the leading community