CB BANCSHARES INC/HI
Form 10-K
March 11, 2004

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549
FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2003

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 0-12396

CB BANCSHARES, INC.

(Exact name of registrant as specified in its charter)

Hawaii	99-0197163
(State of Incorporation)	(IRS Employer Identification No.)

201 Merchant Street Honolulu, Hawaii 96813
(Address of principal executive offices)

(Registrant s Telephone Number) (808) 535-2500

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, Par value $1.00 per share

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

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

The aggregate market value of registrant s Common Stock held by non-affiliates at June 30, 2003 was approximately $248,667,000. As of January 31, 2004, registrant had outstanding 4,338,337 shares of common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement for its annual meeting of shareholders to be held on April 29, 2004 are incorporated by reference into Part III and IV.

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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Securities Exchange Act of 1934, as amended by the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, included in this report that address results or developments that CB Bancshares, Inc. and consolidated subsidiaries (the Company) expects or anticipates will or may occur in the future, where statements are preceded by, followed by or included the words believes , plans , intends , expects , anticipates or similar expressions, including such things as: (i) business strategy; (ii) economic trends and market condition, particularly in Hawaii; (iii) the direction of interest rates and prepayment speeds of mortgage loans and mortgage-backed securities; (iv) the adequacy of the Company s allowances for credit and real estate losses based on credit risks inherent in the lending processes; (v) expansion and growth of the Company s business and operations; (vi) renewal of existing credit agreements with and availability of additional advances from the Federal Home Loan Bank of Seattle (the FHLB); and (vii) other matters are forward-looking statements. These statements are based upon certain assumptions and analyses made by the Company in light of its experience and its perception of historical trends, current conditions and expected future developments as well as other factors it believes are appropriate in the circumstances. These statements are subject to a number of risks and uncertainties, many of which are beyond the control of the Company, including international, national and local economic, market or business conditions; real estate market conditions, particularly in Hawaii; the opportunities (or lack thereof) that may be presented to and pursued by the Company; competitive actions by other companies; changes in laws and regulations; the effects of natural disasters, terrorist acts and wars; and other factors. Actual results could differ materially from those contemplated by these forward-looking statements. Consequently, all of the forward-looking statements made in this report are qualified by these cautionary statements and there can be no assurance that the actual results or developments anticipated by the Company will be realized or, even substantially realized, and that they will have the expected consequences to or effects on the Company and its business or operations. Forward-looking statements made in this report speak as of the date hereof. The Company undertakes no obligation to update or revise any forward-looking statement in this report.

PART I
ITEM 1. BUSINESS

CB BANCSHARES, INC.

CB Bancshares, Inc. (the Parent Company) is a bank holding company which was incorporated in the State of Hawaii in 1980. As a bank holding company, the Parent Company has the flexibility to directly or indirectly engage in certain bank-related activities other than banking, subject to regulation by the Board of Governors of the Federal Reserve System (the Federal Reserve Board or FRB). The Parent Company has three wholly-owned subsidiaries, City Bank (the Bank), Datatronix Financial Services, Inc. (Datatronix) and O.R.E., Inc. (inactive), which are discussed below.

Our Internet address is *www.citybankhawaii.com*. On our Investor Relations web site, which can be accessed through *www.citybankhawaii.com*, we post the following filings as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission: our annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, our proxy statement related to our annual stockholders meeting and any amendments to those reports or statements filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. All such filings on our Investor Relations web site are available free of charge.

CITY BANK

City Bank is a state-chartered bank organized under the laws of the State of Hawaii in 1959. The Bank is insured by the Federal Deposit Insurance Corporation (the FDIC), and provides full commercial banking services through 17 branches on the island of Oahu, 2 branches on the island of Hawaii, 2 branches on the island of Maui and 1 branch on the island of Kauai. These services include receiving demand, savings and time deposits; making commercial, real estate and consumer loans; financing leases; financing international trade activities; issuing letters of credit; handling domestic and foreign collections; selling travelers checks and bank money orders; and renting safe deposit boxes.

The Bank s primary focus has been corporate lending to small- to medium-sized businesses by maintaining relationships and expertise within business segments and providing personal customer service. The Bank intends to continue to develop and enhance the expertise of the corporate sales force and to leverage these corporate relationships to generate core deposit growth. The Bank has linked the corporate and wholesale lending to the retail banking group with the intent of developing seamless service between the corporate loan officers and the branch personnel and to increase cross-sale opportunities between business and retail customers. The Bank has commenced implementing its customer relationship management program which it believes will significantly enhance this effort.

The Bank also plans to further develop its electronic banking activities by continuing to enhance internet banking capability for both business and retail customers.

DATATRONIX FINANCIAL SERVICES, INC.

Datatronix, a wholly-owned subsidiary, was incorporated in the State of Hawaii in June 2000. Datatronix offers item processing services to banks, thrifts and other financial institutions in the State of Hawaii and California. As of December 31, 2003, Datatronix had six customers, with the Bank as its primary customer.

BUSINESS SEGMENTS

The Company s business segments are defined as Retail Banking, Wholesale Banking, Treasury and All Others. Retail Banking is made up of retail deposits, mortgage banking and consumer lending activities. Wholesale Banking consists of wholesale deposits, commercial real estate lending, corporate lending and the specialized lending functions of the Bank. The Treasury segment is responsible for managing the Company s investment securities portfolio and borrowing. The All Other segment consists of the administrative support of the Company. Additional financial and other information about the Company s business segments is presented in the Segments Discussion section of Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) and Note V of Notes to the Consolidated Financial Statements.

FHLB BORROWINGS

A primary source of borrowings for the Company is advances from the FHLB. The Bank has credit line agreements allowing for both short- and long-term advances. The agreements permit the Bank to borrow up to 35% of total qualified assets, provided that adequate mortgage loans or investment securities are pledged as collateral. At December 31, 2003, the Bank had $305.0 million in short-term advances from the

FHLB maturing from August 2004 to December 2004 with rates from 1.10% to 1.49%, and $194.4 million in long-term advances from the FHLB ranging in maturity from January 2004 to September 2014 with rates from 2.26% to 8.22%. Advances are priced at the date of advance as either fixed or variable based. See the Liquidity section of Management s Discussion and Analysis as well as Notes H and I of Notes to the Company s Consolidated Financial Statements for further information.

COMPETITION AND ECONOMIC ENVIRONMENT

The earnings and growth of the Company are affected by the changes in the monetary and fiscal policies of the United States (the U.S.), as well as by local, national and international economic conditions. The overall growth of loans and investments, deposit levels and interest rates are directly influenced by the monetary policies of the Federal Reserve System. Since these changes are generally unpredictable, it is difficult to ascertain the impact of such future changes on the operations of the Company and its subsidiaries.

The banking business is highly competitive. The Bank competes for deposits and loans with five other commercial banks (the Bank is the fourth largest of the five commercial banks) and two other savings associations located in Hawaii. In addition to other commercial banks and savings associations, the Bank competes for savings and time deposits and certain types of loans with other financial institutions, such as consumer finance companies, credit unions, merchandise retailers, and a variety of financial service and advisory companies. The Bank also competes for mortgage loans with insurance and mortgage companies.

The economy of Hawaii is supported principally by tourism, governmental expenditures (primarily for the military), construction, and agriculture. The government has made certain strides in attempting to broaden the state s economic base in the areas of diversified agriculture, biotechnology, information technology and film. A small island economy like that of Hawaii, which significantly depends on imports for consumption, is greatly influenced by the changes in external economic conditions. A key to the economic performance of the state is the health of the U.S. and Japan economies and, to a lesser extent, the economies of Canada, Europe and other Asian nations. With the continued global instability and geopolitical issues in the Middle East and Asia, the Hawaii economy and many businesses are vulnerable to another economic downturn.

The events of September 11, 2001 have had a significant negative impact on the world, U.S. and Hawaii economies. Due to its dependence on tourism, Hawaii has been significantly affected by these events. However, during 2003, the state s tourism industry showed slight improvement over 2002, with total visitor days increasing by 3.0%. At December 31, 2003, Hawaii s unemployment rate was 3.8%, as compared to 3.6% reported a year ago. This coincided with the increase of real personal income by approximately 3.5% over this same period. Another sector showing improvement in 2003 was the state s housing market, supported by low mortgage interest rates. Residential home sales in 2003 were a record $3.5 billion, or a 35.1% increase, compared to $2.6 billion in 2002. The 2003 median sales price for single family homes and condominiums increased by 13.4% and 15.1%, respectively. Private building permits were up 37.8% overall for the year through November 2003 compared with same period in 2002. The total population of the State of Hawaii grew by 1.4% from 2002 to 2003.

Given these positive trends in key non-tourism sectors and overall economic indicators, the Hawaii economy is expected to grow moderately by 2.8% in 2004 excluding inflation. Future growth in Hawaii s economy is expected to be tied primarily to the rate of expansion in the mainland U.S. and Japan economies and increased military spending, and remains vulnerable to uncertainties in the world s geopolitical environment.

REGULATORY CONSIDERATIONS

The following discussion sets forth certain elements of the regulatory framework applicable to the Company. Federal and state regulation of financial institutions is intended primarily for the protection of depositors rather than shareholders of those entities. To the extent that the following discussion describes statutory or regulatory provisions, it is not intended to be complete and is qualified in its entirety by reference to the particular statutory or regulatory provisions, and any case law or interpretive letters concerning such provisions. In addition, there are other statutes and regulations that apply to and regulate the operation of the Company and its subsidiaries. Any change in applicable laws, or regulations, may have a material or possibly adverse effect on the business of the Company or other subsidiaries of the Company.

Bank Holding Company. The Parent Company is a bank holding company subject to supervision and regulations by the FRB under the Bank Holding Company Act of 1956, as amended (the BHCA). As a bank holding company, the Parent Company s activities and those of its banking and non-banking subsidiaries are limited to the business of banking and activities closely related or incidental to banking and to certain expressly permitted nonbanking activities. In addition, with certain exceptions, the Parent Company may not acquire, directly or indirectly, more than 5% of any class of the voting shares of, or substantially all of the assets of, a bank or any other company without the prior approval of the FRB.

The Bank. The Bank is organized under the laws of the State of Hawaii and is subject to significant regulations by the FDIC and the State of Hawaii Division of Financial Institutions of the Department of Commerce and Consumer Affairs. The Bank is also subject to significant federal and state regulations which materially affects its operations.

The Community Reinvestment Act. The Community Reinvestment Act (the CRA) requires lenders to identify the communities served by the Company s offices and to identify the types of credit the institution is prepared to extend within such communities. Under the CRA regulations of the FDIC and the other federal banking agencies, an institution s performance in making loans and investments and maintaining branches and providing services in low- and moderate-income areas within the communities that it serves is evaluated. In connection with its assessment of CRA performance, the FDIC assigns a rating of outstanding, satisfactory, needs to improve, or substantial noncompliance.

The Federal Home Loan Banks. Under the Federal Home Loan Bank Act, as amended, the ongoing stock investment requirement is equal to 0.3% of total assets, 1% of residential mortgages and mortgage-backed securities, or 5% of advances divided by the institution s Qualifying Assets Ratio (QAR), whichever is higher. The institution s QAR will determine a ratio of stock to borrowings (the higher the QAR, the lower the stock to borrowings requirement). The stock is recorded as a restricted investment security at par. Furthermore, FHLB advances must be collateralized with certain types of assets. Accordingly, the Company has pledged certain investments and loans to the FHLB as collateral for its advances.

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Dividend Restrictions. The principal source of the Parent Company s cash flow has been dividend payments received from the Bank. Dividends paid to the Parent Company by the Bank totaled $11.8 million and $5.8 million in 2003 and 2002, respectively. Under the laws of Hawaii, payment of dividends by the Bank is subject to certain restrictions, and payment of dividends by the Parent Company is likewise subject to certain restrictions.

The Company will continue to evaluate the dividend on a quarterly basis. In addition, applicable regulatory authorities are authorized to prohibit banks, thrifts and their holding companies from paying dividends which would constitute an unsafe and unsound banking practice. The FRB has indicated that it would generally be an unsafe and unsound banking practice for banks to pay dividends except out of current operating earnings. Furthermore, an insured depository institution, such as the Bank, cannot make a capital distribution (broadly defined to include, among other things, dividends, redemptions and other repurchases of stock), or pay management fees to its holding company if, thereafter, the depository institution would be undercapitalized.

Capital Standards. The Parent Company and the Bank are subject to capital standards promulgated by the FRB, the FDIC, and the Hawaii Division of Financial Institutions. The minimum ratio of total capital to risk-weighted assets, provided for in the guidelines adopted by the FRB, including certain off-balance-sheet items such as standby letters of credit, is 8%. At least half of the total capital is to be comprised of common equity, retained earnings, non-cumulative perpetual preferred stock, and a limited amount of cumulative perpetual preferred stock less goodwill (Tier 1 Capital). The remainder may consist of a limited amount of subordinated debt, other preferred stock, certain other instruments, and a limited amount of reserves for loan losses (Tier 2 Capital). The FDIC s risk-based capital guidelines for state non-member banks of the Federal Reserve System are generally similar to those established by the FRB for bank holding companies.

The FRB and FDIC also have adopted minimum leverage ratios for bank holding companies and banks requiring bank organizations to maintain a Leverage Ratio (defined as Tier 1 Capital divided by average total assets less goodwill) of at least 4% of total assets. The most highly rated banking organizations are expected to maintain an additional cushion of at least 100 basis points (1% equals 100 basis points), taking into account the level and nature of risk, to be allocated to the specific banking organizations by the primary regulator.

FRB guidelines also provide that banking organizations experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. Furthermore, the guidelines indicate that the FRB will continue to consider a tangible Tier 1 leverage ratio in evaluating proposals for expansion or new activities. The tangible Tier 1 leverage ratio is the ratio of a banking organization s Tier 1 Capital, less intangibles, to total assets, less intangibles.

Failure to meet capital guidelines could subject a bank to a variety of enforcement remedies, including the termination of deposit insurance by the FDIC, and to certain restrictions on its business, including restricting the payment of dividends. At December 31, 2003, the Company and the Bank exceeded applicable capital requirements. The consolidated capital position of the Parent Company at December 31, 2003 was as follows:

	Company ratio	Minimum required ratio
Risk-based Capital:		
Tier 1 capital ratio	11.03%	4.00%
Total capital ratio	12.29%	8.00%
Leverage ratio	8.90%	4.00%

Under FRB regulations, a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, it is the FRB s policy that in serving as a source of strength to its subsidiary banks, a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company s failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice or a violation of the FRB regulations, or both. Any capital loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. Moreover, Congress has passed legislation pursuant to which depositors are granted a preference over all other unsecured creditors in the event of the insolvency of a bank or thrift.

Affiliate Transactions. Unless an exemption applies, sections 23A and 23B of the Federal Reserve Act and Regulation W thereunder (i) limit the extent to which a financial institution or its subsidiaries may engage in covered transactions with an affiliate, to an amount equal to 10% of such institution s capital and surplus and an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such capital and surplus and (ii) require that all transactions with an affiliate be on terms substantially the same, or at least as favorable to the institution or subsidiary, as those provided to a non-affiliate. The term covered transaction includes the making of loans, purchase of assets, issuance of a guarantee and other similar types of transactions.

Safety and Soundness. The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) requires each federal banking regulatory agency to prescribe, by regulation, standards for all insured depository institutions and depository institution holding companies relating to: (i) internal controls, information systems and audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate risk exposure; (v) asset growth; (vi) compensation, fees and benefits; and (vii) such other operational and managerial standards as the agency determines to be appropriate. The compensation standards would prohibit employment contracts, compensation or benefit arrangements, stock option plans, fee arrangements or other compensatory arrangements that provide excessive compensation, fees or benefits or could lead to material financial loss. In addition, each federal banking regulatory agency must prescribe by regulation standards specifying: (i) a maximum ratio of classified assets to capital; (ii) minimum earnings sufficient to absorb losses without impairing capital to the extent feasible; (iii) a minimum ratio of market value to book value for publicly traded shares of depository institutions and depository institution holding companies; and (iv) such other standards relating to asset quality, earnings and valuation as the agency determines to be appropriate. If an insured depository institution or its holding company fail to meet any of the standards promulgated by regulations, then such company will be required to submit a plan to its federal regulator specifying the steps it will take to correct the deficiency. The federal banking agencies have uniform rules concerning these standards.

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Prompt Corrective Action. Under FDICIA, each federal banking agency is required to take prompt corrective action to resolve the problems of insured depository institutions that do not meet minimum capital ratios. The extent of an agency s power to take prompt corrective action depends upon whether an institution is well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, or critically undercapitalized.

The federal banking agencies have adopted regulations to implement the prompt corrective action provisions of FDICIA. Under the regulations, an institution shall be deemed to be: (i) well-capitalized if it has total risk-based capital of 10% or more, has a Tier 1 risk-based capital ratio of 6% or more, has a Tier 1 leverage capital ratio of 5% or more and is not subject to any written agreement, order or directive to meet and maintain a specific capital level for any capital measure; (ii) adequately capitalized if it has a total risk-based capital ratio of 8% or more, a Tier 1 risk-based capital ratio of 4% or more and a Tier 1 leverage capital ratio of 4% or more (3% under certain circumstances) and does not meet the definition of well-capitalized; (iii) undercapitalized if it has a total risk-based capital ratio that is less than 8%, a Tier 1 risk-based capital ratio of 4% or more or a Tier 1 leverage capital ratio that is less than 4% (3% under certain circumstances); (iv) significantly undercapitalized if it has a total risk-based capital ratio that is less than 6%, a Tier 1 risk-based capital ratio that is less than 3% or a Tier 1 leverage capital ratio that is less than 3%; and (v) critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2%.

FDICIA authorizes the appropriate federal banking agency, after notice and an opportunity for a hearing, to treat an insured depository institution as if it had a lower capital-based classification if it is in an unsafe or unsound condition, engages in an unsafe or unsound practice or receives an unsatisfactory examination rating. Thus, a well-capitalized institution could be subjected to the restrictions of undercapitalized institutions.

An undercapitalized institution is required to submit an acceptable capital restoration plan to its appropriate federal banking agency. The plan must specify: (i) the steps the institution will take to become adequately capitalized; (ii) the capital levels to be attained each year; (iii) how the institution will comply with any regulatory sanctions then in effect against the institution; and (iv) the types and levels of activities in which the institution will engage. An undercapitalized institution is also generally prohibited from paying any management fee or dividends to its holding company, increasing its average total assets and is generally prohibited from making any acquisitions, establishing any new branches or engaging in any new line of business except in accordance with an accepted capital restoration plan or with the approval of the FDIC.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the IBBEA) amended the BHCA to create certain interstate banking and branching opportunities. Under the IBBEA, a bank holding company may acquire a bank located in any state, provided that the acquisition does not result in the bank holding company controlling more than 10% of the deposits in insured depository institutions in the United States, or 30% of deposits in insured institutions in the state in which the bank to be acquired is located (unless the state waives the 30% deposit limitation or it is the initial entry into the state). The IBBEA permits individual states to restrict the ability of an out-of-state bank holding company or bank to acquire an in-state bank that has been in existence for less than five years and to establish a state concentration limit of less than 30% if such reduced limit does not discriminate against out-of-state bank holding companies or banks.

The IBBEA authorizes an adequately-capitalized bank, with the approval of the appropriate federal banking agency, to merge with another adequately-capitalized bank in any state that has not opted out of interstate branching. Such a bank may operate the target s offices as branches if certain conditions are satisfied. The same national and state deposit concentration limits and applicable state minimum-existence restrictions which apply to interstate acquisitions (as discussed above) also apply to interstate mergers. The applicant also must comply with any non-discriminatory host state filing and notice requirements and demonstrate a record of compliance with applicable federal and state community reinvestment laws. Hawaii enacted an interstate branching and bank mergers law which expressly permits interstate branching under Sections 102 and 103 of the IBBEA.

Under the IBBEA, the resulting bank in an interstate merger may establish or acquire additional branches at any location in a state where any of the banks involved in the merger could have established or acquired a branch. A bank also may acquire one or more branches of an out-of-state bank without acquiring the target out-of-state bank if the law of the target s home state permits such a transaction. In addition, the IBBEA permits a bank to establish a de novo branch in another state if the host state statutorily permits de novo interstate branching.

Hawaii law authorizes out-of-state banks to engage in interstate merger transactions (mergers and consolidations with and purchases of all or substantially all of the assets and branches of) with Hawaii banks, following which any such out-of-state bank may operate the branches of the Hawaii bank it has acquired. The Hawaii bank must have been in continuous operation for at least five years prior to such an acquisition, unless it is subject to or in danger of becoming subject to certain types of supervisory action. This statute does not permit out-of-state banks to acquire branches of Hawaii banks other than through an interstate merger transaction (except in the case of a bank that is subject to or in danger of becoming subject to certain types of supervisory action) nor to open branches in Hawaii on a de novo basis. Hawaii law imposes no state deposit caps or concentration limits. It also permits the State Commissioner of Financial Institutions to waive, on a case-by-case basis, federal statewide concentration limits, in accordance with standards that do not discriminate against out-of-state banks.

The IBBEA also permits a bank subsidiary of a bank holding company to act as agent for other depository institutions owned by the same holding company for purposes of receiving deposits, renewing time deposits, closing or servicing loans and receiving loan payments.

Gramm-Leach Bliley Act. The Gramm-Leach-Bliley Act (the GLB Act) revised and expanded the existing BHCA and certain sections of the 1933 Glass-Steagall Act to permit a holding company system to engage in a full range of financial activities, including but not limited to, banking, insurance, securities, merchant banking and other activities incidental to financial services. The GLB Act permits the scope of financial and incidental activities to evolve with technology and competition. It also provides expanded financial affiliation opportunities for existing bank holding companies (BHC) and allows all financial holding companies to control a full-service insured bank. These expanded permissible activities are allowable for a BHC if it becomes a financial holding company (FHC). In order to become an FHC, a BHC must file a declaration with the FRB electing to engage in activities under the new BHCA Section 4(k) and certifying that it is eligible to do so because all of its insured depository institution subsidiaries are well-capitalized and well-managed. An institution is well-capitalized if it meets the primary regulator s definition for that status under the Federal Deposit Insurance Act for prompt corrective action purposes. Additionally, the FRB must determine that each depository institution controlled by an FHC has a satisfactory or better rating under the CRA in order for a company to become an FHC or for an FHC to engage in new financial activities or acquire, directly or indirectly, a company engaged in any activity under subsection (k) or (n). The FRB will be the overall regulatory agency and, along with the Department of Treasury, will have joint oversight to determine new financial activities of FHC companies. The Parent Company has not elected FHC status.

It is anticipated that this change in legislation will serve to provide consumers added convenience and savings as FHCs will be able to provide one-stop shops for financial services. It also provides for added privacy for consumers as policies on collecting, using and protecting personal financial information must be disclosed in writing to customers and customers will have the option to block information sharing with unaffiliated third parties, such as telemarketing companies.

Depository Insurance. The FDIC has a premium schedule under which the assessment rate for a bank depends upon the risk classification the FDIC assigns the institution. This allows institutions with improving capital positions to benefit from the improvement by lower assessments, while requiring those whose capital is falling to pay higher assessments. The FDIC may raise an institution s insurance premiums or terminate insurance altogether upon a finding that the institution has engaged in unsafe and unsound practices.

Other Regulatory Considerations. The Bank is also subject to a wide array of other state and federal laws and regulations, including, without limitation, usury laws, the Patriot Act, the Equal Credit Opportunity Act, the Electronic Funds Transfer requirements, the Truth-in-Lending Act, the Truth-in-Savings Act and the Real Estate Settlement Procedures Act.

UNSOLICITED TAKEOVER PROPOSAL

On April 16, 2003, Central Pacific Financial Corp., a Hawaii corporation (CPF), delivered an unsolicited proposal to merge with the Parent Company. CPF s proposal included the exchange of each share of the Parent Company s common stock outstanding for $21 in cash and 1.8956 shares of CPF common stock.

On April 17, 2003, the Parent Company announced that it had received the proposal from CPF, and on April 23, 2003, it advised CPF that the Parent Company s Board would address the merger proposal promptly and in an orderly manner and would respond in a timely fashion. On April 23, the Parent Company also issued a press release announcing that it had engaged a financial advisor and legal counsel to assist its Board of Directors and management team in evaluating CPF s merger proposal.

On April 28, 2003, CPF filed a registration statement with the Securities and Exchange Commission in which it described its intent to commence an exchange offer for all outstanding shares of the Parent Company s common stock. On the same day, CPF filed applications with federal and state regulators in furtherance of its proposed exchange offer. Also on April 28, 2003, CPF delivered to the Parent Company a letter requesting a special meeting of shareholders of the Parent Company to vote on whether to approve CPF s acquisition of shares of the Parent Company s common stock pursuant to the proposed exchange offer under the Hawaii Control Share Acquisitions Act.

On April 29, 2003, the Parent Company announced that at its Board of Directors meeting held on April 23, 2003, the Board declared a 10% stock dividend and a cash dividend of $0.12 per common share for the second quarter of 2003, payable on June 27, 2003 to stockholders of record on June 16, 2003. Similar 10% stock dividends were declared in the second quarters of 2001 and 2002.

On May 1, 2003, CPF announced that, in light of the 10% stock dividend announced by the Parent Company on April 29, it was amending its offer so that the per share amount of cash to be paid and number of shares of CPF common stock to be issued pursuant to the proposed offer to exchange was adjusted from $21.00 to $19.09 in cash and from 1.8956 to 1.7233 in shares of CPF common stock.

On May 2, 2003, CPF amended and supplemented its prior application submitted to the Division of Financial Institutions of the Department of Commerce & Consumer Affairs of Hawaii to include a request that the Commissioner of the Division approve CPF making a tender/exchange offer, pursuant to Section 412:3-612(a)(2) of the Hawaii Revised Statutes.

On May 4, 2003, the Board of Directors of the Parent Company met with senior management and independent financial and legal advisors to consider and discuss CPF s merger proposal and the Parent Company s response. After careful consideration, the Board concluded that the CPF proposal was inadequate and not in the best interests of the Parent Company. The Board of Directors of the Parent Company authorized the issuance of a press release and delivery of a letter to CPF communicating its determination. Accordingly, on May 4, 2003, the Parent Company issued a press release announcing the Board s unanimous rejection of CPF s proposal.

On May 5, 2003, the Parent Company received a letter from CPF requesting that the date of the special meeting be moved by three weeks, from May 28, 2003 to June 19, 2003. On May 7, 2003, the Parent Company delivered to CPF a letter rejecting CPF s request.

On May 9, 2003, CPF delivered a letter to the Parent Company purporting to rescind, revoke and withdraw its April 15 merger proposal and the related information statement delivered on April 28. In the same letter, CPF argued that in light of its withdrawal of its prior proposal, the special meeting scheduled for May 28 was moot and should be cancelled.

Also on May 9, 2003, CPF delivered a second letter to the Parent Company presenting a revised proposal pursuant to which the Parent Company s shareholders would receive 1.7606 shares of CPF common stock and $24.50 in cash for each outstanding share of common stock (or 1.6005 shares and $22.27 in cash per share of common stock on a post-stock dividend basis). This revised proposal did not materially modify the value of the total consideration offered by CPF, but only changed the mix of cash and stock consideration to be received per share of common stock.

On May 9, 2003, CPF also amended its registration statement on Form S-4 so that the consideration to be paid in its proposed offer to exchange would be the same as that to be paid pursuant to the proposal reflected in CPF s May 9 letter to the Parent Company.

On May 12, 2003, the Board of Directors of the Parent Company met with senior management and independent financial and legal advisors to consider and discuss CPF s revised proposal and the Parent Company s response. After careful consideration, the Board unanimously concluded that the revised proposal was inadequate and not in the best interests of the Parent Company. Following the Board meeting, the

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Parent Company issued a press release announcing the Board s unanimous decision. The Parent Company also advised CPF that the special meeting to consider CPF s control share acquisition would be held on May 28, 2003, as the Parent Company s Board had previously scheduled in accordance with Hawaii law and CPF s letter dated April 28, 2003.

On May 13, 2003, CPF delivered to the Parent Company a letter requesting that a special meeting of shareholders be held on June 26, 2003 to vote on CPF s control share acquisition proposal. CPF s letter was accompanied by letters executed by a number of the Parent Company s shareholders purporting to designate CPF as their agent to call a special meeting. The Parent Company believed that CPF s request was invalid because, among other things, a special meeting of shareholders had already been properly called by the Board of Directors of the Parent Company to consider the control share acquisition proposal. CPF disputed the Parent Company s position and maintained that the May 28 special meeting was moot.

On May 14, 2003, CPF filed a complaint against the Parent Company in the Hawaii State court seeking a temporary restraining order and preliminary injunction to prevent the Parent Company from holding the special meeting or taking any actions in furtherance of a solicitation in connection with the special meeting. On May 16, 2003, CPF s motion for a temporary restraining order was denied.

On May 28, 2003, the Parent Company announced that based on the proxies submitted to the independent inspector of elections at the May 28 special meeting, it believed that the Parent Company s shareholders rejected CPF s proposal to acquire a majority of the Parent Company s outstanding shares.

On May 28, 2003, the Parent Company also announced that its Board of Directors amended the Parent Company s shareholder rights plan to avoid a distribution of the rights as a result of CPF s invalid request for a special meeting. Under the plan as it existed prior to the amendment, a distribution of the rights would have resulted from CPF s obtaining authorizations to call a special shareholders meeting from the Parent Company s shareholders owning approximately 27% of the outstanding shares in a non-public solicitation. The amendment to the plan states that CPF will not be deemed to be the beneficial owner of the shares underlying any of these authorizations unless the authorization ultimately is delivered to the Parent Company for a valid and effective purpose under Hawaii law and the Parent Company s governing documents.

On June 12, 2003, the Parent Company announced that the independent inspectors of election certified the final results of the shareholder vote at the special meeting held on May 28, 2003, confirming that the Parent Company s shareholders rejected CPF s proposal to acquire a majority of the Parent Company s outstanding shares.

On June 17, 2003, CPF announced that it would not continue to pursue the special meeting of shareholders that CPF purported to call for June 26, 2003.

On June 28, 2003, the Parent Company announced that CPF withdrew all pending legal claims made against the Parent Company regarding the May 28, 2003 special shareholders meeting. The Parent Company also announced that Circuit Court Judge Victoria Marks approved the stipulation dismissing CPF s complaint with prejudice, meaning its claims regarding the validity of the May 28 shareholders meeting cannot be re-filed.

On July 22, 2003, the Parent Company announced that it had filed a lawsuit in Hawaii State court against CPF asserting that CPF violated the Hawaii Control Share Acquisitions statute. The lawsuit alleged that CPF illegally formed a voting group with certain shareholders of the Parent Company without obtaining the approval of the Parent Company s shareholders as required by Hawaii law.

On July 30, 2003, CPF filed a complaint against the Parent Company in the Hawaii State court seeking to invalidate provisions of the Parent Company s new Rights Plan and bylaws, both adopted on July 23, 2003. CPF also seeks to enjoin the Parent Company from using its Rights Plans and bylaws.

On December 8 and December 9, 2003, the Division of Financial Institutions held a public hearing regarding CPF s application. On February 2, 2004, the Division of Financial Institutions approved CPF s application subject to certain conditions.

NUMBER OF EMPLOYEES

As of December 31, 2003, the Company and its subsidiaries employed 547 persons, 503 on a full-time basis and 44 on a part-time basis. Neither the Company nor any of its subsidiaries are a party to any collective bargaining agreements.

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STATISTICAL DISCLOSURES

Guide 3 of the Securities Act Industry Guides sets forth certain statistical disclosures to be included in the Description of Business section of bank holding company filings with the Securities and Exchange Commission (the SEC).

The statistical information required is presented in the index shown below and as part of Items 6 or 7 of this Form 10-K for the fiscal year ended December 31, 2003. The tables and information contained therein have been prepared by the Company and have not been audited or reported upon by the Company s independent accountants.

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ITEM 2. PROPERTIES

The operations of the Bank are transacted through its main banking office and 22 other branches. The Company s facilities are located on leased premises, and expenditures by the Company for interior improvements are capitalized. The leases for these premises expire on various dates through the year 2035. Lease terms generally provide for additional payments for real property taxes, insurance and maintenance. See Note F of Notes to the Company s Consolidated Financial Statements.

ITEM 3. LEGAL PROCEEDINGS

Claridge Complaint. On April 28, 2003, Barbara Claridge (the Plaintiff) filed a complaint against the Parent Company and each of the members of the Parent Company s Board of Directors in the Circuit Court of the First Circuit, State of Hawaii. The case is denominated as a class action on behalf of all shareholders of the Parent Company although no proceedings have taken place regarding possible class certification. Plaintiff alleges, among other things, that the offer proposed by CPF is futile without approval of the Parent Company s directors because of the Parent Company s Rights Plan, and that the defendants have refused to seriously consider the CPF offer. The complaint seeks a judgment: (1) directing the defendants to give due consideration to any proposed business combination; (2) directing the defendants to assure that no conflicts of interest exist between the directors and their duties to the corporation; (3) awarding the plaintiff the costs and attorneys fees; and (4) granting such other relief as the court deems proper.

On May 8, 2003, the Plaintiff filed a motion for preliminary injunction asking the court to: (1) enjoin indefinitely, until further order of the court, the special shareholders meeting scheduled for May 28, 2003; (2) enjoin enforcement of the Bylaw amendment adopted May 4, 2003 regarding adjournment of shareholders meetings; and (3) enjoin any further amendment to the Parent Company s Bylaws prior to the special shareholders meeting.

On May 23, 2003, the Parent Company announced that the court denied the Plaintiff s motion for a preliminary injunction to halt the Parent Company s May 28 special meeting of shareholders.

On July 14, 2003, Plaintiff filed a First Amended Complaint, in which she updated the complaint s factual allegations to reflect the results of the May 28, 2003 special shareholders meeting and alleged that the Parent Company s Directors had further breached their fiduciary duties by amending the Parent Company s Rights Plan on May 28, 2003.

On February 13, 2004, Plaintiff filed a Second Amended and Supplemental Complaint, in which she included allegations that the Parent Company s Directors had further breached their fiduciary duties by amending the Parent Company s Bylaws and Rights Plan on July 23, 2003 and adopting the 2003 Rights Agreement.

The Parent Company believes the claims are without merit and intends to defend against them vigorously.

CPF Complaints. On May 15, 2003, CPF filed a complaint against the Parent Company in the Circuit Court of the First Circuit, State of Hawaii seeking a temporary restraining order and preliminary injunction to stop the May 28, 2003 shareholders meeting called by the Parent Company to consider matters related to CPF s merger proposal. The suit also asked the court to: (1) declare the meeting in violation of Hawaii law; (2) find the meeting moot because CPF s first offer to the Parent Company had been revoked and withdrawn; and (3) stop the Parent Company from soliciting shareholder proxies for that May 28, 2003 meeting.

On May 16, 2003, the Hawaii State court denied CPF s motion for a temporary restraining order to block the Parent Company from providing its shareholders with proxy material regarding CPF s hostile takeover proposal.

On May 20, 2003, CPF withdrew, without prejudice, its motion for a preliminary injunction to stop the May 28, 2003 special shareholders meeting of the Parent Company.

On May 20, 2003, the Parent Company filed a counterclaim against CPF seeking injunctive and declaratory relief for CPF s violations of the Hawaii Control Share Acquisitions statute. The Parent Company alleges, among other things, that CPF violated Hawaii law by soliciting proxies well in advance of the statutory period - thirty days prior to a scheduled shareholder meeting - and that CPF failed to obtain shareholder approval, as required by statute, prior to acquiring beneficial ownership of more than ten percent of the outstanding shares of stock of the Parent Company.

On June 28, 2003, the Parent Company announced that CPF withdrew all pending legal claims made against the Parent Company regarding the May 28, 2003 special shareholders meeting. The Parent Company also announced that Circuit Court Judge Victoria Marks approved the stipulation dismissing CPF s complaint with prejudice, which means CPF s claims regarding the validity of the May 28 shareholders meeting cannot be re-filed.

On June 30, 2003, CPF filed a motion to dismiss portions of the Parent Company s counterclaim. On August 6, 2003, CPF withdrew its motion to dismiss after the Circuit Court ruled that the Parent Company is entitled to take discovery in support of its remaining claims under the Hawaii Control Share Acquisition statute. On July 30, 2003, CPF filed a second complaint against the Parent Company in Circuit Court of the First Circuit, State of Hawaii seeking to invalidate provisions of the Parent Company s new Rights Plan and bylaws, both adopted on July 23, 2003. CPF also seeks to enjoin the Parent Company from using its Rights Plans and bylaws.

On August 19, 2003, CPF filed a motion for judgment on the pleadings in the Parent Company s counterclaim. CPF argued in the motion that the Hawaii Control Share Acquisitions statute could not be triggered by the voting agreement between CPF and the Parent Company s shareholders and that the statute was unconstitutional. On September 29, 2003, the court rejected CPF s arguments regarding the applicability and constitutionality of the statute and denied CPF s motion for judgment on the pleadings. Thus, the Parent Company s counterclaim remains in the first lawsuit filed by CPF, and was amended on October 31, 2003 to include additional allegations.

On December 18, 2003, CPF filed a counterclaim against the Parent Company and each of the members of the Parent Company s Board of Directors. CPF s counterclaim asks the court to (1) declare that the Parent Company s voting agreement with one of its shareholders, TON Finance, B.V. (TON), constitutes unlawful vote-buying; (2) declare that the Parent Company induced TON to breach its agreement with CPF in a manner constituting tortious interference with contract; (3) enjoin further such conduct by the Parent Company; (3) declare that the Parent

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Company s agreement with TON is null and void; and (4) in the alternative, impose monetary damages. CPF s counterclaim has been served on the Parent Company, but has not yet been served on the members of the Parent Company s Board of Directors.

The parties have commenced the discovery process in both CPF lawsuits, including the production of documents and oral depositions.

The Parent Company s Complaint. On July 22, 2003, the Parent Company announced that it had filed a lawsuit in the Circuit Court of the First Circuit, State of Hawaii against CPF asserting that CPF violated the Hawaii Control Share Acquisitions statute. The lawsuit alleges that CPF illegally formed a voting group with certain shareholders of the Parent Company without obtaining the approval of the Parent Company s shareholders as required by Hawaii law.

On August 19, 2003, CPF filed a motion to dismiss the Parent Company s complaint. CPF argued in the motion that the complaint was duplicative of the Parent Company s counterclaim asserted in the first lawsuit filed by CPF, that the Hawaii Control Share Acquisitions statute could not be triggered by voting agreements or arrangements between CPF and the Parent Company s shareholders, and that the statute was unconstitutional. On September 29, 2003, the court denied the motion to dismiss on the substantive arguments, but granted the motion in part based on procedural grounds, finding similar claims had already been filed in the Parent Company s counterclaim in the first CPF lawsuit. Thus, the Parent Company s lawsuit has been dismissed. However, in its ruling the court specifically granted the Parent Company leave to file an amended counterclaim in the first lawsuit filed by CPF to include all additional allegations made in the Parent Company s complaint. Therefore, all of the allegations made in the Parent Company s lawsuit have been incorporated in the amended counterclaim, which was filed on October 31, 2003.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted during the fourth quarter of 2003 to a vote of security holders through the solicitation of proxies or otherwise.

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Parent Company s common stock is traded on the NASDAQ National Market System under the symbol CBBI . At March 1, 2004, the Parent Company had approximately 3,500 common shareholders of record.

The following table sets forth quarterly high and low bid and dividend information on a per share basis for the Parent Company s common stock over the preceding two years. Common stock prices have been retroactively adjusted to reflect stock dividends:

	High	Low	Dividends
2003			
First quarter	**$45.28**	**$36.68**	**$0.11**
Second quarter	**61.73**	**40.74**	**0.12**
Third quarter	**62.27**	**58.83**	**0.36**
Fourth quarter	**64.50**	**59.61**	**0.36**
2002			
First quarter	$30.23	$27.08	$0.11
Second quarter	35.38	29.73	0.11
Third quarter	35.67	29.70	0.11
Fourth quarter	38.44	31.66	0.11

The Parent Company s ability to pay dividends is limited by certain restrictions generally imposed on Hawaii corporations. The Parent Company may pay dividends out of funds legally available at such times as the Board of Directors determines are appropriate.

The following table details the total number of shares available for issuance under the Company s employee stock-based incentive plans (including shares available for issuance to nonemployee directors). The Company is not authorized to grant stock-based incentive awards to nonemployees other than to nonemployee directors.

	Number of shares to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of shares remaining available for future use under equity compensation plans
December 31, 2003			
Employee stock-based incentive plans approved by shareholders	366,791	$ 36.35	233,650
Employee stock-based incentive plans not approved by shareholders			
Total	366,791		233,650

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ITEM 6. SELECTED FINANCIAL DATA
(dollars in thousands, except per share data)

	2003	2002	2001	2000	1999
Income Statement Data:					
Interest income	**$ 103,010**	$ 106,945	$ 128,254	$ 132,472	$ 111,233
Interest expense	**23,416**	30,292	57,448	71,478	52,717
Net interest income	**79,594**	76,653	70,806	60,994	58,516
Provision for credit losses	**7,180**	17,110	13,628	7,539	4,975
Net interest income after provision for credit losses	**72,414**	59,543	57,178	53,455	53,541
Noninterest income (1)	**23,286**	12,815	2,817	10,024	10,328
Noninterest expense (2)	**64,927**	52,618	50,595	46,679	58,336
Income before income taxes	**30,773**	19,740	9,400	16,800	5,533
Income tax expense	**10,025**	6,258	3,250	5,582	5,227
Net income	**$ 20,748**	$ 13,482	$ 6,150	$ 11,218	$ 306
Cash dividends	**$ 4,015**	$ 1,649	$ 1,441	$ 1,093	$ 931
End of Year Balance Sheet Data:					
Total assets	**$1,903,661**	$1,674,358	$1,586,040	$1,721,602	$1,619,549
Total earning assets	**1,808,940**	1,552,936	1,516,583	1,633,545	1,506,732
Total loans	**1,342,111**	1,162,728	1,243,003	1,301,358	1,152,731
Total deposits	**1,205,725**	1,163,227	1,138,435	1,218,463	1,106,145
Long-term debt	**194,389**	319,407	214,424	181,563	225,140
Stockholders equity	**169,210**	151,009	133,762	123,162	114,691
Average Balances:					
Total assets	**$1,740,967**	$1,574,396	$1,678,679	$1,667,243	$1,491,947
Total earning assets	**1,655,563**	1,496,318	1,598,969	1,583,704	1,391,681
Total loans	**1,211,840**	1,149,685	1,296,279	1,236,305	1,077,769
Total deposits	**1,176,512**	1,133,169	1,193,758	1,154,075	1,082,642
Long-term debt	**282,394**	250,658	235,028	205,877	205,098
Stockholders equity	**159,571**	144,253	128,666	118,132	127,567
Common Stock Data:					
Per share (diluted) (3):					
Net income	**$ 4.72**	$ 3.11	$ 1.43	$ 2.62	$ 0.07
Cash dividends declared	**0.95**	0.44	0.43	0.34	0.27
Book value (at December 31)	**39.35**	39.17	35.07	31.84	29.15
Market price (close at December 31)	**62.61**	42.52	31.67	20.99	23.60
Average shares outstanding	**4,391,516**	4,332,455	4,300,431	4,288,860	4,535,017
Selected Ratios:					
Return on average:					
Total assets	**1.19%**	0.86%	0.37%	0.67%	0.02
Stockholders equity	**13.00**	9.35	4.78	9.50	0.24
Dividend payout ratio	**19.35**	12.23	23.43	9.74	304.25
Average stockholders equity to average total assets	**9.17**	9.16	7.66	7.09	8.55
Year ended December 31:					

Net interest margin (taxable equivalent basis)	**4.86**	5.18	4.48	3.91	4.25
Net loans charged off to average loans	**0.48**	0.82	0.90	0.65	0.45
At December 31:					
Risk-based capital ratios:					
Tier 1	**11.03**	12.19	11.32	12.04	11.95
Total	**12.29**	13.46	12.58	13.29	13.21
Tier 1 leverage ratio	**8.90**	9.03	8.31	8.01	7.69
Allowance for credit losses to total loans	**2.12**	2.33	1.57	1.34	1.56
Nonperforming assets to total loans	**0.44**	1.28	1.65	1.43	1.58
Nonperforming assets to total assets	**0.31**	0.89	1.29	1.08	1.12
Allowance for credit losses to nonperforming loans	**497.38**	213.06	123.24	115.35	152.28

(1) Includes impairment charges on asset-backed securities of $1,399,000 and $10,642,000 incurred in 2002 and 2001, respectively.

(2) Includes unsolicited hostile takeover proposal expenses of $6,621,000 million in 2003, restructuring and merger-related charges of $1,551,000 and the write-off of goodwill of $7,873,000 incurred in 1999.

(3) Common stock data retroactively adjusted for 10% stock dividend paid in 2003, 2002 and 2001.

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

The Company is a bank holding company which wholly owns City Bank, the fourth largest bank with headquarters in the State of Hawaii. The Company s activities are divided into four segments:

Retail banking Retail deposits, mortgage banking and consumer lending activities.

Wholesale banking Wholesale deposits, commercial real estate lending, corporate lending and specialized lending functions of the bank.

Treasury Manages the company s investment securities portfolio and borrowing.

All other Consists of administrative support of the bank, transactions of CB Bancshares, Inc. (the Parent Company) and the subsidiaries of the Parent Company and the bank.

When we use the words the Company, we , us and our , we mean CB Bancshares, Inc. and its consolidated subsidiaries. In the discussion below we have included statements that may constitute forward looking statement within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward looking statements are not historical facts but instead represent only our beliefs regarding future events, many of which, by their nature, are inherently uncertain and beyond our control. These statements relate to our future plans and objectives among other things. By identifying these statements for you in this manner we are alerting to you the possibility that our actual results may differ, possibly materially, from the results indicated in these forward looking statements. Important factors, among others, that could cause our results to differ, possibly materially, from those indicated in the forward looking statements, are discussed under Forward Looking Statements and Certain Factors That May Affect Our Business .

Executive Overview. Our diluted earnings per share were $4.72 for 2003, a 53.9% increase over 2002. Return on average shareholder s equity was 13%. The results in 2003 reflected increasing strength in the economy in the State of Hawaii which impacted the credit condition of our borrowers, reduced our provision for credit losses and permitted us to expand our deposit base. Our results were also aided by increased loan production in the last two quarters from our two California loan production offices which were established last year. Allocated net income for our wholesale banking segment increased by $8.5 million, for our retail banking segment it increased $1.6 million and for our treasury segment it increased $2.6 million, with the allocated net loss for the All Other segment increasing by $5.5 million. The wholesale and retail banking net income increases were primarily due to the decrease in the provision for credit losses, which was due to the increased strength of the economy in the State of Hawaii, a stronger Hawaii real estate market and improvement in loan quality. Our results were negatively affected by $6.6 million in expenses to oppose the unsolicited hostile takeover by CPF which was allocated to the All Other segments. The year showed opportunities for expansion in California loan production and opportunities to expand our deposit base in the State of Hawaii and we are implementing some products and marketing efforts to that end.

Business Environment. Our businesses are materially affected by conditions in the financial markets and economic conditions generally, both in the United States but, particularly, in the State of Hawaii. A favorable business environment is generally characterized by low inflation, low and declining interest rates and strong equity markets. That business market strength and an increase in strength of the Hawaii economy during 2003 and particularly during the last two quarters impacted our results positively. The company faces substantial competition in Hawaii. The market for loans in the State of California reflects an economy that is more broad based than the State of Hawaii. In California, there is substantial competition but we believe we can respond competitively to opportunities to make commercial real estate loans there.

Certain Factors That May Affect Our Business. We face a variety of risks that are inherent in our business including market, liquidity, credit, operational, legal and regulatory risk. A summary of some of the important factors that could affect our business follows.

Market Conditions and Market Risks. Our business is materially affected by conditions in the global financial markets and United States markets and economic conditions generally in Hawaii. Business conditions improved in the second half of 2003 in Hawaii although in previous years there has been a challenging environment. Adverse or uncertain economic or market conditions have in the past adversely affected and may in the future adversely affect our business and profitability by affecting our borrowers and our credit loss provision, our ability to compete, our operational costs and the volatility of interest rates which affect our ability to plan and to maintain our interest rate margins.

Credit Risks. We are exposed to the risk that third parties owing us money, securities or other assets will not perform their obligations. These parties may default on their obligations to us due to bankruptcy, lack of liquidity, operational failure or other reasons. The amount and duration of our credit exposures have increased over the past several years as has the breadth of the entities to which we have credit exposure. Competitive factors we have in various markets have pressured us to extend credit and price more aggressively the credit risks that we take.

Liquidity Risks. Liquidity (i.e. ready access to funds) is essential to our business. Our liquidity can be impaired by an inability to access secured or unsecured debt markets, an inability to access funds from our subsidiaries, or an inability to sell assets. This situation might arise due to circumstances that we may not be able to control such as a general market disruption or operational problem that affects third parties or us. Our ability to sell assets may be impaired if other market participants are seeking to sell similar assets at the same time. We have substantially relied for the last several years upon advances from the FHLB for liquidity for short and long term advances. We continue to access these funds, particularly, to pay off loans from the FHLB as they become due. Our continued access to these or other replacement borrowings at a reasonable cost is essential for our business.

Operational and Infrastructure Risk. Our businesses are highly dependent on our ability to process, on a daily basis, a large number of transactions. A failure in our internal processes, people or systems could lead to, among other consequences, financial loss and reputation damage. In addition, despite the contingency plans we have in place, our ability to conduct business may be adversely impacted by a disruption in the infrastructure that supports our business and the communities in which they are located. This may include a disruption involving electrical, communications, transportation or other services used by the Company or third parties with which we conduct business.

Legal and Regulatory Risk. Legal liability or a significant regulatory action against the Company could have material adverse financial effects or cause reputational harm to the Company, which in turn could harm our business prospects. The Company is subject to a comprehensive regulatory framework, which requires it to spend time and funds in order to comply with regulatory requirements. Any changes to laws impacting the Company could materially affect our business. Also, the outcome of pending litigation could impact the Company.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management s discussion and analysis of its financial condition and results of operations are based upon the Company s consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to its investments, loans and allowance for loan losses, intangible assets, income taxes, contingencies, and litigation. The Company bases its estimates on current market conditions, historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The Company believes the following critical accounting policies require significant judgments and estimates used in the preparation of its consolidated financial statements.

Allowance for Credit Losses. The Company s allowance for credit losses represents management s estimate of probable losses inherent in the loan portfolio. The allowance for credit losses is periodically evaluated for adequacy by management. Factors considered include the Company s loan loss experience, known and inherent risks in the portfolio, current economic conditions, known adverse situations that may affect the borrower s ability to repay, regulatory policies, and the estimated value of underlying collateral. The evaluation of the adequacy of the allowance is based on the above factors along with prevailing economic conditions that may impact borrowers ability to repay loans. Determination of the allowance is in part objective and in part a subjective judgment by management given the information it currently has in its possession. Adverse changes in any of these factors or the discovery of new adverse information could result in higher charge-offs and loan loss provisions.

The Allowance consists of allocated and unallocated allowances. The allocated allowance relates to specific allowances for individual loans, pooled graded loans, and homogeneous loans (consumer loans and residential mortgage loans). The Company has established and adopted a loan grading system in which loans are segregated by risk. Certain graded commercial and commercial real estate loans are analyzed on an individual basis based on performance and collateral. The allocated allowance also includes a percentage factor for pooled graded and homogenous pools of loans taking into account the Bank s historical losses as well as the present condition, expected performance of each pool and risks inherent in loan concentrations in certain industries or categories.

To mitigate imprecision in the estimates of expected credit losses, the allocated component of the allowance is supplemented by an unallocated component. The unallocated allowance is more judgmental and takes into consideration the risks inherent in the loan portfolio, estimation errors, and economic trends or uncertainties that are not necessarily captured in determining allocated allowances.

Impairment of Investments. The realization of the Company s investment in certain mortgage/asset-backed securities and collateralized loan and bond obligations is dependent on the credit quality of the underlying borrowers and yields demanded by the marketplace. Increases in market interest rates and deteriorating credit quality of the underlying borrowers because of adverse conditions may result in impairment charges. The Company records an investment impairment charge when it believes an investment has experienced a decline in value that is other than temporary. Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment s current carrying value, thereby possibly requiring an impairment charge in the future. Since the collateralized loan and bond obligations do not have a liquid trading market, management s estimate of value is based upon estimates of future returns that may or may not actually be realized. Accordingly, under different assumptions, the value could be adversely affected. As of December 31, 2003, approximately $34.8 million of these investments were carried on the books of the Company.

Deferred Tax Assets. The Company records a valuation allowance to reduce its deferred tax assets to the amount that it believes is more likely than not to be realized. This requires an objective as well as subjective evaluation and assessment by management. While the Company has considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event the Company were to determine that it would be able to realize its deferred tax assets in the future in excess of its net recorded amount, an adjustment to the valuation allowance would increase income in the period such determination was made. Likewise, should the Company determine that it would not be able to realize all or part of its net deferred tax asset in the future, an adjustment to the valuation allowance would be charged to income in the period such determination was made.

RESULTS OF OPERATIONS

Consolidated net income for 2003 was $20.7 million, a 53.9% increase over consolidated net income of $13.5 million, from 2002. Diluted earnings per share was $4.72 in 2003, as compared to $3.11 in 2002. All per share amounts have been restated for the effect of stock dividends. The increase was primarily due to a $10.5 million increase in noninterest income and a $9.9 million reduction in provision for credit losses, partially offset by a $12.3 million increase in noninterest expense.

Consolidated net income for the quarter and year ended December 31, 2003 includes $470,000 ($320,000, or $0.08 per share, after tax) and $6.6 million ($4.4 million, or $1.01 per share, after tax), respectively, in expenses associated with the defense of the unsolicited hostile takeover proposal by CPF announced on April 16, 2003.

Net interest income was $79.6 million for 2003, an increase of $2.9 million, or 3.8%, compared to 2002. The increase in net interest income for the year ended December 31, 2003 was due to a $157.6 million increase in the average balance of interest-earning assets,

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partially offset by a $116.7 million increase in the average balance of interest-bearing liabilities and a 32 basis points decline in the net interest margin (to 4.86%).

Noninterest income was $23.3 million for 2003, an increase of $10.5 million, or 81.7%, over 2002. The increase was primarily due to: 1) $1.7 million in net gains on the sale of securities (as compared to a $1.8 million net loss on the sale of securities during the same period in 2002); 2) a $1.5 million increase in revenues from item processing fee income; and 3) a $2.5 million increase in other non-interest income. The increase in other non-interest income was primarily due to $975,000 recorded in connection with an insurance company demutualization distribution in the second quarter of 2003 and $756,000 recorded in connection with a deferred gain on sale of a building (gain recognition criteria was met in the fourth quarter of 2003).

Noninterest expense was $64.9 million for 2003, an increase of $12.3 million, or 23.4%, over 2002. The increase was primarily due to a $5.2 million increase in salaries and employee benefits (higher incentive-based compensation and increase in personnel for mainland loan offices and an item processing center) and $6.6 million ($4.4 million after tax) of expenses related to the unsolicited hostile takeover proposal by CPF announced on April 16, 2003.

The provision for credit losses was $7.2 million, $17.1 million and $13.6 million in 2003, 2002 and 2001, respectively. Net charge-offs to average loans and leases were 0.48%, 0.82% and 0.90% for 2003, 2002 and 2001, respectively. The allowance for credit losses was $28.5 million, or 2.13% of total loans and leases, at December 31, 2003, compared with $27.1 million, or 2.34%, at December 31, 2002. Nonperforming assets totaled 0.31%, 0.89% and 1.29% of total assets as of December 31, 2003, 2002 and 2001, respectively.

At December 31, 2003, the Company s ratios of Tier 1 Capital to risk-weighted assets and Total Capital to risk-weighted assets were 11.03% and 12.29%, respectively, compared with 12.19% and 13.46%, respectively, at December 31, 2002. These ratios were in excess of the well-capitalized ratios of 6.00% and 10.00%, respectively, specified by the FRB.

NET INTEREST INCOME

Net interest income is the largest single component of the Company s earnings and represents the difference between interest income received on loans and other earning assets and interest expense paid on deposits and borrowings. Net interest income, on a taxable equivalent basis, was $80.4 million in 2003, an increase of $2.9 million, or 3.8%, over 2002. During 2003, the Company s net interest margin decreased to 4.86%, compared to 5.18% for 2002.

As summarized on Table 2, the $2.9 million increase in net interest income for 2003 consisted of a $6.9 million decrease in interest expense offset by a $3.9 million decrease in interest income.

The average yield on earning assets in 2003 decreased by 94 basis points to 6.27% and the average balance of earning assets increased by $157.6 million. The $3.9 million decrease in interest income was primarily due to the 74 basis point drop in the loan yield.

In 2003, interest costs on interest-bearing deposits and liabilities decreased to $23.4 million, the average balance of interest-bearing deposits and liabilities increased by $116.7 million and the average cost of funds (total interest divided by the average balance of total interest-bearing liabilities and demand deposits) decreased by 65 basis points to 1.50%. The following table sets forth the condensed consolidated average balance sheets, an analysis of interest income/expense and average yield/rate for each major category of earning assets and interest-bearing deposits and liabilities for the years indicated on a taxable equivalent basis. The taxable equivalent adjustment is made for items exempt from federal income taxes (assuming a 35% tax rate) to make them comparable with taxable items before any income taxes are applied.

Net interest income, on a taxable equivalent basis, was $77.5 million in 2002, an increase of $5.8 million, or 8.2%, from 2001. During 2002, the Company s net interest margin increased to 5.18%, compared to 4.48% for 2001. This increase was due to a 161 basis point decrease in the cost of funds, partially offset by an 86 basis point decrease in the yield on average earning assets.

Average earning assets decreased $102.7 million, or 6.4%, in 2002 as compared to 2001. Average interest-bearing deposits and liabilities decreased $146.1 million, or 10.5%, in 2002 as compared to 2001.

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TABLE 1: DISTRIBUTION OF ASSETS, LIABILITIES AND STOCKHOLDERS EQUITY; INTEREST RATES

(dollars in thousands)	2003 Average Balance	2003 Interest Income/ Expense	2003 Yield/ Rate	2002 Average Balance	2002 Interest Income/ Expense	2002 Yield/ Rate	2001 Average Balance	2001 Interest Income/ Expense	2001 Yield/ Rate
ASSETS									
Earning assets:									
Interest-bearing deposits in other banks	**$ 4,894**	**$ 86**	**1.76%**	$ 1,052	$ 25	2.38%	$ 1,030	$ 54	5.24%
Federal funds sold and securities purchased under agreement to resell	**11,657**	**144**	**1.24**	11,174	162	1.45	9,871	397	4.02
Taxable investment and mortgage/asset-backed securities	**396,457**	**15,599**	**3.93**	303,433	15,449	5.09	260,867	17,538	6.72
Nontaxable investment securities	**30,715**	**2,378**	**7.74**	30,974	2,395	7.73	30,922	2,389	7.73
Loans [(1)]	**1,211,840**	**85,635**	**7.07**	1,149,685	89,752	7.81	1,296,279	108,715	8.39
Total interest-earning assets	**1,655,563**	**103,842**	**6.27**	1,496,318	107,783	7.20	1,598,969	129,093	8.07
Non-interest earning assets:									
Cash and due from banks	**45,444**			35,083			28,835		
Premises and equipment - net	**16,350**			17,226			18,372		
Other assets	**54,022**			49,943			50,999		
Less allowance for loan losses	**(30,412)**			(24,174)			(18,496)		
Total assets	**$1,740,967**			$1,574,396			$1,678,679		
LIABILITIES AND STOCKHOLDERS EQUITY									
Interest-bearing liabilities:									
Savings deposits	**$ 537,517**	**$ 2,949**	**0.55%**	$ 471,314	$ 5,255	1.11%	$ 412,331	$ 8,927	2.17%
Time deposits	**448,399**	**8,186**	**1.83**	504,685	12,843	2.54	651,344	30,511	4.68
Short-term borrowings	**98,357**	**1,158**	**1.18**	23,339	672	2.88	97,428	5,095	5.23
Long-term debt	**282,394**	**11,123**	**3.94**	250,658	11,522	4.60	235,028	12,915	5.50
Total interest-bearing liabilities	**1,366,667**	**23,416**	**1.71**	1,249,996	30,292	2.42	1,396,131	57,448	4.11
Non-interest-bearing liabilities:									
Demand deposits	**190,596**			157,170			130,083		
Other liabilities	**24,133**			22,977			23,799		
Total liabilities	**1,581,396**			1,430,143			1,550,013		
Stockholders equity	**159,571**			144,253			128,666		
Total liabilities and stockholders equity	**$1,740,967**			$1,574,396			$1,678,679		

Net interest income	**80,426**	77,491	71,645
Net interest margin on total earning assets	**4.86%**	5.18%	4.48%
Taxable equivalent adjustment	**(832)**	(838)	(839)
Net interest income	**$ 79,594**	$ 76,653	$ 70,806

(1) Yields and amounts earned include loan fees. Nonaccrual loans have been included in earning assets for purposes of these computations.

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TABLE 2: INTEREST DIFFERENTIAL

(in thousands)	2003 compared to 2002 Increase (Decrease) due to change in: (1) Volume	Rate	Net Change	2002 compared to 2001 Increase (Decrease) due to change in: (1) Volume	Rate	Net Change
Earning assets:						
Interest-bearing deposits in other banks	**$ 91**	**$ (30)**	**$ 61**	$ 1	$ (30)	$ (29)
Federal funds sold and securities purchased under agreements to resell	**7**	**(25)**	**(18)**	52	(287)	(235)
Taxable investment and mortgage/asset-backed securities	**4,736**	**(4,586)**	**150**	2,862	(4,951)	(2,089)
Nontaxable investment securities	**(20)**	**3**	**(17)**	4	2	6
Loans [2]	**4,852**	**(8,969)**	**(4,117)**	(12,294)	(6,669)	(18,963)
Total earning assets	**9,666**	**(13,607)**	**(3,941)**	(9,375)	(11,935)	(21,310)
Interest-bearing liabilities:						
Savings deposits	**738**	**(3,044)**	**(2,306)**	1,277	(4,949)	(3,672)
Time deposits	**(1,432)**	**(3,225)**	**(4,657)**	(6,870)	(10,798)	(17,668)
Short-term borrowings	**2,160**	**(1,674)**	**486**	(3,874)	(549)	(4,423)
Long-term debt	**1,459**	**(1,858)**	**(399)**	859	(2,252)	(1,393)
Total interest-bearing deposits and liabilities	**2,925**	**(9,801)**	**(6,876)**	(8,608)	(18,548)	(27,156)
Increase (decrease) in net interest income (taxable equivalent basis)	**$ 6,741**	**$ (3,806)**	**$ 2,935**	$ (767)	$ 6,613	$ 5,846

(1) The change in interest due to both rate and volume has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

(2) Yields and amounts earned include loan fees. Nonaccrual loans have been included in earning assets for purposes of these computations.

NONINTEREST INCOME

Noninterest income totaled $23.3 million and $12.8 million in 2003 and 2002, respectively. In 2003 there was no impairment charge on asset-backed securities. Net realized gains on sales of securities were $1.7 million in 2003 ($855,000 of which were related to the termination of two interest rate swaps) compared to a net loss of $1.8 million in 2002. Net gains on sales of loans increased to $2.5 million in 2003 from $1.5 million in 2002. Item processing fee income increased to $1.9 million in 2003 from $397,000 in 2002. The increase in other noninterest income was primarily due to $975,000 recorded in connection with an insurance company demutualization distribution in 2003 and $756,000 recorded in connection with a deferred gain on sale of a building (gain recognition criteria was met in 2003).

Total noninterest income increased to $12.8 million in 2002 from $2.8 million in 2001. The impairment charge on asset-backed securities decreased to $1.4 million in 2002 from $10.6 million in 2001. There was a $2.4 million increase in service charges and fees in 2002 as a result of the Company s concerted effort to increase fee income related to deposit and credit products. Net realized losses on sales of securities increased to $1.8 million in 2002 from $169,000 in 2001. Net gains on sales of loans decreased to $1.5 million in 2002 from $2.1 million in 2001.

The following table sets forth information by category of noninterest income for the years indicated:

(in thousands)	2003	2002	2001

Service charges on deposits	**$ 4,559**	$ 4,345	$ 3,811
Other service charges and fees	**7,147**	6,784	4,897
Net realized gains (losses) on sales of securities	**1,718**	(1,765)	(169)
Net gains on sales of loans	**2,533**	1,493	2,060
Earnings on bank-owned life insurance	**1,989**	1,762	1,359
Item processing fee income	**1,866**	397	135
Impairment on asset-backed securities		(1,399)	(10,642)
Other	**3,474**	1,198	1,366
Total	**$23,286**	$12,815	$ 2,817

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PROVISION AND ALLOWANCE FOR CREDIT LOSSES

The following table summarizes changes in the allowance for credit losses for the years indicated:

(dollars in thousands)	2003	2002	2001	2000	1999
Balance at beginning of year	$27,123	$19,464	$17,447	$17,942	$17,771
Charge-offs:					
Commercial and financial	2,751	6,901	9,052	3,138	442
Real estate mortgage	3,602	1,353	2,034	4,378	4,085
Installment and consumer	5,402	5,043	1,342	1,490	896
Total charge-offs	11,755	13,297	12,428	9,006	5,423
Recoveries:					
Commercial and financial	2,541	924	108	170	94
Real estate mortgage	1,219	1,175	399	537	314
Installment and consumer	2,182	1,747	310	265	211
Total recoveries	5,942	3,846	817	972	619
Net loans charged-off	5,813	9,451	11,611	8,034	4,804
Provision for credit losses	7,180	17,110	13,628	7,539	4,975
Balance at end of year	$28,490	$27,123	$19,464	$17,447	$17,942
Net charge-offs to average loans outstanding	0.48%	0.82%	0.90%	0.65%	0.45%
Allowance for credit losses to year-end loans	2.12%	2.33%	1.57%	1.34%	1.56%
Allowance for credit losses to year-end nonperforming loans	497.38%	213.06%	123.24%	115.35%	152.28%

The provision for credit losses is based upon periodic evaluations by management as to the adequacy of the allowance for credit losses. In these evaluations, management considers numerous factors including, but not limited to, global, national and local economic conditions, loan portfolio composition, loan loss experience and management s estimate of potential losses. These various analyses lead to a determination of the amount needed in the allowance for credit losses. To the extent the existing allowance is below the amount so determined, a provision is made that will bring the allowance to such amount. Thus, the provision for credit losses may fluctuate and may not be comparable from year to year. Factors affecting the components of the allowance for credit losses and the related provision for credit losses are discussed below.

Provision for credit losses was $7.2 million, $17.1 million and $13.6 million in 2003, 2002 and 2001, respectively. The Company s allowance for credit losses increased to $28.5 million at December 31, 2003, from $27.1 million at December 31, 2002 and $19.5 million at December 31, 2001. The allowance for credit losses as a percentage of total loans was 2.13% at December 31, 2003, compared to 2.34% and 1.57% at December 31, 2002 and 2001, respectively. Allowance for credit losses as a percentage of nonperforming loans increased to 497.38% at December 31, 2003 compared to 213.06% and 123.24% at December 31, 2002 and 2001, respectively. The Company s lower provision in 2003 reflects the reduction in non-performing loans, improvement in asset quality and the stronger Hawaii economy as well as elimination of uncertainties concerning the impact of hostilities in Iraq upon the tourism industry.

Net loans charged-off were $5.8 million in 2003, a decrease of $3.6 million from the $9.5 million in 2002. Commercial and financial net charged-off decreased by $5.8 million in 2003 over 2002.

The net investment in loans that were considered to be impaired was $5.4 million at December 31, 2003, a decrease of $6.9 million from the $12.3 million at December 31, 2002. Additional information on impaired loans is presented in Note D of Notes to the Company s Consolidated Financial Statements.

The Company s allowance for credit losses represents management s estimate of probable losses inherent in the loan portfolio. The allowance for credit losses is periodically evaluated for adequacy by management. Factors considered include the Company s loan loss experience, known and inherent risks in the portfolio, known adverse situations that may affect the borrower s ability to repay, regulatory policies, and the estimated value of underlying collateral. The evaluation of the adequacy of the allowance is based on the above factors along with prevailing economic conditions that may impact borrowers ability to repay loans. The determination of the allowance is in part objective and in part a subjective assessment by management given the information it currently has in its possession. Adverse changes in any of these factors or the discovery of new adverse information could result in higher charge-offs and loan loss provisions.

The Allowance consists of allocated and unallocated allowances. The allocated allowance relates to specific allowances for individual loans, pooled graded loans, and homogeneous loans (consumer loans and residential mortgage loans). The Company has established and adopted a loan grading system in which loans are segregated by risk. Certain graded commercial and commercial real estate loans are analyzed on an individual basis based on performance and collateral. The allocated allowance also includes a percentage factor for homogenous pools of loans taking into account the Bank s historical losses as well as the present condition, expected performance of each pool and risks inherent in loan concentrations in certain industries or categories.

To mitigate imprecision in the estimates of expected credit losses, the allocated component of the allowance is supplemented by an unallocated component. The unallocated allowance is more judgmental and takes into consideration the risks inherent in the loan portfolio, estimation errors, and economic trends or uncertainties that are not necessarily captured in determining allocated allowances.

There were no material changes in the allowance methodology in 2003 or cross border credits affecting the allowance calculation.

At December 31, 2003, the allowance for loan losses was $28.5 million, or 2.12% of total loans, an increase of $1.4 million over the $27.1 million, or 2.33% of total loans, at December 31, 2002. The components of the allowance, allocated and unallocated, are shown in the table below. The allocated component increased to $25.8 million at December 31, 2003 from $24.6 million at December 31, 2002, while the unallocated component increased to $2.7 million at December 31, 2003 from $2.5 million at December 31, 2002.

Certain changes in loan concentrations, credit quality, terms, and other factors affecting the allocated allowance for credit losses at December 31, 2003 are noted below:

Commercial and financial loans balances increased by $18.1 million in 2003 to $245.9 million from $227.7 million in 2002. Non-performing commercial and financial loans declined by $1.9 million in 2003 to $3.3 million from $5.2 million in 2002. As a result of the improvement in asset quality, the allocated allowance for commercial and financial credits declined by $1.2 million to $14.1 million from $15.3 million in 2002.

Real estate construction loan balances increased by $45.7 million in 2003 to $98.2 million from $52.5 million in 2002. This resulted in a $664,000 increase in allocated allowance for real estate construction loans.

Real estate residential loans declined to $367.7 million in 2003, a decrease of $76.6 million from the $444.2 million in 2002. The decrease in outstanding loan balances resulted in a $636,000 reduction in allocated allowance for real estate residential loans to $1.1 million in 2003, from $1.8 million in 2002.

Real estate commercial loan balances increased to $403.9 million, an increase of $193.4 million over $210.5 million in 2002. Non-performing loans in this category declined to $708,000, a decrease of $3.4 million from the $4.2 million in 2002. The aggregate effect of these factors was an increase in the allocated allowance for real estate commercial credits to $4.9 million from $4.7 million in 2002.

Installment and consumer loan balances increased by $44.6 million in 2003 to $180.1 million. Estimated credit loss factors on installment and consumer loans were increased due to the higher losses in this loan category. The aggregate effect of these factors was an increase in the allocated allowance to $4.2 million, an increase of $2.3 million over 2002.

The unallocated allowance for credit losses at December 31, 2003 was $2.7 million, an increase over the $2.5 million in 2002. The unallocated balance reflects risks inherent in the loan portfolio, estimation errors, and economic trends or uncertainties that are not necessarily captured in determining allocated allowances. In management s judgment, the allowance for credit losses was adequate to absorb potential losses currently inherent in the loan portfolio at December 31, 2003. However, changes in prevailing economic conditions in the Company s markets or in the financial condition of its customers could alter the level of nonperforming assets and charge-offs in the future and, accordingly, affect the allowance for credit losses.

The allowance for credit losses has been allocated by the Company s management according to the amount deemed to be reasonably necessary to provide for the possibility of loan losses being incurred within the following categories of loans at December 31 for the years indicated:

(dollars in thousands)	2003 Amount	2003 % (1)	2002 Amount	2002 % (1)	2001 Amount	2001 % (1)	2000 Amount	2000 % (1)	1999 Amount	1999 % (1)
Commercial & Financial	**$14,063**	**18.97%**	$15,250	21.27%	$11,208	19.19%	$10,303	19.40%	$ 7,359	19.55%
Real estate Construction	**1,555**	**7.58**	891	4.91	487	4.41		2.06		1.31
Real estate Residential	**1,114**	**28.37**	1,750	41.50	2,262	49.15	2,634	54.45	4,000	54.04
Real estate Commercial	**4,884**	**31.18**	4,740	19.67	2,594	15.90	2,121	15.10	3,680	17.12
Installment & Consumer	**4,219**	**13.90**	1,952	12.65	860	11.35	483	9.00	1,432	7.97

Unallocated	**2,655**	**n/a**	2,540	n/a	2,053	n/a	1,906	n/a	1,471	n/a
Total	**$28,490**	**100.00%**	$27,123	100.00%	$19,464	100.00%	$17,447	100.00%	$17,942	100.00%

(1) Represents percentage of loans in each category to total loans.

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NONINTEREST EXPENSE

The following table sets forth information by category of noninterest expense for the years indicated:

(dollars in thousands)	2003	2002	2001
Salaries and employee benefits	**$29,852**	$24,675	$23,111
Net occupancy expense	**6,639**	6,367	6,588
Unsolicited hostile takeover proposal expenses	**6,621**		
Legal and professional fees	**4,599**	4,740	4,147
Advertising and promotion	**2,611**	2,716	2,997
Equipment expense	**2,406**	2,942	3,469
Stationery, supplies, postage and delivery	**2,317**	2,070	1,867
Deposit insurance premiums	**198**	201	227
Provision for other real estate owned losses	**176**	500	150
Other	**9,508**	8,407	8,039
Total	**$64,927**	$52,618	$50,595
Efficiency ratio	56.41%	57.37%	59.33%

Noninterest expense increased $12.3 million, or 23.4%, in 2003, as compared to 2002. The Company s efficiency ratio decreased to 56.41% in 2003, as compared to 57.37% in 2002.

The Company incurred $6.6 million in expenses associated with the defense of the unsolicited hostile takeover proposal by CPF announced on April 16, 2003. Among other things, such expenses included attorneys fees, special shareholders meeting expenses, solicitation costs and other related expenses.

Salaries and employment benefits increased by $5.2 million, or 21.0%, in 2003, to $29.9 million, compared to $24.7 million in 2002. The increase in salaries and employee benefits over 2002 was due to higher incentive-based compensation in 2003 and an increase in personnel for the mainland loan offices and an item processing center.

Net occupancy expense was $6.6 million in 2003, which compares to $6.4 million in 2002. The increase in net occupancy expense in 2003 was primarily attributable to new branch locations.

Total noninterest expense increased $2.0 million, or 4.0%, in 2002, as compared to 2001. The primary reason for the increase in noninterest expense was the $1.6 million increase in salaries and employment benefits.

INCOME TAXES

Total income tax expense of the Company was $10.0 million, $6.3 million and $3.3 million in 2003, 2002 and 2001, respectively. The corresponding effective income tax rate was 32.6%, 31.7% and 34.6%, respectively. The significant decline in the effective tax rate in 2003 and 2002 as compared to 2001 was primarily due to the utilization of state investment tax credits. Note L of Notes to the Company s Consolidated Financial Statements presents a reconciliation of the Company s effective and statutory income tax rates.

SEGMENT DISCUSSION

The Company s business segments are Retail Banking, Wholesale Banking, Treasury and All Others. Retail Banking is made up of retail deposits, mortgage banking and consumer lending activities. Wholesale Banking consists of wholesale deposits, commercial real estate lending, corporate lending and the specialized lending functions of the Bank. The Treasury segment is responsible for managing the Company s interest rate risk, investment securities portfolio and borrowing. The All Other segment consists of the administrative support of the Bank, transactions of CB Bancshares, Inc. (the Parent Company), and subsidiaries of the Parent Company and Bank. See Note V of Notes to the Consolidated Financial Statements for financial information on segments.

Retail banking net interest income is made up of interest income from revolving real estate, residential real estate and consumer loans, partially offset by the interest expense on retail deposits. Wholesale banking net interest income is made up of interest income from commercial, real estate construction, and commercial real estate loans, partially offset by the interest expense on wholesale deposits. Treasury net interest income is derived from the interest income on investment securities, partially offset by the interest expense on short- and long-term borrowings.

Intersegment net interest income is allocated based on the net funding needs of each segment and applying an interest credit or charge based on an internal cost of capital. Other operating income and expense is the non-interest income and expense designated to Retail Banking, Wholesale Banking, Treasury, and All Other. Administrative overhead allocates the non-interest income and expense from the All Other non-banking function segment to the other three segments, Retail Banking, Wholesale Banking and Treasury.

Assets are composed of cash, investments, loans, premises and equipment and other assets. Loan balances and any corresponding allowance for credit losses are allocated based on loan product types. Premises and equipment are allocated by location and function within the Company.

The Company continues to enhance its segment reporting process methodologies for assigning balance sheet and income statement items to the appropriate operating segment. This process is dynamic and, unlike financial accounting, there is no comprehensive, authoritative guidance for management accounting equivalent to generally accepted accounting principles. The Company defines its segments by product and service type.

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Allocated net income for the Retail Banking segment increased by $1.1 million, or 6.8%, in 2003 as compared to 2002. This was primarily due to decreases in the provision for credit losses of $1.5 million, or 50.1%, and decrease in noninterest expense of $3.6 million, or 22.7%, partially offset by a $2.7 million, or 6.4%, decline in net interest income.

Allocated net income for Wholesale Banking increased by $8.5 million, or 286.4%, in 2003 as compared to 2002. This was primarily due to decreases in the provision for credit losses of $7.6 million, or 54.1%, and an increase in net interest income of $5.5 million, or 18.7%, partially offset by decreases in intersegment net interest expense of $606,000, or 22.8%, and noninterest expense of $1.7 million, or 14.0%.

Allocated net income for Treasury increased by $2.6 million, or 179.5%. This was primarily a result of a decrease in noninterest expense of $3.7 million, or 90.1%, partially offset by the decrease in intersegment net interest income of $178,000, or 8.6%, in 2003 compared to 2002.

Allocated net loss for the All Other segment increased by $5.5 million, or 432.9%. This was primarily the result of an increase in non-interest expense of 41.6% (due primarily to the $6.6 million hostile takeover proposal expenses), partially offset by an increase in the administrative overhead expense allocation of 15.5%.

LOAN PORTFOLIO

Total loans at December 31, 2003 increased to $1,295.8 million, a $225.4 million, or 21.1%, increase from the previous year-end. The increase in total loans was primarily due to an increase in commercial mortgage loans.

The amount of loans outstanding at December 31 for the years indicated are shown in the following table categorized as to types of loans:

(in thousands)	2003	2002	2001	2000	1999
Commercial and financial	**$ 245,875**	$ 227,736	$ 229,885	$ 246,877	$ 224,660
Real estate construction	**98,237**	52,538	52,750	26,237	15,096
Real estate residential mortgage	**367,685**	444,246	588,525	693,068	621,200
Real estate commercial mortgage	**403,946**	210,512	190,328	192,194	196,810
Installment and consumer	**180,064**	135,415	135,901	114,562	91,647
	$1,295,807	$1,070,447	$1,197,388	$1,272,938	$1,149,413

Commercial and financial. Loans outstanding in this category comprise 19.0% of total loans, or $245.9 million, an increase of $18.1 million, or 8.0%, above year-end 2002. Loans in this category are primarily loans to small- and medium-sized businesses and professionals doing business in Hawaii. Cash flow from the borrower s business is typically regarded as the principal source of repayment, although the Bank s underwriting policy and practice generally requires collateral as an additional source of repayment, including real estate, where possible, as well as equipment, receivables and personal assets or guarantees as deemed necessary. Risks of credit losses are greater in this loan category relative to other secured loans, such as commercial and residential mortgages, where, generally, a greater percentage of the loan amount is covered by collateral. Any collateral or guarantees obtained mitigates such risk.

Real estate construction. Loans in this category comprise 7.6% of total loans, or $98.2 million, an increase of $45.7 million, or 87.0%, above year-end 2002. For construction loans, each project is evaluated independently for economic viability, while maximum loan-to-value ratios of 80% are generally required. A construction loan poses higher credit risks than a typical secured loan due to the risk that the project will not be completed on time and within budget. Consideration of the ability and reputation of the developer and monitoring of a project during the construction phase are undertaken to mitigate the increased risk in construction lending.

Real estate residential mortgage. Loans in this category comprise 28.4% of total loans, or $367.7 million, at December 31, 2003, a decrease of $76.6 million, or 17.2%, below year-end 2002. The decreasing balances are primarily the result of the low interest rate environment which provides an incentive to borrowers to refinance existing loans at lower rates. Prepayments are expected to continue until interest rates increase to the point that refinance activity is not cost-effective for borrowers. The Bank allows a maximum loan-to-value ratio of 80% for residential mortgage loans, although higher levels are permitted with mortgage insurance. First mortgage loans secured by residential properties typically represent a moderate credit risk and the improved residential real estate market is expected to have a positive effect on credit losses. Mortgage loans on one-to-four family residential loans have the lowest credit risk and amounted to $340.1 million at December 31, 2003. Additional information on residential mortgage loans at December 31, 2003 is presented below:

(dollars in thousands)	At December 31, 2003	Weighted Average Coupon	Weighted Average Maturity
Fixed	$175,880	7.30%	21.4 years
Adjustable	191,805	5.46%	25.0 years
	$367,685		

Real estate commercial mortgage. Loans in this category comprise 31.3% of total loans, an increase of $193.4 million, or 91.9%, from year-end 2002. These loans consist primarily of loans secured by office and industrial buildings and warehouses located in Hawaii and California. Loans secured by commercial property carry a greater risk than loans secured by residential property as they

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are typically less marketable than residential properties, have rental income risk and are subject to market and interest rate conditions. The Bank utilizes property inspections, rental projections and analysis of market conditions to mitigate risk in these loans.

Installment and consumer. Loans in this category comprise 13.9% of total loans, or $180.1 million, an increase of $44.6 million, or 33.0%, from year-end 2002, and consist primarily of automobile and other revolving consumer credits, including home equity lines of credit. For consumer loans, credit risk is managed on a pooled basis including an evaluation of the quality, character and inherent risks in the loan portfolio, current economic conditions, and past loan loss experience. Consumer loans represent a moderate credit risk. However, the average loan size is modest and risk is diversified among many borrowers and credit profiles. The Bank utilizes credit-scoring systems for most of its consumer loans which offer the ability to modify credit exposure based on the Bank s risk tolerance and loss experience.

Maturities and Sensitivities of Loans to Changes in Interest Rates

The following table shows the contractual maturities of the Company s loan portfolio by category (excluding real estate-mortgage and installment and consumer) at December 31, 2003. Demand loans are included as due within one year:

(in thousands)	Within 1 year	After 1 but Within 5 years	After 5 years	Total
Commercial and financial	$ 88,335	$123,601	$33,939	$245,875
Real estate construction	32,340	65,422	475	98,237
	$120,675	$189,023	$34,415	$344,112

The following table sets forth the interest rate sensitivity of the above amounts due after one year at December 31, 2003:

(in thousands)	Fixed Rate	Variable Rate	Total
After 1 but within 5 years	$127,957	$61,065	$189,022
After 5 years	34,282	133	34,415
	$162,239	$61,198	$223,437

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RISK ELEMENTS IN LENDING ACTIVITIES

Nonperforming (nonaccrual) assets and past due and restructured loans at December 31 are reflected below for the years indicated:

(dollars in thousands)	2003	2002	2001	2000	1999
Nonperforming loans:					
Commercial	**$3,264**	$ 5,190	$ 7,034	$ 6,268	$ 1,831
Real estate:					
Commercial	**708**	4,152	2,438	3,030	518
Residential	**1,756**	3,219	6,174	5,827	8,992
Total real estate loans	**2,464**	7,371	8,612	8,857	9,510
Consumer		169	148		441
Total nonperforming loans	**5,728**	12,730	15,794	15,125	11,782
Other real estate owned	**173**	2,193	4,674	3,458	6,385
Total nonperforming assets	**$5,901**	$14,923	$20,468	$18,583	$18,167
Past due loans:					
Commercial	**$**	$	$	$ 975	$ 96
Real estate	**213**	72	2,190	473	3,481
Consumer	**728**	860	1,464	1,256	592
Total past due loans [(1)]	**$ 941**	$ 932	$ 3,654	$ 2,704	$ 4,169
Restructured loans:					
Commercial	**$**	$	$ 2,214	$ 4,153	$ 4,440
Real estate:					
Commercial					1,231
Residential	**1,413**	2,919	8,629	11,730	11,280
Total restructured loans [(2)]	**$1,413**	$ 2,919	$10,843	$15,883	$16,951
Nonperforming assets to total loans and other real estate owned (end of year):					
Excluding 90 days past due accruing loans	0.44%	1.28%	1.64%	1.42%	1.57%
Including 90 days past due accruing loans	0.51%	1.36%	1.93%	1.63%	1.93%
Nonperforming assets to total assets (end of year):					
Excluding 90 days past due accruing loans	0.31%	0.89%	1.29%	1.08%	1.12%
Including 90 days past due accruing loans	0.36%	0.95%	1.52%	1.24%	1.38%

(1) Represents loans which are past due 90 days or more as to principal and/or interest, are still accruing interest and are in the process of collection.

(2) Represents loans which have been restructured, are current and still accruing interest.

Nonperforming loans decreased to $5.7 million at December 31, 2003, a decrease of $7.0 million, or 55.0%, below the $12.7 million at year-end 2002. The decrease in nonperforming loans was primarily due to a $4.9 million decrease in real estate loans. At December 31, 2003, other real estate owned (net of valuation allowance) amounted to $173,000, a decrease of $2.0 million, or 92.1%, from the prior year-end.

Past due loans which are still accruing interest increased $9,000, to $941,000 at December 31, 2003. Substantially all loans in this category are both well-collateralized and in the process of collection.

Restructured loans decreased $1.5 million, or 51.6%, as compared to 2002, primarily due to pay-off of certain residential loans.

Interest on non-accrual loans that would have been recorded in 2003 had such loans been performing in accordance with their original terms was $448,000. The amount of interest on non-accrual loans that was included in net income in 2003 was $138,000.

At December 31, 2003, the Company was not aware of any significant potential problem loans (not otherwise classified as nonperforming or past due) where possible credit problems of the borrower caused management to have serious concerns as to the ability of such borrower to comply with the present loan repayment terms.

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DEPOSITS

The Company competes for deposits in Hawaii principally by providing quality customer service at its branch offices.

The Company has a network of 22 branch offices which seek to provide a stable core deposit base. The deposit base provided by these branches consists of interest- and noninterest-bearing demand and savings accounts, money market certificates and time certificates of deposit.

The average daily amount of deposits and the average rate paid on such deposit categories is summarized below:

(dollars in thousands)	2003 Amount	Rate	2002 Amount	Rate	2001 Amount	Rate
Noninterest-bearing demand deposits	**$ 190,596**	**%**	$ 157,170	%	$ 130,083	%
Interest-bearing demand deposits	**285,506**	**0.41**	285,480	1.08	256,882	2.29
Savings	**252,011**	**0.71**	185,834	1.17	155,449	1.97
Time deposits	**448,399**	**1.83**	504,685	2.54	651,344	4.68
Total	**$1,176,512**	**0.95%**	$1,133,169	1.60%	$1,193,758	3.30%

The remaining maturities of time deposits in amounts of $100,000 or more outstanding at December 31, 2003 is summarized below:

(in thousands)	
3 months or less	**$110,397**
Over 3 months through 6 months	**51,850**
Over 6 months through 12 months	**29,576**
Over 12 months	**18,684**
Total	**$210,507**

INVESTMENT AND MORTGAGE-BACKED SECURITIES PORTFOLIO

The following table sets forth the book value and the distribution by category of investment securities at December 31 for the years indicated:

(in thousands)	2003	2002	2001
Held-to-Maturity			
U.S. Treasury and other U.S. government agencies and corporations	**$ 79,126**	$ 75,996	$
Corporate bonds	**29,199**	34,861	24,830
Mortgage-backed securities	**25,838**	1,156	1,170
Total	**$134,163**	$112,013	$ 26,000
Available-for-sale			
U.S. Treasury and other U.S. government agencies and corporations	**$ 50,457**	$ 5,462	$ 5,450
State and political subdivisions	**35,167**	35,036	33,204
Mortgage/asset-backed securities	**195,970**	168,371	164,909

Others	**21,052**	19,466	
Total	**$302,646**	$228,335	$203,563
FHLB stock	**$ 31,576**	$ 29,886	$ 32,406

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The following table sets forth the maturities of investment securities (at amortized cost) at December 31, 2003 and the weighted average yields of such securities (calculated on the basis of the cost and effective yields weighted for the scheduled maturity of each security, not adjusted to a fully tax-equivalent basis as impact, not material):

(dollars in thousands)	Within 1 year Amount	Within 1 year Yield	After 1 but within 5 years Amount	After 1 but within 5 years Yield	After 5 but within 10 years Amount	After 5 but within 10 years Yield	After 10 years Amount	After 10 years Yield
Held-to-maturity								
U.S. Treasury and other U.S. government agencies and corporations	$	%	$53,757	2.31%	$ 25,369	2.38%		%
Corporate bonds	18,925	4.59	10,274	4.13				
Mortgage-backed securities							25,838	3.95
Total	$18,925	4.59%	$64,031	2.98%	$ 25,369	2.38%	$ 25,838	3.95%
Available-for-sale								
U.S. Treasury and other U.S government agencies and corporations	$ 5,005	6.31%	$44,507	5.53%	$	%	$	%
State and political subdivisions					11,955	6.07	20,703	5.01
Mortgage/asset-backed securities	572	7.25	741	8.04	90,276	3.36	97,592	5.94
Other							20,906	3.27
Total	$ 5,577	6.41%	$45,248	5.54%	$102,231	3.58%	$139,201	5.40%

A table setting forth information regarding investment and mortgage/asset-backed securities, including estimated fair value and carrying value of such securities is included in Note B of Notes to the Company s Consolidated Financial Statements.

SHORT-TERM BORROWINGS AND LONG-TERM DEBT

Federal funds purchased generally mature on the day following the date of purchase.

Advances from the FHLB were made under a credit line agreement providing for advances up to $570.1 million, of which $70.7 million was undrawn at December 31, 2003. See Notes H and I of Notes to the Company s Consolidated Financial Statements and the discussions below under Liquidity Management.

At December 31, 2003, there were seven long-term FHLB advances totaling $123.0 million, callable after initial lockout periods. The next call date range is between January 2004 and August 2006.

FINANCIAL CONDITION

Total assets at December 31, 2003 were $1,903.7 million, an increase of $229.3 million, or 13.7%, from 2002. The increase was due primarily to increases in investment securities available for sale and loans of $74.3 million, or 32.5% and $218.6 million, or 21.1%, respectively. These increases were a result of cash flows generated from a decrease in loans held for sale of $42.1 million, or 42.7% and an increase in deposits of $42.5 million, or 3.7%, and an increase in borrowings of $170.0 million, or 51.5%.

LIQUIDITY AND CAPITAL RESOURCES

The primary objective of liquidity management is to maintain a balance between sources and uses of funds in order that the cash flow needs of the Company are met in the most economical and expedient manner. The liquidity needs of a financial institution require the availability of cash to meet the withdrawal demands of depositors and the credit commitments of borrowers. In order to optimize liquidity, management monitors and forecasts the various sources and uses of funds in an effort to continually meet the financial requirements of the Company and the financial needs of its customer base.

To ensure liquidity on a short-term basis, the Company s primary sources are cash or cash equivalents, loan repayments, proceeds from the sale of assets available for sale, increases in deposits, proceeds from maturing securities and, when necessary, federal funds purchased, brokered deposits and credit arrangements with correspondent banks and the FHLB. Maturities of investment securities are also structured to cover large commitments and seasonal fluctuations in credit arrangements.

At December 31, 2003, the Bank had advances outstanding from the FHLB of $499.4 million (28.8% of total liabilities) at December 31, 2003 compared to $329.4 million (21.6% of total liabilities) at December 31, 2002. The maximum amount of advances from the FHLB that the Bank had outstanding at any month-end during such periods was $499.4 million. As of December 31, 2003, the Bank had available unused credit lines of $70.7 million from the FHLB. During 2004, $305.0 million of short-term and $31.2 million of long-term borrowings from the FHLB mature see Note I of Notes to the Company s Consolidated Financial Statements for future maturity of long-term borrowings from the FHLB. It has been the Company s general practice to satisfy maturing obligations to the FHLB in part by additional advances under its credit line agreement with the FHLB. The creditline agreements have standard FHLB default provisions which, among other matters, accelerate the maturity date if there is a material adverse change to the financial condition of the Bank and/or if repayment ability becomes impaired. The Bank s ability to continue to draw upon this credit line and avoid an acceleration of the maturity dates is dependent upon the Company s continued adequate financial condition and fulfillment of collateral requirements. As of December 31, 2003, these borrowings were collateralized by $686.3 million in U.S. Treasury and other U.S. government agency securities and loans. Management believes that the FHLB will continue to extend borrowings to the Bank to refinance advances maturing in 2004. In the remote case that the FHLB ceases to make advances available as a reliable source of liquidity, the Bank would be required to repay the advances as they mature or are accelerated from other sources of funds in order to mitigate the risk that the security pledged as collateral for the advances might be realized upon by the FHLB. Management believes that the Bank could obtain other sources of funding, such as through repurchase agreements, brokered CDs, federal fund lines with other correspondent banks or lines of credit with the Federal Reserve System in order to meet such repayment requirements.

The Company s most liquid assets are cash, interest bearing deposits, Federal funds sold, investment securities available for sale and loans held for sale. The levels of these assets are dependent on the Company s operating, financing, lending and investing activities during any given period. At December 31, 2003, cash, interest-bearing deposits, Federal funds sold and available for sale investment securities and loans held for sale totaled $407.0 million, a decrease of 3.8% from $423.1 million at December 31, 2002.

Investing activities used cash flow of $84.7 million in 2003, while providing cash flow of $27.1 million and $124.4 million in 2002 and 2001, respectively. The primary use of cash for investing activities in 2003 was the $230.1 million in net loan originations, partially offset by proceeds from sales of available-for-sale securities of $179.4 million. The primary source of cash for investing activities in 2002 was proceeds from sales and maturities of available-for-sale securities of $113.5 million and net loan payoffs of $117.1 million.

Financing activities provided cash flow of $209.9 million and $62.2 million in 2003 and 2002, respectively, and used $149.4 million in 2001. During 2003, proceeds from short-term debt of $295.0 million were the primary source of cash flows from financing activities and, in 2002; proceeds from long-term debt of $140.0 million were the primary source of cash flows from financing activities.

At any time, the Company has outstanding commitments to extend credit. See Note O of Notes to the Company s Consolidated Financial Statements. See Note N of Notes to the Company s Consolidated Financial Statements for further discussion and disclosure of risk management activities.

OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of business, the Company is a party to various financial transactions that are not recorded on the Company s balance sheet, in accordance with generally accepted accounting principles. Such transactions are structured to meet the financial needs of customers and manage the Company s interest rate risk, and include transactions such as interest rate lock commitments and forward sales of securities, and derivative financial instruments such as swaps, caps, floors, and options. Management is not aware of any known event, demand, commitment, trend or uncertainty that will result in or is reasonably likely to result in the termination or material reduction in availability of these off-balance sheet arrangements. See Notes A, Derivative Instruments and Hedging Activities, and N of Notes to the Company s Consolidated Financial Statements for further discussion on Derivative Instruments and Hedging Activities, and Risk Management Activities.

During 2003, swaps and call options resulted in a net gain of $1.5 million. Based on the off-balance sheet arrangements with which it is involved, the Company does not believe that such arrangements are reasonably likely to have a material impact on its current or future financial condition, results of operations, liquidity or capital.

CONTRACTUAL OBLIGATIONS

Set forth below is a summary of Contractual Obligations as of December 31, 2003 on total payments due during the indicated periods for the specified obligations. Additional information on operating leases and long-term debt can be found in Notes F and I of Notes to the Company s Consolidated Financial Statements.

(in thousands)	Within 1 year	2 to 3 years	4 to 5 years	After 5 years	Total
Long-term debt	$31,200	$40,000	$13,000	$110,189	$194,389
Operating leases	4,470	8,238	7,694	9,762	30,164
Facilities management services	1,164	2,632	2,793	1,710	8,299
Minority interest in consolidated subsidiary				2,720	2,720
Total contractual obligations	$36,834	$50,870	$23,487	$124,381	$235,572

At any time, the Company has a significant number of outstanding commitments to extend credit. These commitments take the form of approved lines of credit and loans with terms of up to one year. The Company also provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements generally extend for up to one year. The contractual amounts of these credit-related instruments are set out in the following table by category of instrument. Because many of those instruments expire without being advanced in whole or in part, the amounts do not represent future cash flow requirements.

(in thousands)	Within 1 year
Loan commitments	$391,394
Guarantees and letters of credit	16,147
Totals	$407,541

The Company did not have material commitment for capital expenditures at December 31, 2003.

UNSOLICITED TAKEOVER PROPOSAL

CPF has not withdrawn its unsolicited takeover proposal and continues to litigate and states that it intends to proceed with such takeover. In 2003, the Company expended approximately $6.6 million in unsolicited hostile takeover proposal expenses. It is unknown as to what expenses and expenditure of time of personnel the Company will incur in the future for this matter, whether CPF will withdraw its proposal or what the result of such proposal will be. These uncertainties could affect the financial performance of the Company and the price at which the shares of the Company trade.

EFFECTS OF INFLATION

The financial statements and related data presented herein have been prepared in accordance with generally accepted accounting principles which require the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. Virtually all of the assets and liabilities of the Company are monetary in nature. As a result, interest rate changes have a more significant impact on the Company s performance than the effects of general levels of inflation.

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QUARTERLY RESULTS OF OPERATIONS (Unaudited)

Net income for the fourth quarter of 2003 was $6.9 million, or $1.56 per diluted share, a 90.7% increase over net income of $3.6 million, or $0.83 per diluted share, for the same quarter in 2002.

The higher net income for the fourth quarter of 2003 was primarily due to a $2.7 million increase in net interest income, a $3.0 million decrease in provision for credit losses and a $2.8 million increase in noninterest income, partially offset by a $3.5 million increase in noninterest expense.

The following table summarizes the Company s quarterly results for the years 2003 and 2002:

(in thousands, except per share data)	First	Second	Quarter Third	Fourth	Total
2003:					
Total interest income	**$24,933**	**$25,299**	**$26,009**	**$26,769**	**$103,010**
Total interest expense	**6,631**	**6,085**	**5,590**	**5,110**	**23,416**
Net interest income	**18,302**	**19,214**	**20,419**	**21,659**	**79,594**
Provision for credit losses	**4,330**	**550**	**1,150**	**1,150**	**7,180**
Noninterest income	**5,511**	**6,464**	**5,023**	**6,288**	**23,286**
Noninterest expense	**13,642**	**18,717**	**15,998**	**16,570**	**64,927**
Income before income taxes	**5,841**	**6,411**	**8,294**	**10,227**	**30,773**
Income tax expense	**1,869**	**2,051**	**2,750**	**3,355**	**10,025**
Net income	**$ 3,972**	**$ 4,360**	**$ 5,544**	**$ 6,872**	**$ 20,748**
Basic earnings per share	**$ 0.93**	**$ 1.03**	**$ 1.29**	**$ 1.61**	**$ 4.86**
Diluted earnings per share	**$ 0.92**	**$ 0.99**	**$ 1.25**	**$ 1.56**	**$ 4.72**
2002:					
Total interest income	$27,634	$26,720	$26,480	$26,111	$106,945
Total interest expense	8,195	7,682	7,257	7,158	30,292
Net interest income	19,439	19,038	19,223	18,953	76,653
Provision for credit losses	4,868	4,102	3,989	4,151	17,110
Noninterest income	3,959	3,760	1,589	3,507	12,815
Noninterest expense	13,348	13,321	12,845	13,104	52,618
Income before income taxes	5,182	5,375	3,978	5,205	19,740
Income tax expense	1,646	1,754	1,257	1,601	6,258
Net income	$ 3,536	$ 3,621	$ 2,721	$ 3,604	$ 13,482
Basic earnings per share	$ 0.84	$ 0.85	$ 0.63	$ 0.85	$ 3.17
Diluted earnings per share	$ 0.83	$ 0.83	$ 0.62	$ 0.83	$ 3.11

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ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

ASSET/LIABILITY MANAGEMENT AND INTEREST RATE SENSITIVITY

Market risk is the risk of loss in a financial instrument arising from adverse changes in market rates/prices such as interest rates, foreign currency exchange rates, commodity prices and equity prices. The Company s primary market risk exposure is interest rate risk. The ongoing monitoring and management of this risk is an important component of the Company s asset/liability management process which is governed by policies established by its Board of Directors that are reviewed and approved annually. The Board of Directors delegates responsibility for carrying out the asset/liability management policies to the Asset/Liability Committee (ALCO). In this capacity, ALCO develops guidelines and strategies impacting the Company s asset/liability management related activities based upon estimated market risk sensitivity, policy limits and overall market interest rate levels and trends.

The matching of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are interest rate sensitive and by monitoring an institution s interest rate sensitivity gap . An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. During a period of falling interest rates, the net earnings of an institution with a positive gap theoretically may be adversely affected due to its interest-earning assets repricing to a greater extent than its interest-bearing liabilities. Conversely, during a period of rising interest rates, theoretically, the net earnings of an institution with a positive gap position may increase as it is able to invest in higher yielding interest-earning assets at a more rapid rate than its interest-bearing liabilities reprice.

The Company also measures and monitors its sensitivity to interest rates using net interest income simulations on a quarterly basis. Any identified exposure is managed primarily through the use of on-balance-sheet hedges such as the extension or shortening of the duration of the investment and mortgage/asset-backed securities portfolio, retail certificates of deposit and FHLB advances. Additionally, the Company uses derivative instruments that have been designated and have qualified as either cash flow hedging instruments such as swaps, caps and floors or fair value hedging instruments such as options. The Company currently does not engage in the use of trading activities, high-risk derivatives and synthetic instruments in controlling its interest rate risk. Such uses are permitted at the recommendation of ALCO with the approval of the Board of Directors.

The following table sets forth the amounts of interest-earning assets and interest-bearing liabilities outstanding at December 31, 2003, which are anticipated by the Company, based upon certain assumptions, to reprice or mature in each of the future time periods shown. Except as stated below, the amounts of assets and liabilities shown which reprice or mature during a particular period were determined in accordance with the earlier of the term to repricing or the contractual terms of the asset or liability. Since all interest rates and yields do not adjust at the same velocity or magnitude, and since volatility is subject to change, the gap is only a general indicator of interest rate sensitivity.

(in thousands)	0-90 Days	91-180 Days	181-365 Days	1-5 Years	Over 5 Years	Non-rate sensitive	Total
Assets:							
Investment and mortgage/ asset-backed securities and interest-bearing deposits in other banks	$ 99,492	$ 38,011	$ 68,552	$ 156,916	$ 106,757	$	$ 469,728
Federal funds sold	400						400
Commercial loans	113,806	13,139	15,622	66,660	13,055		222,282
Real estate loans	219,734	80,577	142,019	432,566	39,735		914,631
Consumer loans	52,969	10,807	17,345	83,496	12,091		176,708
Other assets						119,912	119,912
Total assets	$ 486,401	$ 142,534	$ 243,538	$ 739,638	$ 171,638	$ 119,912	$ 1,903,661
Liabilities and stockholders equity:							

Noninterest-bearing deposits	$	$	$	$	$	$ 217,148	$ 217,148
Time and savings deposits	417,573	114,442	71,179	80,477	304,906		988,577
Short-term borrowings	300,400		5,000				305,400
Long-term debt	20,003	3	11,206	53,054	110,123		194,389
Other liabilities						28,937	28,937
Stockholders equity						169,210	169,210
Total liabilities and stockholders equity	$ 737,976	$ 114,445	$ 87,385	$ 133,531	$ 415,029	$ 415,295	$ 1,903,661
Interest rate sensitivity gap	$ (251,575)	$ 28,089	$ 156,153	$ 606,107	$ (243,391)	$ (295,383)	$
Cumulative interest rate sensitivity gap	$ (251,575)	$ (223,486)	$ (67,333)	$ 538,774	$ 295,383	$	$

The Company s policy is to match its level of interest-earning assets and interest-bearing liabilities within a limited range, thereby reducing its exposure to interest rate fluctuations. In connection with these asset and liability management objectives, various actions have been taken, including changes in the composition of assets and liabilities, and the use of financial instruments.

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When appropriate, ALCO may utilize off-balance sheet instruments such as interest rate swaps, caps and floors to hedge its interest rate risk position. A Board of Directors approved hedging policy statement governs the use of these instruments.

The financial instruments used and their notional amounts outstanding at December 31 for the years indicated were as follows:

(dollars in thousands)	2003	2002	2001
Interest rate swaps:			
Pay-floating swaps-notional amount	**$30,000**	$20,000	$15,000
Average receive rate	**5.98%**	6.40%	7.29%
Average pay rate	**4.00%**	4.25%	2.07%
Pay-fixed swaps-notional amount	**$10,000**	$35,000	$
Average receive rate	**1.17%**	1.72%	%
Average pay rate	**4.17%**	3.99%	%

Under interest rate swaps, the Company agrees with other parties to exchange, at specified intervals, the difference between fixed rate and floating rate interest amounts calculated by reference to the agreed notional amount.

Interest rate contracts are primarily used to convert certain deposits and long-term debt to fixed interest rates or to convert certain groups of customer loans and other interest earning assets to fixed rates. Certain interest rate swaps specifically match the amounts and terms of particular assets and liabilities.

Interest rate options, which primarily consist of caps and floors, are interest rate protection instruments that involve the payment from the seller to the buyer of an interest rate differential in exchange for a premium paid by the buyer. This differential represents the difference between current interest rates and an agreed upon rate applied to a notional amount. Interest rate caps limit the cap holder s risk associated with an increase in interest rates. Interest rate floors limit the risk associated with a decline in interest rates.

The Company has a mortgage banking operation and thus holds a portfolio of residential loans funded, pending sale to investors. These loans were $56.0 million and $97.9 million at December 31, 2003 and 2002, respectively, and are carried on the books at the lower of cost or market. Because the market value of these loans are subject to change due to interest rates, the Company utilizes forward sales and short call options to protect against rising rates.

Interest rate options at December 31, 2003, 2002 and 2001 consisted of the following:

	2003		2002		2001	
(in thousands)	Notional Amount	Estimated Fair Value	Notional Amount	Estimated Fair Value	Notional Amount	Estimated Fair Value
Caps	**$**	**nil**	$	nil	$50,000	nil
Options	**30,000**	**(230)**	30,000	(217)	5,000	(40)
Total interest rate options	**$30,000**	**$(230)**	$30,000	$(217)	$55,000	$ (40)

INTEREST RATE RISK

Interest rate risk represents the sensitivity of earnings to changes in market interest rates. As interest rates change, the interest income and expense streams associated with the Company s financial instruments also change thereby impacting net interest income (NII), the primary component of the Company s earnings. ALCO utilizes the results of a detailed and dynamic simulation model to quantify the estimated exposure of NII to sustained interest rate changes. While ALCO routinely monitors simulated NII sensitivity over a rolling two-year horizon, it also utilizes additional tools to monitor potential longer-term interest rate risk.

Based on the results of the simulation model and interest rate risk position, management monitors short- and long-term exposure to market risk by managing rates paid on liabilities; pricing on loans; volumes of loans, deposits and investments; mix of asset types varying in term, optionality and cash flow characteristics; and other factors. These tactics are employed considering market conditions, competition, and loan demand and customer preferences.

A unique aspect of the Bank s earning asset base is that 28% of total gross loans are residential mortgage loans, which have longer terms and greater option risk arising from the borrower s right to prepay. This potentially creates significant mismatch risk as funding of those assets are typically at terms much shorter than the expected terms of the loans. As a result, the Bank has generally been liability-sensitive in the past. Due to the presence of an established secondary market for residential real estate loans and its acceptance as collateral for wholesale borrowing for the Bank, this portfolio and continuing operation is a significant source of liquidity, regardless of the interest rate environment.

Over the last year, the Bank s interest rate risk position has shifted from being asset-sensitive in the first half of the year to being liability-sensitive in the second half as rates generally remained low during the year, as compared to historical averages. Continued high prepayments of residential mortgages were replaced with loans and investments that were either variable rate or with shorter fixed maturities (3 to 5 years). Additionally, long-term advances that came due were replaced with overnight borrowings. As a result, the balance sheet became liability-sensitive which had a positive impact on the net interest margin, which was continuing to compress in this low interest rate environment. Management continues to monitor the gap position at least quarterly and determines its risk management strategies based on income at risk, growth projections and biases for interest rate direction.

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The simulation model captures the impact of changing interest rates on the interest income received and interest expense paid on all assets and liabilities reflected on the Company s balance sheet as well as for off-balance sheet derivative financial instruments. This sensitivity analysis is compared to ALCO policy limits which specify a maximum tolerance level for NII exposure over a one-year horizon, assuming no balance sheet growth, given both a 200 basis point (bp) upward and 100 bp downward shift in interest rates. A parallel and pro rata shift in rates over a 12-month period is assumed. The following reflects the Company s NII sensitivity analysis as of December 31, 2003.

Rate Change	Estimated NII Sensitivity
+200bp	(1.35)%
-100bp	(1.22)%

The preceding sensitivity analysis does not represent a Company forecast and should not be relied upon as being indicative of expected operating results. These hypothetical estimates are based upon numerous assumptions including: the nature and timing of interest rate levels including yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment/replacement of asset and liability cashflows, and others. While assumptions are developed based upon current economic and local market conditions, the Company cannot make any assurances as to the predictive nature of these assumptions including how customer preferences or competitor influences might change.

Also, as market conditions vary from those assumed in the sensitivity analysis, actual results will differ due to: prepayment/refinancing levels likely deviating from those assumed, the varying impact of interest rate change, caps or floors on adjustable rate assets, the potential effect of changing debt service levels on customers with adjustable rate loans, depositor early withdrawals and product preference changes, and other internal/external variables. Furthermore, the sensitivity analysis does not reflect actions that ALCO might take in responding to or anticipating changes in interest rates.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

CONSOLIDATED FINANCIAL STATEMENTS
INDEPENDENT AUDITOR S REPORT

CB BANCSHARES, INC. AND SUBSIDIARIES

December 31, 2003, 2002 and 2001

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INDEPENDENT AUDITOR S REPORT
CB Bancshares, Inc. and Subsidiaries

The Board of Directors and Stockholders
CB Bancshares, Inc.:

We have audited the accompanying consolidated balance sheets of CB Bancshares, Inc. and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of income, changes in stockholders equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2003. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of CB Bancshares, Inc. and subsidiaries as of December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

KPMG LLP

Honolulu, Hawaii
February 13, 2004

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CONSOLIDATED BALANCE SHEETS
CB Bancshares, Inc. and Subsidiaries

(in thousands, except number of shares and per share data)	December 31, 2003	2002
ASSETS		
Cash and due from banks (Note A)	**$ 46,566**	$ 75,069
Interest-bearing deposits and deposits in other banks	**1,343**	1,214
Federal funds sold	**400**	20,525
Investment and mortgage/asset-backed securities (Notes B and I):		
Held-to-maturity (fair value of $134,552 and $113,138 at December 31, 2003 and 2002, respectively	**134,163**	112,013
Available-for-sale	**302,646**	228,335
FHLB stock	**31,576**	29,886
Loans held-for-sale	**56,039**	97,948
Loans, net (Notes C, D and I)	**1,257,582**	1,037,657
Premises and equipment, net (Note F)	**16,867**	16,596
Other real estate owned and other repossessed property (Note E)	**173**	2,193
Accrued interest receivable and other assets (Note L)	**56,306**	52,922
TOTAL ASSETS	**$1,903,661**	$1,674,358
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits (Note G):		
Noninterest-bearing	**$ 217,148**	$ 212,140
Interest-bearing	**988,577**	951,087
Total deposits	**1,205,725**	1,163,227
Short-term borrowings (Note H)	**305,400**	10,400
Accrued expenses and other liabilities (Notes L and M)	**26,217**	27,595
Long-term debt (Note I)	**194,389**	319,407
Minority interest in consolidated subsidiary (Note J)	**2,720**	2,720
Total liabilities	**1,734,451**	1,523,349
Commitments and contingencies (Notes F, I, N, O, P and Q)		
Stockholders equity (Notes Q and R):		
Preferred stock $1 par value -		
Authorized and unissued 25,000,000 shares		

Common stock $1 par value - Authorized 50,000,000 shares; issued and outstanding 4,337,211 shares in 2003 and 3,897,975 shares in 2002	**4,337**	3,898
Additional paid-in capital	**103,050**	78,311
Retained earnings	**56,542**	63,679
Unreleased shares to employee stock ownership plan	**(1,323)**	(1,486)
Accumulated other comprehensive income, net of tax	**6,604**	6,607
Total stockholders equity	**169,210**	151,009
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	**$1,903,661**	$1,674,358

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME
CB Bancshares, Inc. and Subsidiaries

	Years ended December 31,		
(in thousands, except per share data)	**2003**	**2002**	**2001**
Interest income:			
Interest and fees on loans	**$ 85,635**	$ 89,752	$108,712
Interest and dividends on investment and mortgage/ asset-backed securities:			
Taxable interest income	**13,906**	13,478	15,260
Nontaxable interest income	**1,546**	1,557	1,553
Dividends	**1,693**	1,971	2,278
Other interest income	**230**	187	451
Total interest income	**103,010**	106,945	128,254
Interest expense:			
Deposits (Note G)	**11,135**	18,098	39,438
FHLB advances and other short-term borrowings	**1,158**	672	5,095
Long-term debt	**11,123**	11,522	12,915
Total interest expense	**23,416**	30,292	57,448
Net interest income	**79,594**	76,653	70,806
Provision for credit losses (Note D)	**7,180**	17,110	13,628
Net interest income after provision for credit losses	**72,414**	59,543	57,178
Noninterest income:			
Service charges on deposit accounts	**4,559**	4,345	3,811
Other service charges and fees	**7,147**	6,784	4,897
Net realized gains (losses) on sales of securities (Notes B and S)	**1,718**	(1,765)	(169)
Net gains on sales of loans	**2,533**	1,493	2,060
Item processing fee	**1,866**	397	135
Impairment of asset-backed securities (Note A)		(1,399)	(10,642)
Other (Note M)	**5,463**	2,960	2,725
Total noninterest income	**23,286**	12,815	2,817

Noninterest expense:			
Salaries and employee benefits (Note Q)	**29,852**	24,675	23,111
Net occupancy expense (Note F)	**6,639**	6,367	6,588
Equipment expense (Note F)	**2,406**	2,942	3,469
Unsolicited hostile takeover proposal expenses	**6,621**		
Other (Note K)	**19,409**	18,634	17,427
Total noninterest expense	**64,927**	52,618	50,595
Income before income taxes	**30,773**	19,740	9,400
Income tax expense (Note L)	**10,025**	6,258	3,250
NET INCOME	**$ 20,748**	$ 13,482	$ 6,150
Per share data (Note R):			
Basic	**$ 4.86**	$ 3.17	$ 1.45
Diluted	**$ 4.72**	$ 3.11	$ 1.43

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME (LOSS)
CB Bancshares, Inc. and Subsidiaries

(in thousands, except per share data)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Unreleased Shares to Employee Stock	Accumulated Other Comprehensive Income (Loss)	Total
Year ended December 31, 2003:							
Balance at January 1, 2003	**3,898**	**$3,898**	**$ 78,311**	**$ 63,679**	**$(1,486)**	**$ 6,607**	**$151,009**
Comprehensive income							
Net income				**20,748**			**20,748**
Other comprehensive income, net of tax							
Unrealized loss on securities, net of reclassification adjustment						**(3)**	**(3)**
Total comprehensive income				**20,748**		**(3)**	**20,745**
Cash dividends:							
$0.95 per share				**(4,015)**			**(4,015)**
Options exercised	**47**	**47**	**1,178**				**1,225**
Directors compensation	**1**	**1**	**31**				**32**
Stock dividend	**391**	**391**	**23,381**	**(23,870)**			**(98)**
Cancelled and retired shares			**(12)**				**(12)**
Unreleased ESOP shares			**161**		**163**		**324**
Balance at December 31, 2003	**4,337**	**$4,337**	**$103,050**	**$ 56,542**	**$(1,323)**	**$ 6,604**	**$169,210**
Year ended December 31, 2002:							
Balance at January 1, 2002	3,506	$3,506	$ 65,427	$ 65,714	$(1,839)	$ 954	$133,762
Comprehensive income							
Net income				13,482			13,482
Other comprehensive income, net of tax							
Unrealized gains on securities, net of reclassification adjustment						5,653	5,653
Total comprehensive income				13,482		5,653	19,135

Cash dividends:							
$0.44 per share				(1,649)			(1,649)
Options exercised	182	182	4,786				4968
Stock dividend	362	362	13,448	(13,868)			(58)
Cancelled and retired shares	(152)	(152)	(5412)				(5,564)
Unreleased ESOP shares			62		353		415
Balance at December 31, 2002	3,898	$3,898	$ 78,311	$ 63,679	$(1,486)	$ 6,607	$151,009
Year ended December 31, 2001:							
Balance at January 1, 2001	3,189	$3,189	$ 54,594	$ 72,284	$	$(6,905)	$123,162
Comprehensive income							
Net income				6,150			6,150
Other comprehensive income, net of tax							
Unrealized gains on securities, net of reclassification adjustment						7,859	7,859
Total comprehensive income				6,150		7,859	14,009
Cash dividends:							
$0.43 per share				(1,441)			(1,441)
Options exercised	8	8	191				199
Stock dividend	318	318	10,907	(11,279)			(54)
Cancelled and retired shares	(9)	(9)	(265)				(274)
Unreleased ESOP shares					(1,839)		(1,839)
Balance at December 31, 2001	3,506	$3,506	$ 65,427	$ 65,714	$(1,839)	$ 954	$133,762

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS
CB Bancshares, Inc. and Subsidiaries

	Years ended December 31,		
(in thousands)	**2003**	**2002**	**2001**
Cash flows from operating activities:			
Net income	**$ 20,748**	$ 13,482	$ 6,150
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	**7,180**	17,110	13,628
Impairment of asset-backed securities		1,399	10,642
Gain on sale of foreclosed assets	**(440)**	(359)	(50)
Net realized (gains) losses on sales of securities	**(1,718)**	1,765	169
Depreciation and amortization	**4,924**	3,916	2,329
Deferred income taxes	**(570)**	(1,467)	86
Decrease in accrued interest receivable	**166**	1,516	1,526
Increase (decrease) in accrued interest payable	**(728)**	69	(3,577)
Gain on sale of loans available for sale	**(2,533)**	(1,493)	(2,060)
Loans originated for sale	**(416,018)**	(238,790)	(189,441)
Proceeds from sale of loans held for sale	**238,070**	165,238	172,476
Increase in other assets	**(3,273)**	(1,675)	(1,891)
Increase (decrease) in other liabilities	**1,904**	4,110	(1,601)
FHLB stock dividends	**(1,690)**	(1,969)	(2,276)
Other	**236**	500	1,111
Net cash provided by (used in) operating activities	**(153,742)**	(36,648)	7,221
Cash flows from investing activities:			
Net decrease (increase) in interest-bearing deposits in other banks	**(129)**	(197)	41
Net decrease (increase) in federal funds sold	**20,125**	(9,870)	(10,045)
Purchase of held-to-maturity securities	**(163,978)**	(143,401)	(26,200)
Repayments of held-to-maturity securities	**139,583**	57,125	198
Proceeds from sales of available-for-sale securities	**179,414**	63,493	54,607
Proceeds from maturities of available-for-sale securities	**74,675**	49,987	43,843
Purchase of available-for-sale securities	**(104,166)**	(105,900)	(928)
Proceeds from sale of FHLB stock		4,489	2,300
Net loan originations under (over) principal payments	**(230,555)**	115,375	56,447
Capital expenditures	**(2,913)**	(2,101)	(1,805)
Proceeds from sales of foreclosed assets	**3,280**	5,635	5,946
Purchase of bank owned life insurance		(7,500)	
Net cash provided by (used in) investing activities	**(84,664)**	27,135	124,404

Cash flows from financing activities:			
Net increase (decrease) in time deposits	**(29,217)**	(74,176)	(186,798)
Net increase (decrease) in other deposits	**71,714**	98,968	106,770
Net increase (decrease) in short-term borrowings	**295,000**	(65,700)	(94,600)
Proceeds from long-term debt	**35,000**	140,000	151,200
Principal payments on long-term debt	**(160,018)**	(35,017)	(118,285)
Net decrease in minority interest in consolidated subsidiary			(4,280)
Cash dividends paid	**(4,015)**	(1,649)	(1,441)
Cash-in-lieu payments on stock dividend	**(98)**	(58)	(54)
Stock repurchase	**(12)**	(5,564)	(274)
Stock options exercised	**1,225**	4,968	199
Unreleased ESOP shares	**324**	415	(1,839)
Net cash provided by (used in) financing activities	**209,903**	62,187	(149,402)
Increase (decrease) in cash and due from banks	**(28,503)**	52,674	(17,777)
Cash and due from banks at beginning of year	**75,069**	22,395	40,172
Cash and due from banks at end of year	**$ 46,566**	$ 75,069	$ 22,395
Supplemental disclosures of cash flow information:			
Interest paid on deposits and other borrowings	**$ 24,203**	$ 29,555	$ 61,023
Income taxes paid	**12,582**	3,400	5,248
Supplemental disclosure of non-cash activities:			
Loan securitizations	**$ 223,010**	$ 27,138	$

Supplemental schedule of non-cash operating and investing activity:

See accompanying notes to the consolidated financial statements.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CB Bancshares, Inc. and Subsidiaries

NOTE A BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

CB Bancshares, Inc. and Subsidiaries (the Company) provide financial services to domestic markets and grant commercial, financial, real estate, installment and consumer loans to customers throughout the State of Hawaii. Although the Company has a diversified loan portfolio, a substantial portion of its debtors ability to honor their contracts is primarily dependent upon the economy and the real estate market in the State of Hawaii.

The significant accounting policies of the Company are as follows:

Principles of Consolidation and Presentation. The consolidated financial statements include the accounts of CB Bancshares, Inc. (the Parent Company) and its wholly-owned subsidiaries: City Bank and its wholly-owned subsidiaries (the Bank); Datatronix Financial Services, Inc. (Datatronix); and O.R.E., Inc. Significant intercompany transactions and balances have been eliminated in consolidation.

The Company s consolidated financial statements have been prepared in accordance with generally accepted accounting principles and conform to prevailing practices within the banking industry. Preparing financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates. Also, certain reclassifications have been made to the consolidated financial statements and accompanying notes for the previous two years to conform to the current year s presentation. Such reclassifications did not have a material effect on the consolidated financial statements.

Risks Associated with Financial Instruments. The credit risk of a financial instrument is the possibility that a loss may result from the failure of another party to perform in accordance with the terms of the contract. The most significant credit risk associated with the Company s financial instruments is concentrated in its loans receivable. The Company has established a system for monitoring the level of credit risk in its loan portfolio.

Concentrations of credit risk would exist for groups of borrowers when they have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The ability of the Company s borrowers to repay their commitments is contingent on several factors, including the economic conditions in the borrowers geographic area and the individual financial condition of the borrowers. The Company generally requires collateral or other security to support borrower commitments on loans receivable. This collateral may take several forms. Generally, on the Company s mortgage loans, the collateral will be the underlying mortgaged property. The Company s lending activities are primarily concentrated in the State of Hawaii.

Market risk is the risk of loss from adverse changes in market prices and rates. The Company s market risk arises primarily from interest rate risk inherent in its lending and deposit taking activities. To that end, management actively monitors and manages its interest rate risk exposure. The Company does not currently engage in trading activities. The Company is subject to interest rate risk to the degree that its interest-earning assets reprice on a different frequency or schedule than its interest-bearing liabilities. The Company closely monitors the pricing sensitivity of its financial instruments.

Cash and Cash Equivalents. For purposes of the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet caption, Cash and due from banks . Included in cash are amounts restricted for the Federal Reserve requirement of $8,022,000 and $11,179,000 in 2003 and 2002, respectively.

Investment and Mortgage/Asset-Backed Securities. Investment and mortgage/asset-backed securities are classified into the following categories:

Trading securities are securities that are bought and held principally for the purpose of selling them in the near term and are reported at fair value with changes in fair value reported in current earnings.

Held-to-maturity securities are securities the Company has the positive intent and ability to hold to maturity. Held-to-maturity securities are reported at amortized cost with premiums and discounts included in interest income over the period to maturity, using the interest method.

Available-for-sale securities are securities not classified as either trading or held-to-maturity. Securities available-for-sale are reported at fair value with unrealized gains and losses, net of tax, included as other comprehensive income in stockholders equity. Gains and losses on sales are determined using the specific identification method.

For individual held-to-maturity and available-for-sale securities, declines in fair value below cost for other than temporary market conditions would result in write-downs of the carrying value to the current fair value and the realized losses included in earnings.

As a member of the Federal Home Loan Bank of Seattle (the FHLB), the Company is required to maintain a minimum investment in the capital stock of the FHLB in an amount at least equal to the greater of 1% of the aggregate principal amount of its unpaid residential loans, residential purchase contracts and similar obligations at the end of each calendar year, assuming for such purposes that at least 30% of its assets were residential mortgage loans, or 5% of its advances from the FHLB. The stock is recorded as a restricted investment security at amortized cost, which approximates fair value.

Interest income earned on retained or purchased beneficial interests in securitized financial assets is recognized over the life of the investment based on an anticipated yield determined by periodically estimating cash flows. Interest income is revised prospectively for changes in cash flows and impairment is recognized if the fair value of the beneficial interest has declined below its carrying amount and the decline is other than temporary. Because the book values of certain of the Company s asset backed securities were more than the fair values of those securities during 2002 and 2001, the Company recognized a $1.4 million (after tax charge of $1.0 million) and $10.6 million (after tax charge of $6.4 million), respectively, noncash charge in the Consolidated Statements of Income.

Loans and Leases Held for Investment. Interest income on loans receivable is accrued as it is earned. Loans receivable are reported at the outstanding principal balance, adjusted for any charge-offs, the allowance for credit losses, any deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans.

Direct financing leases are carried at the aggregate of lease payments receivable plus estimated residual value of the leased property, less unearned income. Unearned income is amortized over the lease terms by methods that approximate the interest method. Residual values on leased assets are reviewed regularly for other than temporary impairment.

Loan origination fees and costs are deferred and recognized as an adjustment of the yield. Accretion of discounts and deferred loan fees is discontinued when loans are placed on nonaccrual status. Loan commitment fees received are deferred as other liabilities until the loan is advanced and are then recognized over the term or estimated life of the loan as an adjustment of the yield. At expiration, unused commitment fees are recognized as fees and commission revenue. Guarantee fees received are recognized as fee revenue over the related terms.

The allowance for credit losses is periodically evaluated for adequacy by management. Factors considered include the Company s loan loss experience, known and inherent risks in the portfolio, current economic conditions, adverse situations that may affect the borrower s ability to repay, regulatory policies, and the estimated value of underlying collateral, if any. The allowance for credit losses is increased by any provision for credit losses and decreased by charge-offs (net of recoveries).

Loans are impaired when, based on current information and events, it is probable that principal or interest will not be collected at scheduled maturity or will be unreasonably delayed. Impaired loans are measured at the present value of expected future cash flows discounted at the loan s effective interest rate or the fair value of the collateral, if the loan is collateral dependent. Impairment losses are reflected as charge-offs in the allowance for loan losses. For smaller-balance homogeneous loans (primarily residential real estate and consumer loans), the allowance for loan losses is based upon Management s evaluation of the quality, character and inherent risks in the loan portfolio, current economic conditions, and historical loan loss experience. Delinquent close-ended consumer loans are charged off within 120 days (180 days for open-ended consumer loans and residential real estate loans), unless determined to be adequately collateralized or in imminent process of collection.

Interest accrual on impaired loans is discontinued when, in management s opinion, the borrower may be unable to make scheduled payments. When interest accrual is discontinued, any outstanding accrued interest is reversed and, subsequently, interest income is recognized as payments are received.

The Company generally places loans on nonaccrual status that are 90 days past due as to principal or interest unless well-collateralized and in the process of collection, or when management believes that collection of principal or interest has become doubtful, or when a loan is first classified as impaired. When loans are placed on nonaccrual status, previously accrued and uncollected interest is reversed against interest income of the current period. Cash interest payments received on nonaccrual loans are applied as a reduction of principal balance when doubt exists as to the ultimate collection of the principal; otherwise, such payments are recorded as income.

Nonaccrual loans are generally returned to accrual status when they become both current as to principal and interest or become both well collateralized and in the process of collection.

Loans Held-for-Sale. The Company sells loans and participations in loans with yield rates to the investors based upon current market rates. Gain or loss on the sale of loans is recognized to the extent that the selling prices differ from the carrying value of the loans sold based on the estimated relative fair values of the loans sold and any retained interests. Residential mortgage loans originated for sale are classified as loans held-for-sale and are accounted for at the lower of aggregate cost or fair value.

Transfers and Servicing of Financial Assets. A transfer of financial assets is accounted for as a sale when control is surrendered over the assets transferred. Servicing rights and other retained interests in the assets sold are recorded by allocating the previous recorded investment between the asset sold and the interest retained based on their relative fair values, if practicable to determine, at the date of transfer. For the years presented, servicing assets and amortization were not material.

Premises and Equipment. Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are computed using both the straight-line and accelerated methods over the estimated useful lives of the assets or the applicable facility leases, whichever is shorter. The range of estimated useful lives is 3 to 45 years for premises and leasehold improvements and 3 to 20 years for equipment.

Other Real Estate Owned. Other real estate owned properties acquired through, or in lieu of, foreclosure proceedings are recorded at fair value on the date of foreclosure establishing a new cost basis. Losses arising at the time of acquisition of such properties are charged against the allowance for credit losses. After foreclosure, management performs periodic valuations and the properties are carried at the lower of cost or fair value, less estimated costs to sell. Revenues, expenses and provisions to the valuation allowance are included in operations as incurred.

Income Taxes. The Company files consolidated income tax returns. The Bank and Datatronix pay to the Parent Company the amount of income taxes they would have paid had they filed separate income tax returns.

Income taxes are accounted for under the asset and liability method. 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 and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using

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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.

Intangible Assets. Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets, requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually. SFAS No. 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and also be reviewed for impairment in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. The Company adopted the provisions of SFAS No. 142 beginning January 1, 2002. At December 31, 2003 and 2002, the Company did not have any assets classified as goodwill under the new pronouncement. However, the Company does have servicing premiums. Under the provisions of SFAS No. 142, the Company expects to continue amortizing these intangible assets over the period of estimated net servicing income. The impact of the adoption of SFAS No. 142 has not had a material impact on the Company s consolidated financial statements.

Stock-Based Compensation. The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations including Financial Accounting Standards Board (FASB) interpretation No. 44, Accounting for Certain Transactions Involving Stock Compensation, an interpretation of APB Opinion No. 25 issued in March 2002, in accounting for its fixed plan stock options. As such, compensation expense would be recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123, Accounting for Stock-Based Compensation, established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. In December 2002, SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure, an amendment of FASB Statement No. 123* was issued. This Statement amends SFAS No. 123 to provide alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements. As allowed by SFAS No. 123 (as amended by SFAS No. 148), the Company has elected to continue to apply the intrinsic value-based method of accounting described above, and has adopted the disclosure requirements of SFAS No. 148.

The original exercise price of each option equals the market price of the Company s stock on the date of grant. Accordingly, no compensation cost has been recognized for the plan. Had compensation cost for the plan been determined using the fair value based method, the Company s net income and net income per share would have been the pro forma amounts below:

	2003	**2002**	**2001**
Net income:			
As reported	**$20,748,000**	$13,482,000	$6,150,000
Deduct: total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	**(634,000)**	(179,000)	(603,000)
Pro forma	**$20,114,000**	$13,303,000	$5,547,000
Earnings per share:			

Basic as reported	**$**	**4.86**	$	3.17	$	1.45
Basic Pro forma	**$**	**4.71**	$	3.12	$	1.31
Diluted as reported	**$**	**4.72**	$	3.11	$	1.43
Diluted Pro forma	**$**	**4.58**	$	3.07	$	1.29

The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model. For grants in 2003, 2002 and 2001, the following weighted average assumptions were used; expected dividend of 1.03%, 1.03% and 1.25%, expected volatility of 19.00%, 19.00% and 23.00%, risk-free interest rate of 4.61%, 5.55% and 4.55%, and expected life of 4.0 years, 5.0 years and 6.0 years. The weighted average fair value of options granted during 2003, 2002 and 2001 was $20.91, $8.77 and $9.82, respectively.

Derivative Instruments and Hedging Activities. The Company uses interest rate swaps, caps and floors to modify the interest rate characteristics of certain assets and liabilities. The Company documents the relationship between the hedging instruments and hedged items, as well as the risk management objective and strategy for undertaking the hedge. To qualify for hedge accounting, the derivative instruments that are designated as fair value or cash flow hedges are linked to specific assets and/or liabilities on the balance sheet. Additionally, the Company assesses on an ongoing basis, whether the derivative instruments are highly effective in offsetting changes in fair values or cashflows of hedged items. If it is determined that the derivative instrument is not highly effective as a hedge, hedge accounting would be discontinued. The interest rate swap contracts that were designated as a hedge at inception are still highly effective based on the Company s ongoing assessments.

In 2003, interest rate swaps were used to convert floating assets and liabilities to fixed rates. $20 million of pay-floating swaps qualify as cash flow hedging instruments as they served to convert $20 million of prime-based loans to fixed rates. During 2003, no amounts were recognized in earnings in connection with the ineffective portion of these cash flow hedges and no amounts were excluded from the measure of effectiveness.

Derivatives not designated as hedges consist of $10 million of pay-floating swaps, $10 million of pay-fixed swaps and $30 million of options and instruments containing option features that behave based on limits. At December 31, 2003, the Company also had $15.0 million of forward sales on securities to hedge residential mortgage loans. These instruments are used to hedge risks associated with interest rate movements and serve as hedges from an economic perspective; however, they do not qualify for hedge accounting under SFAS No. 133, as amended. The Bank recorded a gain of approximately $1.5 million in 2003 for these instruments as a component of noninterest income in the consolidated statement of income. Included in this $1.5 million gain is a one-time gain of $855,000 recognized on the termination of two (2) interest rate swaps.

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The Company occasionally purchases or originates financial instruments that contain an embedded derivative instrument. At inception of the financial instrument, the Company assesses whether the economic characteristics of the embedded derivative instrument are clearly and closely related to the economic characteristics of the financial instrument (host contract), whether the financial instrument that embodies both the embedded derivative instrument and the host contract is currently measured at fair value with changes in fair value reported in earnings, and whether a separate instrument with the same terms as the embedded instrument would meet the definition of a derivative instrument. As of December 31, 2003 and 2002, all of the Company s embedded derivatives are considered clearly and closely related to the host contract and therefore are not required to be separated from their host contract

On January 1, 2001, the Company recorded the cumulative effect of adopting SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended, in its identified fair value hedges that were employed at the time. A transition adjustment of $263,000 associated with establishing fair values of the derivative instruments and hedged items on the balance sheet was recorded in investment securities.

Earnings Per Share. Basic earnings per common share are based on the weighted-average number of common shares outstanding for the year. Diluted earnings per common share are based on the assumption that all potentially dilutive common shares and dilutive stock options were converted at the beginning of the year. All per share amounts have been restated to reflect the impact of the 10% stock dividend issued in June 2003.

New Accounting Principles. SFAS No. 143. In June 2001, FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations, which requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs would be capitalized as part of the carrying amount of the long-lived asset and depreciated over the life of the asset. The liability is accreted at the end of each period through charges to operating expense. If the obligation is settled for other than the carrying amount of the liability, the Company will recognize a gain or loss on settlement. The adoption of SFAS No. 143 on January 1, 2003 had no effect on the Company s consolidated financial statements.

SFAS No. 146. In June 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities, which addresses financial accounting and reporting for costs associated with exit or disposal activities. The provisions of this Statement were effective for exit or disposal activities that are initiated after December 31, 2002. The adoption of SFAS No. 146 on January 1, 2003 had no effect on the Company s consolidated financial statements.

SFAS No. 149. In April 2003, the FASB issued SFAS 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 SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. SFAS No. 149 is effective for contracts entered into or modified and for hedging relationships designated after June 30, 2003. The adoption of SFAS No. 149 on July 1, 2003 had no material effect on the Company s consolidated financial statements.

SFAS No. 150. In May 2003, the FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity which 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 150 is effective for all 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. In October 2003, however, the FASB indefinitely deferred the effective date of the provisions of SFAS No. 150 related to classification and measurement requirements for mandatorily redeemable financial instruments that become subject to SFAS No. 150 solely as a result of consolidation. At December 31, 2003, the Company had no financial instruments falling within the scope of SFAS

No. 150.

FASB Interpretation No. 45. In November 2002, the FASB issued Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. This interpretation provides disclosures to be made by a guarantor in its interim and annual financial statements for periods ending after December 15, 2002 about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The Company adopted the provisions of the Interpretation on January 1, 2003 with no effect on the Company s historical consolidated financial statements.

FASB Interpretation No. 46. In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities , an interpretation of ARB No. 51. This Interpretation addresses the consolidation by business enterprises of variable interest entities (VIEs) as defined. The Interpretation applies immediately to variable interests in VIEs created after January 31, 2003, and to variable interests in VIEs obtained after January 31, 2003. For variable interests in VIEs that an enterprise acquired before February 1, 2003, the Interpretation is applicable in the first fiscal year or interim period beginning after June 15, 2003. In December 2003, the FASB revised Interpretation No. 46, which replaced its original interpretation issued in January 2003, and among other things, revised certain effective dates. At December 31, 2003, the Company had no significant variable interests in a variable interest entity requiring consolidation or disclosure in accordance with the Interpretation.

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NOTE B - INVESTMENT AND MORTGAGE-BACKED SECURITIES

The amortized cost and estimated fair values of the Company s investment portfolio at December 31, 2003 and 2002 were as follows:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2003:				
Held to Maturity:				
U.S. Treasury and other U.S. government agencies and corporations	**$ 79,126**	**$ 292**	**$ 375**	**$ 79,043**
Corporate bonds	**29,199**	**417**		**29,616**
Mortgage-backed securities	**25,838**	**215**	**160**	**25,893**
Total held to maturity	**$134,163**	**$ 924**	**$ 535**	**$134,552**
Available-for-sale securities:				
U.S. Treasury and other U.S. government agencies and corporations	**$ 49,512**	**$ 969**	**$ 24**	**$ 50,457**
States and political subdivisions	**32,658**	**2,509**		**35,167**
Mortgage/asset-backed securities	**189,181**	**8,048**	**1,259**	**195,970**
Others	**20,906**	**146**		**21,052**
Total available-for-sale	**$292,257**	**$11,672**	**$1,283**	**$302,646**
Total investments	**$426,420**	**$12,596**	**$1,818**	**$437,198**
2002:				
Held to Maturity:				
U.S. Treasury and other U.S. government agencies and corporations	$ 75,996	$ 410	$	$ 76,406
Corporate bonds	34,861	655		35,516
Mortgage-backed securities	1,156	60		1,216
Total held to maturity	$112,013	$ 1,125	$	$113,138

Available-for-sale securities:				
U.S. Treasury and other U.S. government agencies and corporations	$ 5,125	$ 337	$	$ 5,462
States and political subdivisions	32,975	2,073	12	35,036
Mortgage/asset-backed securities	159,866	8,641	136	168,371
Others	19,399	97	30	19,466
Total available-for-sale	$217,365	$11,148	$ 178	$228,335
Total investments	$329,378	$12,273	$ 178	$341,473

At December 31, 2003 and 2002, the Company had no securities classified as trading.

Securities with an aggregate carrying value of $320,507,000 and $160,512,000, at December 31, 2003 and 2002, respectively, were pledged to collateralize public deposits and for other purposes required by law. Investment in the stock of the FHLB of Seattle totaled $31.6 million and $29.9 million at December 31, 2003 and 2002, respectively. The stock of the FHLB of Seattle is pledged as collateral for FHLB advances.

The following presents the amortized cost and estimated fair value of investment securities at December 31, 2003 by contractual maturity. Expected maturity will differ from contractual maturity because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The stated maturity of mortgage/asset-backed securities is presented in total since the principal cash flows of these securities are not received at a single maturity date.

	Held to Maturity		**Available for Sale**	
(in thousands)	**Amortized Cost**	**Estimated Fair Value**	**Amortized Cost**	**Estimated Fair Value**
Due in one year or less	**$ 18,925**	**$ 19,017**	**$ 5,005**	**$ 5,136**
Due 1 to 5 years	**64,031**	**64,131**	**44,507**	**45,321**
Due 5 to 10 years	**25,369**	**25,511**	**11,955**	**13,039**
Due > 10 years			**41,609**	**43,180**
Mortgage/asset-backed securities	**25,838**	**25,893**	**189,181**	**195,970**
Total	**$134,163**	**$134,552**	**$292,257**	**$302,646**

Proceeds from sales of securities available-for-sale during 2003, 2002, and 2001 were $179,414,000, $63,493,000, and $54,607,000, respectively. These sales resulted in gross realized gains of $2,672,000, $175,003 and $1,075,000, respectively, and gross realized losses of $954,000, $12,170 and $1,000, respectively.

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At December 31, 2003, there were $1.8 million of unrealized losses on temporarily impaired securities. The unrealized losses were primarily due to the increases in market interest rates and not from the deterioration in the creditworthiness of the issuer. At the end of 2003, there were 14 securities in the investment portfolio that were in an unrealized loss position for less than 12 months and one security for more than 12 months. The following is a summary of the unrealized losses on temporarily impaired securities at December 31, 2003:

(in thousands)	Less than 12 months		12 months or longer		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Treasury obligations and direct obligations of US Government agencies	$37,034	$ 399	$	$	$37,034	$ 399
Federal agency mortgage-backed securities	49,739	1,419			49,739	1,419
Other mortgage-backed securities			4		4	
Total temporarily impaired securities	$86,773	$1,818	$ 4	$	$86,777	$1,818

NOTE C - LOANS

The loan portfolio consisted of the following at December 31, 2003 and 2002:

(in thousands)	2003	2002
Commercial and financial	**$ 245,875**	$ 227,736
Real estate:		
Construction	**98,237**	52,538
Commercial	**403,946**	210,512
Residential	**367,685**	444,246
Installment and consumer	**180,064**	135,415
Gross loans	**1,295,807**	1,070,447
Less:		
Unearned income	**2,453**	1,683
Net deferred loan fees	**7,282**	3,984
Allowance for credit losses	**28,490**	27,123
Loans, net	**$1,257,582**	$1,037,657

Substantially all of the Company s residential real estate loans are collateralized by properties located in the State of Hawaii.

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage loans, including mortgage/asset-backed securities serviced for others, were $420,914,000 and $327,728,000 at December 31, 2003 and 2002, respectively. Custodial escrow balances maintained with the foregoing loan servicing, and included in demand deposits, were $1,741,000 and $1,624,000 at December 31, 2003 and 2002, respectively.

Commercial and financial loans at December 31, 2003 and 2002 include financing lease receivables of $26.5 million and $16.6 million, respectively.

Nonaccrual loans amounted to $5.7 million and $12.7 million at December 31, 2003 and 2002, respectively. Loans past due 90 days or more still accruing interest amounted to $941,000 and $932,000 at December 31, 2003 and 2002, respectively. Interest on nonaccrual loans that would have been recorded in 2003 and 2002 had such loans been performing in accordance with their original terms was $448,000 and $1.2 million, respectively. The amount of interest on nonaccrual loans that was included in net income in 2003 and 2002 was $138,000 and $711,000, respectively.

At December 31, 2003, the Company had $24.0 million of commitments to sell loans and $23.9 million of rate lock commitments.

In the normal course of business, the Company makes loans to its executive officers and directors and to companies and individuals affiliated with its executive officers and directors. In management s opinion, such loans and loan commitments were made at the Company s normal credit terms, including interest rates and collateral requirements, and do not represent more than a normal risk of collection. The following is the activity of loans to such parties in 2003:

(in thousands)	
Balance at beginning of year	**$ 6,032**
New loans	**7,072**
Repayments	**(10,112)**
Balance at end of year	**$ 2,992**

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NOTE D - ALLOWANCE FOR CREDIT LOSSES

The changes in the allowance for credit losses for the years indicated were as follows:

(in thousands)	2003	2002	2001
Balance at beginning of year	**$ 27,123**	$ 19,464	$ 17,477
Provision charged to expense	**7,180**	17,110	13,628
Recoveries	**5,942**	3,846	817
Charge-offs	**(11,755)**	(13,297)	(12,428)
Balance at end of year	**$ 28,490**	$ 27,123	$ 19,494

Information related to loans considered to be impaired for the years indicated were as follows:

(in thousands)	2003	2002	2001
Recorded investment in impaired loans	**$5,385**	$12,261	$20,315
Impaired loans with related allowance for credit losses calculated under SFAS No. 114	**1,413**	1,493	8,052
Total allowance for credit losses on impaired loans	**1,122**	3,395	1,555
Average recorded investment in impaired loans during the year	**8,737**	17,021	23,897
Interest income on impaired loans using cash basis of income recognition	**368**	1,027	937

NOTE E OTHER REAL ESTATE OWNED

The carrying value of foreclosed real estate, net of the following allowance for losses, were $173,000, $2,193,000, and $4,674,000 at December 31, 2003, 2002 and 2001, respectively. Activity in the allowance for losses on other real estate owned was as follows:

(in thousands)	2003	2002	2001
Balance at beginning of year	**$ 69**	$ 177	$ 217
Provision charged to expense	**176**	500	150
Charge-offs, net of recoveries		(608)	(190)
Balance at end of year	**$245**	$ 69	$ 177

NOTE F - PREMISES AND EQUIPMENT

The Company s premises and equipment at December 31, 2003 and 2002 were as follows:

(in thousands)	2003	2002
Premises	**$ 23,961**	$22,326
Equipment	**28,818**	27,838
Total cost	**52,779**	50,164
Less accumulated depreciation and amortization	**(35,912)**	33,568
Net carrying value	**$ 16,867**	$16,596

Depreciation and amortization charged to operations for the years ended December 31, 2003, 2002 and 2001 were as follows:

(in thousands)	2003	2002	2001
Net occupancy expense	**$ 926**	$ 967	$1,036
Equipment expense	**1,719**	2,172	2,234
Total depreciation and amortization	**$2,645**	$3,139	$3,270

The Company leases certain properties and equipment under leases that expire on various dates through 2067. Certain leases provide for renegotiations at fixed intervals and require payment of real estate taxes, maintenance, insurance and certain other operating expenses. Rent charged against operations, including equipment rental, was as follows:

(in thousands)	2003	2002	2001
Rental expense	**$5,714**	$5,541	$5,505
Less sublease income	**566**	580	557
Total net rental expense	**$5,148**	$4,961	$4,948

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The following are future minimum net rental commitments for long-term noncancelable operating leases as of December 31, 2003. Future rentals subject to renegotiations are computed at the latest annual rents.

(in thousands)	Operating Leases
2004	$ 4,470
2005	4,357
2006	3,881
2007	3,848
2008	3,846
Thereafter	9,762
Total	$30,164

NOTE G - DEPOSITS

Deposits consisted of the following at December 31, 2003 and 2002:

(in thousands)	2003	2002
Noninterest-bearing deposits	**$ 217,148**	$ 212,140
Interest-bearing deposits:		
Demand deposits	**198,943**	194,108
Savings	**352,276**	290,404
Time deposits of $100 or more	**210,507**	211,030
Time deposits less than $100	**226,851**	255,545
Total interest-bearing deposits	**988,577**	951,087
Total deposits	**$1,205,725**	$1,163,227

Interest expense on deposits for the years ended December 31, 2003, 2002 and 2001 were as follows:

(in thousands)	2003	2002	2001
Demand deposits	**$ 500**	$ 2,284	$ 5,200
Savings	**2,449**	2,970	3,727

Time deposits of $100 or more	**3,553**	4,486	10,908
Time deposits less than $100	**4,633**	8,358	19,603
Total interest expense	**$11,135**	$18,098	$39,438

At December 31, 2003, the scheduled maturities of time deposits were as follows:

(in thousands)	
2003	**$366,803**
2004	**43,551**
2005	**12,058**
2006	**7,875**
2007	**7,071**
Total	**$437,358**

NOTE H - SHORT-TERM BORROWINGS

Short-term borrowings at December 31, 2003 and 2002 consisted of the following:

(in thousands)	**2003**	**2002**
Advances from the FHLB	**$305,000**	$10,000
Federal treasury tax and loan note	**400**	400
Total short-term borrowings	**$305,400**	$10,400

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Average interest rates and average and maximum balances for short-term borrowing categories were as follows for categories of borrowings where the average outstanding balance for the year was 30% or more of stockholders equity at December 31 for the years indicated:

(dollars in thousands)	2003	2002	2001
Advances from the FHLB:			
Average interest rate at year-end	**1.11%**	1.87%	3.13%
Maximum outstanding at any month-end	**$305,000**	$79,000	$174,000
Average outstanding	**98,357**	22,938	93,273
Average interest rate for the year	**1.18%**	2.66%	4.71%
Federal funds purchased:			
Average interest rate at year-end	%	%	%
Maximum outstanding at any month-end			14,300
Average outstanding			3,755
Average interest rate for the year	%	%	3.48%

NOTE I - LONG-TERM DEBT

Long-term debt at December 31, 2003 and 2002 consisted of the following:

(in thousands)	2003	2002
Advances from the FHLB	**$194,389**	$319,407
Total long-term debt	**$194,389**	$319,407

The advances from the FHLB bear interest at rates ranging from 2.26% to 8.22%. Interest is payable monthly over the term of each advance. Pursuant to collateral agreements with the FHLB, short and long-term advances are collateralized by a blanket pledge of certain securities with carrying values of $221,014,000 and $47,326,000, and loans of $465,246,000 and $458,670,000 in 2003 and 2002, respectively. FHLB advances are under credit line agreements of $570,107,000 and $416,450,000 in 2003 and 2002, respectively. At December 31, 2003, FHLB advances aggregating $123.0 million are callable, on a quarterly basis, after initial lockout periods. The next call date range is from January 2004 to August 2006. Aggregate maturities of long-term advances from the FHLB as of December 31, 2003 were as follows:

(in thousands)	
2004	**$ 31,200**
2005	**5,000**
2006	**35,000**
2007	**10,000**
2008	**3,000**
Thereafter	**110,189**
Total	**$194,389**

NOTE J - MINORITY INTEREST IN CONSOLIDATED SUBSIDIARY

During 2000, Citibank Properties, Inc. (CB Properties), a wholly-owned subsidiary of the Bank, elected to be taxed as a real estate investment trust (REIT). On July 18, 2000, CB Properties issued 120 shares of Series A Preferred Stock, 10,000 shares of Series B Preferred Stock, and 55,000 shares of Series C Preferred Stock at $1,000 per share in exchange for approximately $150 million in participation interests in mortgage loans and mortgage-related securities less the assumption of $85 million in advances made from the FHLB to the Bank. During 2001, CB Properties issued 1.7 million shares of common stock in exchange for approximately $128 million in participation interests in mortgage loans and mortgage-related securities, less the cancellation of $61.3 million in debt owed by CB Properties to the Bank. On August 21, 2000, the Bank sold 7,000 shares of Series B Preferred Stock to third party investors, of which 4,400 shares were repurchased at par value during 2001. This transaction was recorded as a minority interest for financial statement purposes and classified as Tier 1 capital for regulatory purposes pursuant to guidelines set forth by the Federal Deposit Insurance Corporation. CB Properties business objective is to acquire, hold, finance and manage qualifying REIT assets.

NOTE K - OTHER NONINTEREST EXPENSE

Other noninterest expense for the years ended December 31, 2003, 2002 and 2001 were as follows:

(in thousands)	2003	2002	2001
Legal and professional fees	**$ 4,599**	$ 4,740	$ 4,147
Advertising and promotion	**2,611**	2,716	2,997
Stationary, supplies, postage and delivery	**2,317**	2,070	1,867
Provision for other real estate owned losses	**176**	500	150
Deposit insurance premiums	**198**	201	227
Other	**9,508**	8,407	8,039
Total other noninterest expense	**$19,409**	$18,634	$17,427

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NOTE L - INCOME TAXES

The components of income tax expense for the years ended December 31, 2003, 2002 and 2001 were as follows:

(in thousands)	2003	2002	2001
Current:			
Federal	**$10,595**	$ 7,725	$2,571
State			593
Total current	**10,595**	7,725	3,164
Deferred:			
Federal	**(465)**	(1,191)	70
State	**(105)**	(276)	16
Total deferred	**(570)**	(1,467)	86
Total income tax expense	**$10,025**	$ 6,258	$3,250

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities as of December 31, 2003 and 2002 were as follows:

(in thousands)	2003	2002
Deferred tax assets:		
Allowance for credit losses	**$11,331**	$ 9,331
Gain on sale of building	**918**	1,402
Deferred compensation	**1,441**	705
Capital loss carryforward	**670**	1,283
Other	**638**	452
Gross deferred tax assets	**14,998**	13,173
Less: valuation allowance	**(597)**	(1,193)
Total deferred tax assets	**14,401**	11,980
Deferred tax liabilities:		
FHLB stock dividends	**8,281**	7,609
Deferred loan fees	**1,365**	3,372
Capitalized servicing	**1,032**	375
Unrealized gains on available-for-sale securities	**4,361**	4,363
Leasing activities	**2,558**	1,031
Other	**2,350**	1,349
Total deferred tax liabilities	**19,947**	18,099
Net deferred tax liabilities	**$ 5,546**	$ 6,119

The net change in the total valuation allowance for the years ended December 31, 2003 and 2002 was a decrease of $596,000 and $398,000, respectively. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences net of the existing valuation allowance at December 31, 2003.

Reconciliation of the federal statutory rate to the Company s effective income tax rate for the years ended December 31, 2003, 2002 and 2001 was as follows:

	2003	**2002**	**2001**
Federal statutory rate	**35.0%**	35.0%	35.0%
Tax exempt interest	**(1.3)**	(1.8)	(0.2)
Hawaii state franchise taxes, net of federal tax benefit			3.0
Tax exempt earnings on bank owned life insurance	**(2.1)**	(2.8)	(2.4)
Other, net	**1.0**	1.3	-0.8
Effective income tax rate	**32.6%**	31.7%	34.6%

In 2003 and 2002, the Company utilized $2.8 million and $1.8 million, respectively, of Hawaii State investment credits against its state franchise tax liability. At December 31, 2003, the Company had non-refundable state credits (unlimited carry forward) aggregating $4.4 million that become available for use at various dates through 2007.

NOTE M - DEFERRED GAIN

Previously, CB Properties entered into a limited partnership agreement as a limited partner. The partnership acquired the ground leases of certain real property, constructed a commercial building on the property and sold the leasehold estate and commercial

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building to an unrelated third party (the Purchaser). Prior to the sale, the Bank entered into a 20-year office lease agreement with the partnership for the ground floor, mezzanine and first four floors of the building. The Bank s lease was assigned to the Purchaser and has not been affected by the sale of the building.

The Company recognized a deferred gain in a manner similar to that for a sale-leaseback transaction. The deferred gain is being amortized over the remaining lease term, resulting in annual gains of $447,000. As of December 31, 2003, the unamortized deferred gain was $2,309,000.

NOTE N - RISK MANAGEMENT ACTIVITIES

Refer to Note A, Derivative Instruments and Hedging Activities, for the Company s current accounting treatment of derivative financial investments.

Interest rate contracts are primarily used to convert certain deposits or to convert certain groups of customer loans to fixed or floating rates. Certain interest rate swaps specifically match the amounts and terms of particular liabilities.

Under interest rate swaps, the Company agrees with other parties to exchange, at specified intervals, the difference between fixed rate and floating rate interest amounts calculated by reference to an agreed upon notional amount. At December 31, 2003, there were five (5) interest rate swaps outstanding, of which two (2) are classified as cash flow hedges against commercial loans, with notional principal amounts totaling $20 million. The Company paid the floating rate and received the fixed rate on the swaps hedging commercial loans. For the swaps which are not classified as cash flow hedges, the Company paid the floating rate and received the fixed rate on one (1) swap hedging commercial loans (with a notional principal amount of $10 million), and paid the fixed rate and received the floating rate on two (2) swaps hedging time deposits and short-term liabilities (with notional principal amounts totaling $10 million). The estimated fair values of the outstanding interest rate swaps were $(204,307) and $(651,322) at December 31, 2003, and December 31, 2002, respectively, and are recorded as an adjustment to investments.

The following table indicates the types of swaps used, as of December 31, their aggregate notional amounts and weighted-average interest rates, and includes the matched swaps. Average variable rates are based on rates implied in the yield curve at the reporting date. Those rates may change significantly, affecting future cash flows.

(dollars in thousands)	2003	2002	2001
Interest rate swaps:			
Pay-floating swaps-notional amount	**$30,000**	$20,000	$15,000
Average receive rate	**5.98%**	6.40%	7.29%
Average pay rate	**4.00%**	4.25%	2.07%
Pay-fixed swaps-notional amount	**$10,000**	$35,000	$
Average receive rate	**1.17%**	1.72%	%
Average pay rate	**4.17%**	3.99%	%

Interest rate options at December 31, 2003, 2002 and 2001 consisted of the following:

	2003		2002		2001	
(in thousands)	Notional Amount Value	Estimated Fair Value	Notional Amount Value	Estimated Fair Value	Notional Amount Value	Estimated Fair Value
Caps	**$**	**$ nil**	$	$ nil	$50,000	$nil
Options	**30,000**	**(230)**	30,000	(217)	5,000	(40)
Total interest rate options	**$30,000**	**$(230)**	$30,000	$(217)	$55,000	$ (40)

Interest rate lock commitments issued on residential mortgage loans expose the Company to interest rate risk, which is economically hedged with options. At December 31, 2003, the Company also had $15.0 million of forward sales on securities to hedge residential mortgage loans.

These derivatives are carried at fair value with changes in fair value recorded as a component of noninterest income in the consolidated statement of income.

Interest rate options written and purchased are contracts that allow the holder of the option to purchase or sell a financial instrument at a specified price and within a specified period of time from the seller or writer of the option. As a writer of options, the Company receives a premium at the outset and then bears the risk of an unfavorable change in the price of the financial instrument underlying the option. At December 31, 2003, 2002 and 2001, there were outstanding written option contracts with notional principal amounts of $30.0 million, $30.0 million and $5.0 million, respectively, and fair values of $(229,687), $(217,181), and $(39,844), respectively.

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NOTE O - CREDIT-RELATED INSTRUMENTS

At any time, the Company has a significant number of outstanding commitments to extend credit. These commitments take the form of approved lines of credit and loans with terms of up to one year. The Company also provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements generally extend for up to one year. The contractual amounts of these credit-related instruments are set out in the following table by category of instrument. Because many of those instruments expire without being advanced in whole or in part, the amounts do not represent future cash flow requirements.

(in thousands)	2003	2002
Loan commitments	**$391,394**	$259,104
Guarantees and letters of credit	**16,147**	6,587
Totals	**$407,541**	$265,691

These credit-related financial instruments have off-balance sheet risk because only origination fees and accruals for probable losses are recognized in the consolidated financial statements until the commitments are fulfilled or expire. Credit risk represents the accounting loss that would be recognized at the reporting date if counterparties failed completely to perform as contracted. The credit risk amounts are equal to the contractual amounts, assuming that the amounts are fully advanced and that the collateral or other security is of no value.

The Company s policy is to require suitable collateral to be provided by certain customers prior to the disbursement of approved loans. For retail loans, the Company usually retains a security interest in the property or products financed, which provides repossession rights in the event of default by the customer. Guarantees and letters of credit also are subject to strict credit assessments before being provided. Those agreements specify monetary limits to the Company s obligations. Collateral for commercial loans, guarantees, and letters of credit is usually in the form of cash, inventory, marketable securities, or other property.

NOTE P - COMMITMENTS AND CONTINGENCIES

The Company is a defendant in various legal proceedings arising from normal business activities. While the results of these proceedings cannot be predicted with certainty, management believes, based on advice of counsel, the aggregate liability, if any, resulting from these proceedings would not have a material effect on the Company s consolidated financial position or results of operations.

NOTE Q - EMPLOYEE BENEFIT PLANS

Employee Stock Ownership Plan. The Company has an Employee Stock Ownership Plan (the ESOP) for all employees of the Company who satisfy length-of-service requirements. Trust assets under the plan are invested primarily in shares of stock of the Company. Employer contributions are to be paid in cash, shares of stock or other property as determined by the Board of Directors provided, however, contributions may not be made in amounts which cannot be allocated to any participant s account by reason of statutory limitations. In October 2001, the ESOP borrowed $2,115,000 from the Bank to purchase 62,269 outstanding shares of the Company s common stock from a stockholder. The shares purchased collateralize the loan from the Bank in accordance with a stock pledge agreement. The loan will be repaid principally from the Company s contributions to the ESOP. Shares purchased with the loan proceeds are held in a suspense account for allocation to participants as the loan is repaid. Shares released from the suspense account are allocated among participants on the basis of compensation, as described in the plan. The Company accounts for its ESOP in accordance with Statement of Position 93-6, Employers Accounting for Employee Stock Ownership Plans. Accordingly, the Company reports compensation expense equal to the fair value of the shares allocated, and the allocated shares are considered outstanding for the computation of earnings per share. Dividends on allocated ESOP shares are recorded as a reduction to retained earnings. ESOP compensation expense was $898,000, $415,000, and $276,000 for 2003, 2002 and 2001, respectively. The 2003 ESOP compensation expense includes a $575,000 cash contribution for purchases of additional ESOP shares. At December 31, 2003, unreleased ESOP shares amounted to $1,323,000 and are shown as a reduction of stockholders equity in the accompanying consolidated balance sheets. The table below reflects ESOP activity for the periods indicated:

Year ended December 31,	2003	2002
Allocated shares, beginning of year	**245,197**	240,011

Shares committed to be released	**5,956**	11,422
Unallocated shares	**42,006**	47,704
Fair value of unallocated shares	**$2,630,000**	$2,028,000

Profit Sharing Retirement Savings Plan. The Company has a Profit Sharing Retirement Savings Plan for all employees who satisfy length-of-service requirements. Eligible employees may contribute up to 100% of their compensation, limited to the total amount deductible under applicable provisions of the Internal Revenue Code, of which 20% will be matched by the Company, provided that the matching contribution shall not exceed 2% of the participant s compensation. In addition, the Company contributes an amount equal to 3% of the compensation of eligible participants, and additional amounts determined by the Board of Directors at their discretion. Contributions to the plan for 2003, 2002 and 2001 were approximately $429,000, $388,000 and $366,000, respectively.

Deferred Compensation. The Company has deferred compensation agreements with several key management employees, all of whom are officers. Under the agreements, the Company is obligated to provide for each such employee or his beneficiaries, during a period of ten to eighteen years after the employee s death, disability, or retirement, annual benefits ranging from $25,000 to $250,000. The estimated present value of future benefits to be paid is being accrued over the period from the effective date of the agreements until the full eligibility dates of the participants. The expense incurred for this plan for the years ended December 31, 2003, 2002 and 2001 amounted to $52,000, $73,000 and $118,000, respectively. The Company is the beneficiary of life insurance policies, with an aggregate cash surrender value of $13,775,000 at December 31, 2003, that were purchased as a method of partially financing benefits under this plan.

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Supplemental Executive Retirement Plan. In 2002, the Company adopted a non-qualified, unfunded Supplemental Executive Retirement Plan (SERP) for certain executive officers to supplement the benefit these executive officers will receive under the Company s qualified retirement plans (or predecessor qualified retirement plans). The SERP provides annual benefits ranging from 8.9% to 65.0% of the executive s final average compensation (as defined and adjusted under the SERP) payable over the executive s remaining lifetime (assuming the executive attains age 65). The SERP also provides for survivor and certain other termination benefits.

The expense recorded in connection with the SERP was $400,000 and $300,000 for 2003 and 2002, respectively. The Company is the beneficiary of life insurance policies with an aggregate cash surrender value of $7.8 million. The Company is using these policies as a method of funding benefits under this plan.

Stock Compensation Plans. On September 16, 1994, the Board of Directors adopted a Stock Compensation Plan (the SCP) which the shareholders approved on January 26, 1995. On April 30, 1998, the stockholders approved the increase of shares of common stock reserved under the SCP to 532,400 shares. Such shares may be granted to employees, including officers and other key employees, of the Company. The purpose of the SCP is to enhance the ability of the Company to attract, retain and reward key employees and to encourage a sense of proprietorship and to stimulate the interests of those employees in the financial success of the Company. The SCP is administered by the Compensation Committee (the Committee) of the Board of Directors. The SCP provides for the award of incentive stock options, performance stock options, non-qualified stock options, stock grants and stock appreciation rights (SARs). Options granted under the SCP vest after 1 year of service from the date of grant (3 years of service for 2002 and 2003 grants).

The Company adopted the Directors Stock Option Plan (DSOP) which the shareholders approved on April 29, 1999. Under the DSOP, each director of the Company, the Bank or Datatronix, who is not an employee, receives an annual grant of options to acquire restricted stock at a price equal to the fair market value of the Company s common stock at the date of the grant. Under the DSOP, the stock option grants are exercisable from the date of the grant for a ten-year period.

The following table presents information on options outstanding under the SCP and DSOP described above:

	Options Outstanding			Options Exercisable	
Grant Price Range	**Options Outstanding**	**Weighted Average Remaining Contractual Life**	**Weighted Average Exercise Price**	**Options Exercisable**	**Weighted Average Exercise Price**
$18.41 - $20.47	16,422	5.68	$ 19.75	16,422	$ 19.75
$20.48 - $22.16	52,551	6.70	$ 21.94	52,551	$ 21.94
$22.17 - $23.51	24,527	4.99	$ 22.93	24,527	$ 22.93
$23.52 - $26.00	16,004	7.10	$ 25.97	16,004	$ 25.97
$26.01 - $31.28	21,104	8.13	$ 31.20	21,104	$ 31.20
$31.29 - $32.31	67,828	3.97	$ 32.23	67,828	$ 32.23
$32.32 - $34.96	88,305	8.43	$ 34.96		$
$34.97 - $61.61	65,750	9.75	$ 61.61		$
$61.62 - $62.57	14,300	9.26	$ 62.57	14,300	$ 62.57
	366,791	7.20	$ 36.35	212,736	$ 29.12

Transactions involving stock options are summarized as follows:

Description	Stock Options Outstanding	Weighted Average Exercise Price

Balance at December 31, 2000	344,574	$ 24.80
Granted		