

LAKELAND BANCORP INC  
Form 10-Q  
May 06, 2011  
Table of Contents

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended March 31, 2011

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 000-17820

LAKELAND BANCORP, INC.

(Exact name of registrant as specified in its charter)

New Jersey  
(State or other jurisdiction of

22-2953275  
(I.R.S. Employer

incorporation or organization)

Identification No.)

250 Oak Ridge Road, Oak Ridge, New Jersey  
(Address of principal executive offices)

07438  
(Zip Code)

(973) 697-2000

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed  
since last report.)

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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, any Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes  No  Not applicable.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act: (Check one):

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Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.):

Yes  No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of April 29, 2011 there were 25,467,678 outstanding shares of Common Stock, no par value.

**Table of Contents**

LAKELAND BANCORP, INC.

Form 10-Q Index

|                                                                                                                                          | PAGE |
|------------------------------------------------------------------------------------------------------------------------------------------|------|
| Part I Financial Information                                                                                                             |      |
| Item 1. Financial Statements:                                                                                                            |      |
| <u>Consolidated Balance Sheets - March 31, 2011 (unaudited) and December 31, 2010</u>                                                    | 1    |
| <u>Consolidated Statements of Operations - Unaudited Three Months ended March 31, 2011 and 2010</u>                                      | 2    |
| <u>Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income - Unaudited Three Months ended March 31, 2011</u> | 3    |
| <u>Consolidated Statements of Cash Flows - Unaudited Three Months ended March 31, 2011 and 2010</u>                                      | 4    |
| <u>Notes to Consolidated Financial Statements (unaudited)</u>                                                                            | 5    |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                                     | 23   |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>                                                                | 31   |
| Item 4. <u>Controls and Procedures</u>                                                                                                   | 32   |
| Part II Other Information                                                                                                                |      |
| Item 1. <u>Legal Proceedings</u>                                                                                                         | 33   |
| Item 1A. <u>Risk Factors</u>                                                                                                             | 33   |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>                                                               | 33   |
| Item 3. <u>Defaults Upon Senior Securities</u>                                                                                           | 33   |
| Item 4. <u>Reserved</u>                                                                                                                  | 33   |
| Item 5. <u>Other Information</u>                                                                                                         | 33   |
| Item 6. <u>Exhibits</u>                                                                                                                  | 33   |
| <u>Signatures</u>                                                                                                                        | 34   |

The Securities and Exchange Commission maintains a web site which contains reports, proxy and information statements and other information relating to registrants that file electronically at the address: <http://www.sec.gov>.

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries****CONSOLIDATED BALANCE SHEETS**

|                                                                                                                                                                                | March 31, 2011<br>(unaudited) | December 31,<br>2010 |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------|----------------------|
|                                                                                                                                                                                | (dollars in thousands)        |                      |
| <b>ASSETS:</b>                                                                                                                                                                 |                               |                      |
| Cash                                                                                                                                                                           | \$47,106                      | \$26,063             |
| Interest-bearing deposits due from banks                                                                                                                                       | 14,856                        | 23,215               |
| <b>Total cash and cash equivalents</b>                                                                                                                                         | <b>61,962</b>                 | <b>49,278</b>        |
| Investment securities available for sale                                                                                                                                       | 469,969                       | 487,107              |
| Investment securities held to maturity; fair value of \$72,231 in 2011 and \$68,815 in 2010                                                                                    | 70,072                        | 66,573               |
| Leases held for sale                                                                                                                                                           | 0                             | 1,517                |
| Loans, net of deferred costs                                                                                                                                                   | 1,977,446                     | 2,013,100            |
| Less: allowance for loan and lease losses                                                                                                                                      | 28,192                        | 27,331               |
| <b>Net loans</b>                                                                                                                                                               | <b>1,949,254</b>              | <b>1,987,286</b>     |
| Premises and equipment, net                                                                                                                                                    | 27,801                        | 27,554               |
| Accrued interest receivable                                                                                                                                                    | 8,583                         | 8,849                |
| Goodwill                                                                                                                                                                       | 87,111                        | 87,111               |
| Other identifiable intangible assets, net                                                                                                                                      | 312                           | 578                  |
| Bank owned life insurance                                                                                                                                                      | 43,639                        | 43,284               |
| Other assets                                                                                                                                                                   | 32,873                        | 35,054               |
| <b>TOTAL ASSETS</b>                                                                                                                                                            | <b>\$2,751,576</b>            | <b>\$2,792,674</b>   |
| <b>LIABILITIES</b>                                                                                                                                                             |                               |                      |
| Deposits:                                                                                                                                                                      |                               |                      |
| Noninterest bearing                                                                                                                                                            | \$407,099                     | \$383,877            |
| Savings and interest-bearing transaction accounts                                                                                                                              | 1,414,604                     | 1,399,163            |
| Time deposits under \$100 thousand                                                                                                                                             | 240,614                       | 241,911              |
| Time deposits \$100 thousand and over                                                                                                                                          | 176,195                       | 170,938              |
| <b>Total deposits</b>                                                                                                                                                          | <b>2,238,512</b>              | <b>2,195,889</b>     |
| Federal funds purchased and securities sold under agreements to repurchase                                                                                                     | 46,382                        | 52,123               |
| Other borrowings                                                                                                                                                               | 130,000                       | 195,000              |
| Subordinated debentures                                                                                                                                                        | 77,322                        | 77,322               |
| Other liabilities                                                                                                                                                              | 14,289                        | 11,631               |
| <b>TOTAL LIABILITIES</b>                                                                                                                                                       | <b>2,506,505</b>              | <b>2,531,965</b>     |
| Commitments and contingencies                                                                                                                                                  |                               |                      |
| <b>STOCKHOLDERS EQUITY</b>                                                                                                                                                     |                               |                      |
| Preferred stock, Series A, no par value, \$1,000 liquidation value, authorized 1,000,000 shares; issued 19,000 shares at March 31, 2011 and 39,000 shares at December 31, 2010 | 18,311                        | 37,474               |
| Common stock, no par value; authorized shares, 40,000,000; issued 25,976,648 shares at March 31, 2011 and 25,977,592 shares at December 31, 2010                               | 269,959                       | 271,595              |
| Accumulated deficit                                                                                                                                                            | (35,671)                      | (38,004)             |
| Treasury stock, at cost, 510,253 shares at March 31, 2011 and 655,768 at December 31, 2010                                                                                     | (6,735)                       | (8,683)              |

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|                                                   |                    |                    |
|---------------------------------------------------|--------------------|--------------------|
| Accumulated other comprehensive loss              | (793)              | (1,673)            |
| TOTAL STOCKHOLDERS' EQUITY                        | 245,071            | 260,709            |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b> | <b>\$2,751,576</b> | <b>\$2,792,674</b> |

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

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

|                                                                            | For the three months ended<br>March 31, |               |
|----------------------------------------------------------------------------|-----------------------------------------|---------------|
|                                                                            | 2011                                    | 2010          |
|                                                                            | (In thousands, except per share data)   |               |
| <b>INTEREST INCOME</b>                                                     |                                         |               |
| Loans, leases and fees                                                     | \$26,665                                | \$28,252      |
| Federal funds sold and interest-bearing deposits with banks                | 12                                      | 28            |
| Taxable investment securities                                              | 2,713                                   | 2,983         |
| Tax-exempt investment securities                                           | 499                                     | 520           |
| <b>TOTAL INTEREST INCOME</b>                                               | <b>29,889</b>                           | <b>31,783</b> |
| <b>INTEREST EXPENSE</b>                                                    |                                         |               |
| Deposits                                                                   | 2,931                                   | 4,405         |
| Federal funds purchased and securities sold under agreements to repurchase | 27                                      | 37            |
| Other borrowings                                                           | 2,347                                   | 2,754         |
| <b>TOTAL INTEREST EXPENSE</b>                                              | <b>5,305</b>                            | <b>7,196</b>  |
| <b>NET INTEREST INCOME</b>                                                 | <b>24,584</b>                           | <b>24,587</b> |
| Provision for loan and lease losses                                        | 4,927                                   | 4,879         |
| <b>NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES</b>       | <b>19,657</b>                           | <b>19,708</b> |
| <b>NONINTEREST INCOME</b>                                                  |                                         |               |
| Service charges on deposit accounts                                        | 2,478                                   | 2,448         |
| Commissions and fees                                                       | 832                                     | 885           |
| Gains on investment securities                                             |                                         | 1             |
| Income on bank owned life insurance                                        | 355                                     | 386           |
| Gains on leasing related assets                                            | 463                                     | 304           |
| Other income                                                               | 102                                     | 85            |
| <b>TOTAL NONINTEREST INCOME</b>                                            | <b>4,230</b>                            | <b>4,109</b>  |
| <b>NONINTEREST EXPENSE</b>                                                 |                                         |               |
| Salaries and employee benefits                                             | 8,986                                   | 8,903         |
| Net occupancy expense                                                      | 1,911                                   | 1,795         |
| Furniture and equipment                                                    | 1,164                                   | 1,170         |
| Stationery, supplies and postage                                           | 365                                     | 426           |
| Marketing expense                                                          | 615                                     | 554           |
| Core deposit intangible amortization                                       | 265                                     | 265           |
| FDIC insurance expense                                                     | 947                                     | 933           |
| Collection expense                                                         | 65                                      | 148           |
| Legal expense                                                              | 295                                     | 341           |
| Other real estate and repossessed asset expense                            | 272                                     | 37            |
| Other expenses                                                             | 2,141                                   | 2,208         |
| <b>TOTAL NONINTEREST EXPENSE</b>                                           | <b>17,026</b>                           | <b>16,780</b> |
| Income before provision for income taxes                                   | 6,861                                   | 7,037         |

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|                                                    |         |         |
|----------------------------------------------------|---------|---------|
| Income tax expense                                 | 2,090   | 2,471   |
| <b>NET INCOME</b>                                  | \$4,771 | \$4,566 |
| Dividends on Preferred Stock and Accretion         | 1,286   | 898     |
| <b>Net Income Available to Common Stockholders</b> | \$3,485 | \$3,668 |
| <b>PER SHARE OF COMMON STOCK</b>                   |         |         |
| Basic earnings                                     | \$0.14  | \$0.15  |
| Diluted earnings                                   | \$0.14  | \$0.15  |
| Dividends                                          | \$0.06  | \$0.05  |

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

**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Three Months ended March 31, 2011

|                                                                    | Common stock     |            | Series A Preferred Stock | Accumulated deficit | Treasury Stock | Accumulated Other Comprehensive Income (Loss) | Total      |
|--------------------------------------------------------------------|------------------|------------|--------------------------|---------------------|----------------|-----------------------------------------------|------------|
|                                                                    | Number of Shares | Amount     |                          |                     |                |                                               |            |
| (dollars in thousands)                                             |                  |            |                          |                     |                |                                               |            |
| BALANCE DECEMBER 31, 2010                                          | 25,977,592       | \$ 271,595 | \$37,474                 | (\$38,004)          | (\$8,683)      | (\$1,673)                                     | \$ 260,709 |
| Comprehensive income:                                              |                  |            |                          |                     |                |                                               |            |
| Net Income                                                         |                  |            |                          | 4,771               |                |                                               | 4,771      |
| Other comprehensive income, net of tax                             |                  |            |                          |                     |                | 880                                           | 880        |
| <i>Total comprehensive income</i>                                  |                  |            |                          |                     |                |                                               | 5,651      |
| Preferred dividends                                                |                  |            |                          | (449)               |                |                                               | (449)      |
| Accretion of discount                                              |                  |            | 837                      | (837)               |                |                                               |            |
| Stock based compensation                                           |                  | 155        |                          |                     |                |                                               | 155        |
| Redemption of preferred stock                                      |                  |            | (20,000)                 |                     |                |                                               | (20,000)   |
| Adjustment for stock dividend                                      | (944)            | (309)      |                          | 309                 |                |                                               |            |
| Issuance of restricted stock awards                                |                  | (1,262)    |                          |                     | 1,262          |                                               |            |
| Issuance of stock to dividend reinvestment and stock purchase plan |                  | (157)      |                          | (245)               | 550            |                                               | 148        |
| Exercise of stock options, net of excess tax benefits              |                  | (63)       |                          |                     | 136            |                                               | 73         |
| Cash dividends, common stock                                       |                  |            |                          | (1,216)             |                |                                               | (1,216)    |
| BALANCE March 31, 2011 (UNAUDITED)                                 | 25,976,648       | \$ 269,959 | \$18,311                 | (\$35,671)          | (\$6,735)      | (\$793)                                       | \$ 245,071 |

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



**Table of Contents****Lakeland Bancorp, Inc. and Subsidiaries**

## UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

|                                                                                        | For the three months ended<br>March 31, |                  |
|----------------------------------------------------------------------------------------|-----------------------------------------|------------------|
|                                                                                        | 2011                                    | 2010             |
|                                                                                        | (dollars in thousands)                  |                  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                            |                                         |                  |
| Net income                                                                             | \$4,771                                 | \$4,566          |
| Adjustments to reconcile net income to net cash provided by operating activities:      |                                         |                  |
| Net amortization of premiums, discounts and deferred loan fees and costs               | 1,514                                   | 1,047            |
| Depreciation and amortization                                                          | 1,010                                   | 1,046            |
| Provision for loan and lease losses                                                    | 4,927                                   | 4,879            |
| Gains on securities                                                                    |                                         | (1)              |
| Gains on leases                                                                        | (382)                                   | (106)            |
| Gains on sales of other assets                                                         | (35)                                    | (158)            |
| Stock-based compensation                                                               | 155                                     | 132              |
| Decrease in other assets                                                               | 1,737                                   | 2,059            |
| Increase in other liabilities                                                          | 2,791                                   | 76               |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>                                       | <b>16,488</b>                           | <b>13,540</b>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                            |                                         |                  |
| Proceeds from repayments on and maturity of securities:                                |                                         |                  |
| Available for sale                                                                     | 49,560                                  | 37,449           |
| Held to maturity                                                                       | 3,166                                   | 6,837            |
| Purchase of securities:                                                                |                                         |                  |
| Available for sale                                                                     | (32,196)                                | (56,811)         |
| Held to maturity                                                                       | (6,701)                                 | (2,380)          |
| Proceeds from sales of leases                                                          | 16,433                                  | 192              |
| Net decrease in loans and leases                                                       | 15,843                                  | 4,393            |
| Proceeds from sales of other repossessed assets                                        | 769                                     | 1,262            |
| Capital expenditures                                                                   | (991)                                   | (378)            |
| <b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>                             | <b>45,883</b>                           | <b>(9,436)</b>   |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                            |                                         |                  |
| Net increase in deposits                                                               | 42,623                                  | 45,589           |
| Decrease in federal funds purchased and securities sold under agreements to repurchase | (5,741)                                 | (6,346)          |
| Proceeds from other borrowings                                                         | 15,000                                  |                  |
| Repayments of other borrowings                                                         | (80,000)                                |                  |
| Redemption of preferred stock                                                          | (20,000)                                |                  |
| Exercise of stock options                                                              | 57                                      | 389              |
| Excess tax benefits                                                                    | 16                                      |                  |
| Issuance of stock to dividend reinvestment and stock purchase plan                     | 148                                     | 14               |
| Dividends paid                                                                         | (1,790)                                 | (1,728)          |
| <b>NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES</b>                             | <b>(49,687)</b>                         | <b>37,918</b>    |
| Net increase in cash and cash equivalents                                              | 12,684                                  | 42,022           |
| Cash and cash equivalents, beginning of year                                           | 49,278                                  | 58,663           |
| <b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>                                        | <b>\$61,962</b>                         | <b>\$100,685</b> |

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

**Table of Contents**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 1. Significant Accounting Policies**

*Basis of Presentation.*

This quarterly report presents the consolidated financial statements of Lakeland Bancorp, Inc. (the Company) and its subsidiary, Lakeland Bank (Lakeland). The accounting and reporting policies of the Company conform with accounting principles generally accepted in the United States of America (U.S. GAAP) and predominant practices within the banking industry.

The Company's unaudited interim financial statements reflect all adjustments, such as normal recurring accruals that are, in the opinion of management, necessary for fair statement of the results of interim periods presented. The results of operations for the quarter presented do not necessarily indicate the results that the Company will achieve for all of 2011. You should read these interim financial statements in conjunction with the audited consolidated financial statements and accompanying notes that are presented in the Lakeland Bancorp, Inc. Annual Report on Form 10-K for the year ended December 31, 2010.

The financial information in this quarterly report has been prepared in accordance with the Company's customary accounting practices. Certain information and footnote disclosures required under U.S. GAAP have been condensed or omitted, as permitted by rules and regulations of the Securities and Exchange Commission.

The Company evaluated its March 31, 2011 consolidated financial statements for subsequent events through the date the financial statements were issued. The Company is not aware of any subsequent events which would require recognition or disclosure in the financial statements.

**Note 2. Stock-Based Compensation**

Share-based compensation expense of \$155,000 and \$132,000 was recognized for the three months ended March 31, 2011 and 2010, respectively. As of March 31, 2011, there was unrecognized compensation cost of \$1.5 million related to unvested restricted stock; that cost is expected to be recognized over a weighted average period of approximately 4.2 years. Unrecognized compensation expense related to unvested stock options was approximately \$77,000 as of March 31, 2011 and is expected to be recognized over a period of 1.6 years.

In the first three months of 2011, the Company granted 95,345 shares of restricted stock at a fair value of \$9.87 per share under the Company's 2009 equity compensation program. These shares vest over a five year period. Compensation expense on these shares is expected to average approximately \$188,000 per year for the next five years. In the first three months of 2010, the Company granted 36,357 shares of restricted stock at a fair value of \$6.84 per share under the 2009 program. Compensation expense on these shares is expected to average approximately \$50,000 per year over a five year period.

There were no grants of stock options in the first three months of 2011 and 2010.

**Table of Contents**

Option activity under the Company's stock option plans is as follows:

|                                          | Number<br>of shares | Weighted<br>average<br>exercise<br>price | Weighted<br>average<br>remaining<br>contractual<br>term<br><br>( in<br>years) | Aggregate<br>intrinsic<br>value |
|------------------------------------------|---------------------|------------------------------------------|-------------------------------------------------------------------------------|---------------------------------|
| Outstanding, January 1, 2011             | 721,123             | \$12.77                                  |                                                                               | \$158,349                       |
| Issued                                   |                     |                                          |                                                                               |                                 |
| Exercised                                | (10,303)            | 5.49                                     |                                                                               |                                 |
| Forfeited                                |                     |                                          |                                                                               |                                 |
| Outstanding, March 31, 2011              | 710,820             | \$12.88                                  | 3.25                                                                          | \$102,509                       |
| Options exercisable at<br>March 31, 2011 | 673,624             | \$13.04                                  | 2.99                                                                          | \$65,825                        |

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of the first quarter of 2011 and the exercise price, multiplied by the number of in-the-money options).

The aggregate intrinsic value of options exercised during the first three months ended March 31, 2011 and 2010 was \$41,000 and \$34,000, respectively. Exercise of stock options during the first three months of 2011 and 2010 resulted in cash receipts of \$57,000 and \$401,000, respectively.

Information regarding the Company's restricted stock (all unvested) and changes during the three months ended March 31, 2011 is as follows:

|                              | Number of<br>shares | Weighted<br>average<br>price |
|------------------------------|---------------------|------------------------------|
| Outstanding, January 1, 2011 | 101,314             | \$9.62                       |
| Granted                      | 95,345              | 9.87                         |
| Vested                       | (3,557)             | 8.82                         |
| Forfeited                    | (417)               | 9.67                         |
| Outstanding, March 31, 2011  | 192,685             | \$9.76                       |

**Table of Contents****Note 3. Comprehensive Income**

The components of other comprehensive income are as follows:

|                                                                          | Before<br>tax amount | Tax Benefit<br>(Expense) | Net of<br>tax amount |
|--------------------------------------------------------------------------|----------------------|--------------------------|----------------------|
| (in thousands)                                                           |                      |                          |                      |
| For the quarter ended March 31, 2011                                     |                      |                          |                      |
| Net unrealized gains on available for sale securities                    |                      |                          |                      |
| Net unrealized holding gains arising during period                       | \$1,364              | (\$488)                  | \$876                |
| Less reclassification adjustment for net gains arising during the period |                      |                          |                      |
| Net unrealized gains                                                     | 1,364                | (488)                    | 876                  |
| Change in minimum pension liability                                      | 7                    | (3)                      | 4                    |
| Other comprehensive income, net                                          | \$1,371              | (\$491)                  | \$880                |
| (in thousands)                                                           |                      |                          |                      |
| For the quarter ended March 31, 2010                                     |                      |                          |                      |
| Net unrealized gains on available for sale securities                    |                      |                          |                      |
| Net unrealized holding gains arising during period                       | \$2,074              | (\$753)                  | \$1,321              |
| Less reclassification adjustment for net gains arising during the period | 1                    |                          | 1                    |
| Net unrealized gains                                                     | 2,073                | (753)                    | 1,320                |
| Change in minimum pension liability                                      | 8                    | (3)                      | 5                    |
| Other comprehensive income, net                                          | \$2,081              | (\$756)                  | \$1,325              |

**Note 4. Statement of Cash Flow Information, Supplemental Information**

|                                                                                        | For the three months ended<br>March 31, |       |
|----------------------------------------------------------------------------------------|-----------------------------------------|-------|
|                                                                                        | 2011                                    | 2010  |
| (in thousands)                                                                         |                                         |       |
| Supplemental schedule of noncash investing and financing activities:                   |                                         |       |
| Cash paid during the period for income taxes                                           | \$569                                   | \$142 |
| Cash paid during the period for interest                                               | 5,301                                   | 7,176 |
| Transfer of loans and leases into other repossessed assets and other real estate owned | 871                                     | 684   |
| Transfer of leases held for sale to leases held for investment                         | 1,517                                   |       |

**Table of Contents****Note 5. Earnings Per Share.**

All weighted average, actual share and per share information set forth in this quarterly report on Form 10-Q for the period ended March 31, 2010 have been adjusted retroactively for the effects of the stock dividend. The following schedule shows the Company's earnings per share for the periods presented:

| (In thousands except per share data)                             | For the three months ended<br>March 31, |         |
|------------------------------------------------------------------|-----------------------------------------|---------|
|                                                                  | 2011                                    | 2010    |
| Net income available to common shareholders                      | \$3,485                                 | \$3,668 |
| Less: earnings allocated to participating securities             | 24                                      | 20      |
| Net income allocated to common shareholders                      | 3,461                                   | 3,648   |
| Weighted average number of common shares outstanding - basic (1) | 25,249                                  | 25,020  |
| Share-based plans (1)                                            | 133                                     | 11      |
| Weighted average number of common shares diluted (1)             | 25,382                                  | 25,031  |
| Basic earnings per share                                         | \$0.14                                  | \$0.15  |
| Diluted earnings per share                                       | \$0.14                                  | \$0.15  |

(1) Adjusted for 5% stock dividend granted February 16, 2011 to shareholders of record January 31, 2011.

Options to purchase 702,167 shares of common stock at a weighted average price of \$12.97 per share, and 62,035 shares of restricted stock at a weighted average price of \$9.91 per share were outstanding and were not included in the computation of diluted earnings per share for the quarter ended March 31, 2011 because the exercise price and the grant-date price were greater than the average market price. Options to purchase 683,127 shares of common stock at a weighted average price of \$13.15 per share, a warrant to purchase 997,049 shares of common stock at a price of \$8.88 per share, and 110,430 shares of restricted stock at a weighted average price of \$10.57 per share were outstanding and were not included in the computation of diluted earnings per share for the quarter ended March 31, 2010 because the exercise price and the grant-date price were greater than the average market price.

**Table of Contents**
**Note 6. Investment Securities**

| AVAILABLE FOR SALE<br><br>(in thousands)         | March 31, 2011 |                        |                         |            | December 31, 2010 |                        |                         |            |
|--------------------------------------------------|----------------|------------------------|-------------------------|------------|-------------------|------------------------|-------------------------|------------|
|                                                  | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Amortized Cost    | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. government agencies                         | \$103,738      | \$208                  | (\$924)                 | \$103,022  | \$107,870         | \$294                  | \$(867)                 | \$107,297  |
| Mortgage-backed securities                       | 295,473        | 2,692                  | (2,737)                 | 295,428    | 306,882           | 2,536                  | (3,566)                 | 305,852    |
| Obligations of states and political subdivisions | 27,913         | 474                    | (166)                   | 28,221     | 27,567            | 357                    | (375)                   | 27,549     |
| Other debt securities                            | 22,057         | 154                    | (531)                   | 21,680     | 22,582            | 102                    | (811)                   | 21,873     |
| Equity securities                                | 21,197         | 479                    | (58)                    | 21,618     | 23,979            | 559                    | (2)                     | 24,536     |
|                                                  | \$470,378      | \$4,007                | \$(4,416)               | \$469,969  | \$488,880         | \$3,848                | \$(5,621)               | \$487,107  |

| HELD TO MATURITY<br><br>(in thousands)           | March 31, 2011 |                        |                         |            | December 31, 2010 |                        |                         |            |
|--------------------------------------------------|----------------|------------------------|-------------------------|------------|-------------------|------------------------|-------------------------|------------|
|                                                  | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Amortized Cost    | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. government agencies                         | \$4,997        | \$191                  | \$                      | \$5,188    | \$4,996           | \$229                  | \$                      | \$5,225    |
| Mortgage-backed securities                       | 20,851         | 1,027                  |                         | 21,878     | 20,774            | 1,105                  |                         | 21,879     |
| Obligations of states and political subdivisions | 42,658         | 936                    | (69)                    | 43,525     | 39,235            | 956                    | (84)                    | 40,107     |
| Other debt securities                            | 1,566          | 74                     |                         | 1,640      | 1,568             | 40                     | (4)                     | 1,604      |
|                                                  | \$70,072       | \$2,228                | \$(69)                  | \$72,231   | \$66,573          | \$2,330                | \$(88)                  | \$68,815   |

The following table shows investment securities by stated maturity. Securities backed by mortgages have expected maturities that differ from contractual maturities because borrowers have the right to call or prepay, and are, therefore, classified separately with no specific maturity date (in thousands):

|                                        | March 31, 2011     |            |                  |            |
|----------------------------------------|--------------------|------------|------------------|------------|
|                                        | Available for Sale |            | Held to Maturity |            |
|                                        | Amortized Cost     | Fair Value | Amortized Cost   | Fair Value |
| Due in one year or less                | \$35,225           | \$35,259   | \$16,736         | \$16,837   |
| Due after one year through five years  | 88,217             | 87,473     | 20,773           | 21,559     |
| Due after five years through ten years | 23,343             | 23,567     | 10,782           | 10,995     |
| Due after ten years                    | 6,923              | 6,624      | 930              | 962        |
|                                        | 153,708            | 152,923    | 49,221           | 50,353     |
| Mortgage-backed securities             | 295,473            | 295,428    | 20,851           | 21,878     |
| Equity securities                      | 21,197             | 21,618     |                  |            |

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|                  |           |           |          |          |
|------------------|-----------|-----------|----------|----------|
| Total securities | \$470,378 | \$469,969 | \$70,072 | \$72,231 |
|------------------|-----------|-----------|----------|----------|



**Table of Contents**

The following table shows proceeds from sales of securities, gross gains and gross losses on sales or calls of securities and other than temporary impairments for the periods indicated (in thousands):

|                                 | For the three months ended<br>March 31, |      |
|---------------------------------|-----------------------------------------|------|
|                                 | 2011                                    | 2010 |
| Sale proceeds                   | \$                                      | \$   |
| Gross gains                     |                                         | 1    |
| Gross losses                    |                                         |      |
| Other than temporary impairment |                                         |      |

Securities with a carrying value of approximately \$315.7 million and \$340.6 million at March 31, 2011 and December 31, 2010, respectively, were pledged to secure public deposits and for other purposes required by applicable laws and regulations.

The following table indicates the length of time individual securities have been in a continuous unrealized loss position at March 31, 2011 and December 31, 2010:

| March 31, 2011                                   | Less than 12 months    |                   | 12 months or longer |                   | Number of securities | Total      |                   |
|--------------------------------------------------|------------------------|-------------------|---------------------|-------------------|----------------------|------------|-------------------|
|                                                  | Fair value             | Unrealized Losses | Fair value          | Unrealized Losses |                      | Fair value | Unrealized Losses |
| AVAILABLE FOR SALE                               |                        |                   |                     |                   |                      |            |                   |
|                                                  | (dollars in thousands) |                   |                     |                   |                      |            |                   |
| U.S. government agencies                         | \$54,914               | \$924             | \$                  | \$                | 12                   | \$54,914   | \$924             |
| Mortgage-backed securities                       | 124,859                | 2,702             | 5,052               | 35                | 32                   | 129,911    | 2,737             |
| Obligations of states and political subdivisions | 6,678                  | 165               | 40                  | 1                 | 17                   | 6,718      | 166               |
| Other debt securities                            |                        |                   | 6,423               | 531               | 3                    | 6,423      | 531               |
| Equity securities                                | 4,075                  | 56                | 1                   | 2                 | 2                    | 4,076      | 58                |
|                                                  | \$190,526              | \$3,847           | \$11,516            | \$569             | 66                   | \$202,042  | \$4,416           |
| HELD TO MATURITY                                 |                        |                   |                     |                   |                      |            |                   |
| Obligations of states and political subdivisions | \$3,235                | \$60              | \$414               | \$9               | 8                    | \$3,649    | \$69              |
|                                                  | \$3,235                | \$60              | \$414               | \$9               | 8                    | \$3,649    | \$69              |

**Table of Contents**

| December 31, 2010                                | Less than 12 months |                   | 12 months or longer    |                   | Number of securities | Total      |                   |
|--------------------------------------------------|---------------------|-------------------|------------------------|-------------------|----------------------|------------|-------------------|
|                                                  | Fair value          | Unrealized Losses | Fair value             | Unrealized Losses |                      | Fair value | Unrealized Losses |
| AVAILABLE FOR SALE                               |                     |                   |                        |                   |                      |            |                   |
|                                                  |                     |                   | (dollars in thousands) |                   |                      |            |                   |
| U.S. government agencies                         | \$60,037            | \$867             | \$                     | \$                | 13                   | \$60,037   | \$867             |
| Mortgage-backed securities                       | 143,693             | 3,535             | 5,323                  | 31                | 36                   | 149,016    | 3,566             |
| Obligations of states and political subdivisions | 11,404              | 374               | 40                     | 1                 | 27                   | 11,444     | 375               |
| Other debt securities                            | 4,962               | 38                | 6,182                  | 773               | 4                    | 11,144     | 811               |
| Equity securities                                |                     |                   | 1                      | 2                 | 1                    | 1          | 2                 |
|                                                  | \$220,096           | \$4,814           | \$11,546               | \$807             | 81                   | \$231,642  | \$5,621           |
| <b>HELD TO MATURITY</b>                          |                     |                   |                        |                   |                      |            |                   |
| Obligations of states and political subdivisions | \$2,699             | \$76              | \$415                  | \$8               | 8                    | \$3,114    | \$84              |
| Other debt securities                            | 529                 | 4                 |                        |                   | 1                    | 529        | 4                 |
|                                                  | \$3,228             | \$80              | \$415                  | \$8               | 9                    | \$3,643    | \$88              |

Management has evaluated the securities in the above table and has concluded that none of the securities with unrealized losses have impairments that are other-than-temporary. In its evaluation, management considered the credit rating on the securities and the results of discounted cash flow analyses. All investment securities are evaluated on a periodic basis to determine if factors are identified that would require further analysis. In evaluating the Company's securities, management considers the following items:

- The credit ratings of the underlying issuer and if any changes in the credit rating have occurred;
- The Company's ability and intent to hold the securities, including an evaluation of the need to sell the security to meet certain liquidity measures, or whether the Company has sufficient levels of cash to hold the identified security in order to recover the entire amortized cost of the security;
- The length of time the security's fair value has been less than amortized cost; and
- Adverse conditions related to the security or its issuer if the issuer has failed to make scheduled payments or other factors.

**Note 7. Loans and Leases.**

The following sets forth the composition of Lakeland's loan and lease portfolio as of March 31, 2011 and December 31, 2010:

|                                     | March 31,<br>2011 | December 31,<br>2010 |
|-------------------------------------|-------------------|----------------------|
|                                     | (in thousands)    |                      |
| Commercial, secured by real estate  | \$973,223         | \$970,240            |
| Commercial, industrial and other    | 194,616           | 194,259              |
| Leases                              | 46,050            | 65,640               |
| Leases held for sale, at fair value |                   | 1,517                |
| Real estate-residential mortgage    | 393,935           | 403,561              |
| Real estate-construction            | 65,627            | 70,775               |
| Home equity and consumer            | 302,032           | 306,322              |
| Total loans                         | 1,975,483         | 2,012,314            |
| Plus: deferred costs                | 1,963             | 2,303                |
| Loans net of deferred costs         | \$1,977,446       | \$2,014,617          |



**Table of Contents***Non-accrual and Past Due Loans*

The following schedule sets forth certain information regarding the Company's non-accrual loans and leases, its other real estate owned and other repossessed assets, and accruing troubled debt restructurings:

| (in thousands)                                               | March 31,<br>2011 | December 31,<br>2010 |
|--------------------------------------------------------------|-------------------|----------------------|
| Commercial, secured by real estate                           | \$13,423          | \$12,905             |
| Commercial, industrial and other                             | 920               | 1,702                |
| Leases, including leases held for sale                       | 5,299             | 6,277                |
| Real estate - residential mortgage                           | 13,023            | 12,834               |
| Real estate - construction                                   | 12,779            | 6,321                |
| Home equity and consumer                                     | 3,259             | 2,930                |
| <br>                                                         |                   |                      |
| Total non-accrual loans and leases                           | \$48,703          | \$42,969             |
| Other real estate and other repossessed assets               | 1,729             | 1,592                |
| <br>                                                         |                   |                      |
| <b>TOTAL NON-PERFORMING ASSETS</b>                           | <b>\$50,432</b>   | <b>\$44,561</b>      |
| <br>                                                         |                   |                      |
| Non-performing assets as a percent of total assets           | 1.83%             | 1.60%                |
| <br>                                                         |                   |                      |
| Loans and leases past due 90 days or more and still accruing | \$2,499           | \$1,218              |
| <br>                                                         |                   |                      |
| Troubled debt restructurings, still accruing                 | \$8,356           | \$9,073              |

Non-accrual loans included \$3.2 million and \$3.6 million of troubled debt restructurings as of March 31, 2011 and December 31, 2010, respectively.

**Table of Contents**

An age analysis of past due loans, segregated by class of loans as of March 31, 2011 and December 31, 2010 is as follows:

| March 31, 2011                         | 30-59 Days<br>Past<br>Due | 60-89 Days<br>Past Due | Greater<br>Than<br>89 Days | Total<br>Past Due<br>(in thousands) | Current      | Total<br>Loans<br>and Leases | Recorded<br>Investment greater<br>than 89 Days<br>and<br>still accruing |
|----------------------------------------|---------------------------|------------------------|----------------------------|-------------------------------------|--------------|------------------------------|-------------------------------------------------------------------------|
| Commercial, secured by real estate     | \$ 11,193                 | \$ 1,755               | \$ 15,255                  | \$ 28,203                           | \$ 945,020   | \$ 973,223                   | \$ 1,833                                                                |
| Commercial, industrial and other       | 722                       | 98                     | 922                        | 1,742                               | 192,874      | 194,616                      | 1                                                                       |
| Leases                                 | 2,468                     | 1,797                  | 5,305                      | 9,570                               | 36,480       | 46,050                       | 6                                                                       |
| Real estate-residential mortgage       | 4,240                     |                        | 13,273                     | 17,513                              | 376,422      | 393,935                      | 250                                                                     |
| Real estate-construction               | 1,216                     |                        | 12,779                     | 13,995                              | 51,632       | 65,627                       |                                                                         |
| Home equity and consumer               | 2,251                     | 786                    | 3,668                      | 6,705                               | 295,327      | 302,032                      | 409                                                                     |
|                                        | \$ 22,090                 | \$ 4,436               | \$ 51,202                  | \$ 77,728                           | \$ 1,897,755 | \$ 1,975,483                 | \$ 2,499                                                                |
| December 31, 2010                      |                           |                        |                            |                                     |              |                              |                                                                         |
| Commercial, secured by real estate     | \$ 4,387                  | \$ 2,856               | \$ 13,557                  | \$ 20,800                           | \$ 949,440   | \$ 970,240                   | \$ 651                                                                  |
| Commercial, industrial and other       | 175                       | 83                     | 1,703                      | 1,961                               | 192,298      | 194,259                      | 2                                                                       |
| Leases, including leases held for sale | 20,919                    | 427                    | 6,293                      | 27,639                              | 39,518       | 67,157                       | 16                                                                      |
| Real estate-residential mortgage       | 4,867                     | 1,574                  | 13,176                     | 19,617                              | 383,944      | 403,561                      | 343                                                                     |
| Real estate-construction               | 450                       |                        | 6,321                      | 6,771                               | 64,004       | 70,775                       |                                                                         |
| Home equity and consumer               | 3,459                     | 842                    | 3,137                      | 7,438                               | 298,884      | 306,322                      | 206                                                                     |
|                                        | \$ 34,257                 | \$ 5,782               | \$ 44,187                  | \$ 84,226                           | \$ 1,928,088 | \$ 2,012,314                 | \$ 1,218                                                                |

**Table of Contents***Impaired Loans*

Impaired loans as of March 31, 2011 and December 31, 2010 are as follows:

| March 31, 2011                         | Recorded<br>Investment in<br>Impaired loans | Contractual<br>Unpaid<br>Principal<br>Balance | Specific<br>Allowance<br>(in thousands) | Interest<br>Income<br>Recognized | Average<br>Investment in<br>Impaired<br>loans |
|----------------------------------------|---------------------------------------------|-----------------------------------------------|-----------------------------------------|----------------------------------|-----------------------------------------------|
| Loans without specific allowance:      |                                             |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | \$ 11,177                                   | \$ 13,682                                     | \$                                      | \$ 41                            | \$ 11,435                                     |
| Commercial, industrial and other       |                                             | 2                                             |                                         |                                  | 54                                            |
| Leases                                 |                                             | 27                                            |                                         |                                  | 1                                             |
| Real estate-residential mortgage       | 415                                         | 415                                           |                                         |                                  | 5                                             |
| Real estate-construction               | 13,793                                      | 17,257                                        |                                         | 11                               | 7,393                                         |
| Home equity and consumer               | 610                                         | 610                                           |                                         | 5                                | 610                                           |
| Loans with specific allowance:         |                                             |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | 7,377                                       | 8,431                                         | 889                                     | 24                               | 5,931                                         |
| Commercial, industrial and other       | 974                                         | 1,115                                         | 465                                     | 1                                | 1,314                                         |
| Leases                                 | 62                                          | 64                                            | 47                                      |                                  | 61                                            |
| Real estate-residential mortgage       | 397                                         | 397                                           | 60                                      | 4                                | 397                                           |
| Real estate-construction               | 36                                          | 100                                           | 4                                       |                                  | 36                                            |
| Home equity and consumer               | 636                                         | 639                                           | 100                                     | 8                                | 636                                           |
| Total:                                 |                                             |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | \$ 18,554                                   | \$ 22,113                                     | \$ 889                                  | \$ 65                            | \$ 17,366                                     |
| Commercial, industrial and other       | 974                                         | 1,117                                         | 465                                     | 1                                | 1,368                                         |
| Leases, including leases held for sale | 62                                          | 91                                            | 47                                      |                                  | 62                                            |
| Real estate-residential mortgage       | 812                                         | 812                                           | 60                                      | 4                                | 402                                           |
| Real estate-construction               | 13,829                                      | 17,357                                        | 4                                       | 11                               | 7,429                                         |
| Home equity and consumer               | 1,246                                       | 1,249                                         | 100                                     | 13                               | 1,246                                         |
|                                        | \$ 35,477                                   | \$ 42,739                                     | \$ 1,565                                | \$ 94                            | \$ 27,873                                     |

**Table of Contents**

| December 31, 2010                      | Recorded<br>Investment in<br>Impaired<br>loans | Contractual<br>Unpaid<br>Principal<br>Balance | Specific<br>Allowance<br>(in thousands) | Interest<br>Income<br>Recognized | Average<br>Investment in<br>Impaired<br>loans |
|----------------------------------------|------------------------------------------------|-----------------------------------------------|-----------------------------------------|----------------------------------|-----------------------------------------------|
| Loans without specific allowance:      |                                                |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | \$ 14,176                                      | \$ 19,083                                     | \$                                      | \$ 206                           | \$ 11,551                                     |
| Commercial, industrial and other       | 513                                            | 530                                           |                                         |                                  | 375                                           |
| Leases, including leases held for sale |                                                |                                               |                                         |                                  |                                               |
| Real estate-residential mortgage       | 969                                            | 969                                           |                                         | 30                               | 776                                           |
| Real estate-construction               | 7,302                                          | 8,330                                         |                                         | 9                                | 3,195                                         |
| Home equity and consumer               |                                                |                                               |                                         |                                  | 123                                           |
| Loans with specific allowance:         |                                                |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | 3,992                                          | 5,191                                         | 403                                     | 6                                | 11,180                                        |
| Commercial, industrial and other       | 1,243                                          | 1,400                                         | 511                                     | 2                                | 2,485                                         |
| Leases, including leases held for sale | 91                                             | 91                                            | 49                                      |                                  | 114                                           |
| Real estate-residential mortgage       | 397                                            | 397                                           | 60                                      | 6                                | 347                                           |
| Real estate-construction               | 69                                             | 309                                           | 7                                       |                                  | 1,005                                         |
| Home equity and consumer               | 1,249                                          | 1,249                                         | 103                                     | 41                               | 529                                           |
| Total:                                 |                                                |                                               |                                         |                                  |                                               |
| Commercial, secured by real estate     | \$ 18,168                                      | \$ 24,274                                     | \$ 403                                  | \$ 212                           | \$ 22,731                                     |
| Commercial, industrial and other       | 1,756                                          | 1,930                                         | 511                                     | 2                                | 2,860                                         |
| Leases, including leases held for sale | 91                                             | 91                                            | 49                                      |                                  | 114                                           |
| Real estate-residential mortgage       | 1,366                                          | 1,366                                         | 60                                      | 36                               | 1,123                                         |
| Real estate-construction               | 7,371                                          | 8,639                                         | 7                                       | 9                                | 4,200                                         |
| Home equity and consumer               | 1,249                                          | 1,249                                         | 103                                     | 41                               | 652                                           |
|                                        | \$ 30,001                                      | \$ 37,549                                     | \$ 1,133                                | \$ 300                           | \$ 31,680                                     |

The average recorded investment in impaired loans and leases for the first three months of 2010 was \$31.3 million and the income recognized, primarily on a cash basis, on impaired loans during the first three months of 2010 was \$19,000. Interest that would have been accrued on impaired loans and leases during the first three months of 2011 and 2010 had the loans been performing under original terms would have been \$567,000 and \$648,000, respectively.

Troubled debt restructured loans are loans and leases where significant concessions have been made due to borrowers' financial difficulties. Interest on these loans and leases is either accrued or credited directly to interest income upon the receipt of cash.

*Credit Quality Indicators*

The class of loan and leases are determined by internal risk rating. Management closely and continually monitors the quality of its loans and leases and assesses the quantitative and qualitative risks arising from the credit quality of its loans and leases. It is the policy of Lakeland to require that a Credit Risk Rating be assigned to all commercial loans and loan commitments. The Credit Risk Rating System has been developed by management to provide a methodology to be used by Loan Officers, department heads and Senior Management in identifying various levels of credit risk that exist within Lakeland's loan portfolios. The risk rating system assists Senior Management in evaluating Lakeland's loan portfolio, analyzing trends, and determining the proper level of required reserves to be recommended to the Board. In assigning risk ratings, management considers, among other things, a borrower's debt service coverage, earnings strength, loan to value ratios, industry conditions and economic conditions. Management categorizes loans and commitments into a one (1) to nine (9) numerical structure with rating 1 being the strongest rating and rating 9 being the weakest. Ratings 1 through 5W are considered Pass ratings.

**Table of Contents**

The following table shows the Company's commercial loan portfolio as of March 31, 2011 and December 31, 2010, by the risk ratings discussed above (in thousands):

| March 31, 2011                        | Commercial,<br>secured by<br>real estate | Commercial,<br>Industrial<br>and other | Real<br>estate-<br>construction |
|---------------------------------------|------------------------------------------|----------------------------------------|---------------------------------|
| Risk Rating                           |                                          |                                        |                                 |
| 1                                     | \$                                       | \$ 9                                   | \$                              |
| 2                                     |                                          | 4,423                                  |                                 |
| 3                                     | 23,369                                   | 14,158                                 |                                 |
| 4                                     | 297,917                                  | 44,998                                 | 10,508                          |
| 5                                     | 505,286                                  | 93,983                                 | 33,031                          |
| 5W - Watch                            | 54,099                                   | 15,913                                 | 1,082                           |
| 6 - Other Assets Especially Mentioned | 41,548                                   | 9,955                                  | 1,773                           |
| 7 - Substandard                       | 50,833                                   | 11,133                                 | 19,233                          |
| 8 - Doubtful                          | 171                                      | 44                                     |                                 |
| 9 - Loss                              |                                          |                                        |                                 |
| <b>Total</b>                          | <b>\$ 973,223</b>                        | <b>\$ 194,616</b>                      | <b>\$ 65,627</b>                |

| December 31, 2010                     | Commercial,<br>secured by<br>real estate | Commercial,<br>Industrial<br>and other | Real<br>estate-<br>construction |
|---------------------------------------|------------------------------------------|----------------------------------------|---------------------------------|
| Risk Rating                           |                                          |                                        |                                 |
| 1                                     | \$                                       | \$ 9                                   | \$                              |
| 2                                     |                                          | 4,454                                  |                                 |
| 3                                     | 30,704                                   | 14,279                                 |                                 |
| 4                                     | 280,478                                  | 41,018                                 | 10,317                          |
| 5                                     | 495,798                                  | 102,217                                | 35,627                          |
| 5W - Watch                            | 61,383                                   | 14,925                                 | 1,908                           |
| 6 - Other Assets Especially Mentioned | 48,382                                   | 6,593                                  | 17,361                          |
| 7 - Substandard                       | 53,291                                   | 10,205                                 | 5,562                           |
| 8 - Doubtful                          | 204                                      | 559                                    |                                 |
| 9 - Loss                              |                                          |                                        |                                 |
| <b>Total</b>                          | <b>\$ 970,240</b>                        | <b>\$ 194,259</b>                      | <b>\$ 70,775</b>                |

The risk rating tables above do not include consumer or residential loans or leases because they are evaluated on their performing status.



**Table of Contents**

*Allowance for Loan and Lease Losses*

The following table details activity in the allowance for loan and lease losses by portfolio segment and the related recorded investment in loans and leases:

| <b>Quarter ended<br/>March 31, 2011<br/>Allowance for Loan and<br/>Lease Losses:</b> | Commercial,<br>secured<br>by<br>real<br>estate | Commercial,<br>industrial<br>and other | Leases           | Real estate-<br>residential<br>mortgage | Real<br>estate-<br>construction | Home<br>equity and<br>consumer | Total               |
|--------------------------------------------------------------------------------------|------------------------------------------------|----------------------------------------|------------------|-----------------------------------------|---------------------------------|--------------------------------|---------------------|
|                                                                                      | (in thousands)                                 |                                        |                  |                                         |                                 |                                |                     |
| Beginning Balance                                                                    | \$ 11,366                                      | \$ 5,113                               | \$ 3,477         | \$ 2,628                                | \$ 2,176                        | \$ 2,571                       | \$ 27,331           |
| Charge-offs                                                                          | (523)                                          | (698)                                  | (1,090)          | (295)                                   | (2,436)                         | (633)                          | (\$5,675)           |
| Recoveries                                                                           | 958                                            | 100                                    | 503              | 1                                       |                                 | 47                             | \$ 1,609            |
| Provision                                                                            | 1,060                                          | 735                                    | (776)            | 1,003                                   | 2,154                           | 751                            | \$ 4,927            |
| <b>Ending Balance</b>                                                                | <b>\$ 12,861</b>                               | <b>\$ 5,250</b>                        | <b>\$ 2,114</b>  | <b>\$ 3,337</b>                         | <b>\$ 1,894</b>                 | <b>\$ 2,736</b>                | <b>\$ 28,192</b>    |
| Ending Balance: Individually evaluated for impairment                                | \$ 889                                         | \$ 465                                 | \$ 47            | \$ 60                                   | \$ 4                            | \$ 100                         | \$ 1,565            |
| Ending Balance: Collectively evaluated for impairment                                | 11,972                                         | 4,785                                  | 2,067            | 3,277                                   | 1,890                           | 2,636                          | \$ 26,627           |
| <b>Ending Balance</b>                                                                | <b>\$ 12,861</b>                               | <b>\$ 5,250</b>                        | <b>\$ 2,114</b>  | <b>\$ 3,337</b>                         | <b>\$ 1,894</b>                 | <b>\$ 2,736</b>                | <b>\$ 28,192</b>    |
| <b>Loans and Leases:</b>                                                             |                                                |                                        |                  |                                         |                                 |                                |                     |
| Ending Balance: Individually evaluated for impairment                                | \$ 18,554                                      | \$ 974                                 | \$ 62            | \$ 812                                  | \$ 13,829                       | \$ 1,246                       | \$ 35,477           |
| Ending Balance: Collectively evaluated for impairment                                | 954,669                                        | 193,642                                | 45,988           | 393,123                                 | 51,798                          | 300,786                        | \$ 1,940,006        |
| <b>Ending Balance (1)</b>                                                            | <b>\$ 973,223</b>                              | <b>\$ 194,616</b>                      | <b>\$ 46,050</b> | <b>\$ 393,935</b>                       | <b>\$ 65,627</b>                | <b>\$ 302,032</b>              | <b>\$ 1,975,483</b> |

(1) Excludes deferred costs

**Table of Contents**

| <b>Year ended December 31, 2010</b>                   | Commercial,<br>secured<br>by<br>real<br>estate | Commercial,<br>industrial<br>and other | Leases           | Real estate-<br>residential<br>mortgage | Real<br>estate-<br>construction | Home<br>equity and<br>consumer | Total               |
|-------------------------------------------------------|------------------------------------------------|----------------------------------------|------------------|-----------------------------------------|---------------------------------|--------------------------------|---------------------|
| (in thousands)                                        |                                                |                                        |                  |                                         |                                 |                                |                     |
| Beginning Balance                                     | \$ 9,285                                       | \$ 4,647                               | \$ 4,308         | \$ 1,286                                | \$ 3,198                        | \$ 2,839                       | \$ 25,563           |
| Charge-offs                                           | (7,510)                                        | (3,298)                                | (4,307)          | (397)                                   | (1,756)                         | (2,250)                        | (\$19,518)          |
| Recoveries                                            | 134                                            | 62                                     | 1,391            | 7                                       |                                 | 411                            | \$ 2,005            |
| Provision                                             | 9,457                                          | 3,702                                  | 2,085            | 1,732                                   | 734                             | 1,571                          | \$ 19,281           |
| <b>Ending Balance</b>                                 | <b>\$ 11,366</b>                               | <b>\$ 5,113</b>                        | <b>\$ 3,477</b>  | <b>\$ 2,628</b>                         | <b>\$ 2,176</b>                 | <b>\$ 2,571</b>                | <b>\$ 27,331</b>    |
| Ending Balance: Individually evaluated for impairment | \$ 403                                         | \$ 511                                 | \$ 49            | \$ 60                                   | \$ 7                            | \$ 103                         | \$ 1,133            |
| Ending Balance: Collectively evaluated for impairment | 10,963                                         | 4,602                                  | 3,428            | 2,568                                   | 2,169                           | 2,468                          | \$ 26,198           |
| <b>Ending Balance</b>                                 | <b>\$ 11,366</b>                               | <b>\$ 5,113</b>                        | <b>\$ 3,477</b>  | <b>\$ 2,628</b>                         | <b>\$ 2,176</b>                 | <b>\$ 2,571</b>                | <b>\$ 27,331</b>    |
| <b>Loans and Leases:</b>                              |                                                |                                        |                  |                                         |                                 |                                |                     |
| Ending Balance: Individually evaluated for impairment | \$ 18,168                                      | \$ 1,756                               | \$ 91            | \$ 1,366                                | \$ 7,371                        | \$ 1,249                       | \$ 30,001           |
| Ending Balance: Collectively evaluated for impairment | 952,072                                        | 192,503                                | 65,549           | 402,195                                 | 63,404                          | 305,073                        | \$ 1,980,796        |
| <b>Ending Balance(1)</b>                              | <b>\$ 970,240</b>                              | <b>\$ 194,259</b>                      | <b>\$ 65,640</b> | <b>\$ 403,561</b>                       | <b>\$ 70,775</b>                | <b>\$ 306,322</b>              | <b>\$ 2,010,797</b> |

(1) Excludes leases held for sale and deferred costs  
*Leases*

Lakeland had no leases held for sale as of March 31, 2011, compared to \$1.5 million as of December 31, 2010. Management recorded mark-to-market adjustments on the pools of leases based on indications of interest from potential buyers, and sales prices of similar leases previously sold adjusted for differences in types of collateral and other characteristics. During the first quarter of 2011, management reclassified \$1.5 million of leases held for sale as held for investment because management's intent regarding these leases had changed. The following table shows the components of gains on leasing related assets for the periods presented:

|                                   | For the three months ended<br>March 31, |      |
|-----------------------------------|-----------------------------------------|------|
|                                   | 2011                                    | 2010 |
| (in thousands)                    |                                         |      |
| Gains on sales of leases          | \$143                                   | \$10 |
| Realized gains on paid off leases | 239                                     | 136  |
| Gains on other repossessed assets | 81                                      | 158  |

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|                                       |       |       |
|---------------------------------------|-------|-------|
| Total gains on leasing related assets | \$463 | \$304 |
|---------------------------------------|-------|-------|

### *Other Real Estate and Other Repossessed Assets*

At March 31, 2011, the Company had other repossessed assets and other real estate owned of \$590,000 and \$1.1 million, respectively. At December 31, 2010, the Company had other repossessed assets and other real estate owned of \$558,000 and \$1.0 million, respectively.

**Table of Contents****Note 8. Employee Benefit Plans**

The components of net periodic pension cost for the Newton Trust Company's defined benefit pension plan are as follows:

|                                                 | For the three months ended<br>March 31, |      |
|-------------------------------------------------|-----------------------------------------|------|
|                                                 | 2011                                    | 2010 |
|                                                 | (in thousands)                          |      |
| Interest cost                                   | \$24                                    | \$24 |
| Expected return on plan assets                  | (22)                                    | (20) |
| Amortization of unrecognized net actuarial loss | 12                                      | 14   |
| Net periodic benefit expense                    | \$14                                    | \$18 |

**Note 9. Directors Retirement Plan**

The components of net periodic plan costs for the directors' retirement plan are as follows:

|                                                 | For the three months ended<br>March 31, |      |
|-------------------------------------------------|-----------------------------------------|------|
|                                                 | 2011                                    | 2010 |
|                                                 | (in thousands)                          |      |
| Service cost                                    | \$6                                     | \$7  |
| Interest cost                                   | 12                                      | 12   |
| Amortization of prior service cost              | 4                                       | 8    |
| Amortization of unrecognized net actuarial loss | 2                                       | 2    |
| Net periodic benefit expense                    | \$24                                    | \$29 |

The Company made contributions of \$63,000 and \$80,000 to the plan during the three months ended March 31, 2011 and 2010, respectively. The Company expects to make \$25,000 in contributions to the plan in the second quarter of 2011 and does not expect to make any more contributions for the remainder of 2011.

**Note 10. Estimated Fair Value of Financial Instruments and Fair Value Measurement**

U.S. GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest level priority to unobservable inputs (level 3 measurements). The following describes the three levels of fair value hierarchy:

Level 1 unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 quoted prices for similar assets or liabilities in active markets; or quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs other than quoted prices that are observable for the asset or liability.

Level 3 unobservable inputs for the asset or liability that reflect the Company's own assumptions about assumptions that market participants would use in the pricing of the asset or liability and that are consequently not based on market activity but upon particular valuation techniques

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The Company's assets that are measured at fair value on a recurring basis are its available for sale investment securities. The Company obtains fair values on its securities using information from a third party servicer. Standard inputs include benchmark yields, reported trades, broker-dealer quotes, issuer spreads, bids and offers. If quoted prices for securities are available in an active market, those securities are classified as Level 1 securities. The Company has certain equity securities that are classified as Level 1 securities. If quoted prices in active markets are not available, fair values are estimated by the use of pricing models. Level 2 securities were primarily comprised of U.S. Agency bonds, mortgage-backed securities, obligations of state and political subdivisions and corporate securities.

**Table of Contents**

The following table sets forth the Company's financial assets that were accounted for at fair value on a recurring basis as of the periods presented by level within the fair value hierarchy. The Company had no liabilities accounted for at fair value as of March 31, 2011 or December 31, 2010. During the three months ended March 31, 2011, the Company did not make any transfers between recurring Level 1 fair value measurements and recurring Level 2 fair value measurements. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

| <u>March 31, 2011</u>                            | Quoted Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
|--------------------------------------------------|-------------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|------------------------|
| (in thousands)                                   |                                                                                     |                                                           |                                                    |                        |
| <b>Assets:</b>                                   |                                                                                     |                                                           |                                                    |                        |
| Investment securities, available for sale        |                                                                                     |                                                           |                                                    |                        |
| US government agencies                           | \$                                                                                  | \$103,022                                                 | \$                                                 | \$103,022              |
| Mortgage backed securities                       |                                                                                     | 295,428                                                   |                                                    | 295,428                |
| Obligations of states and political subdivisions |                                                                                     | 28,221                                                    |                                                    | 28,221                 |
| Corporate debt securities                        |                                                                                     | 21,680                                                    |                                                    | 21,680                 |
| Equity securities                                | 2,088                                                                               | 19,530                                                    |                                                    | 21,618                 |
| Total securities available for sale              | \$2,088                                                                             | \$467,881                                                 | \$                                                 | \$469,969              |

December 31, 2010

|                                                  |         |           |    |           |
|--------------------------------------------------|---------|-----------|----|-----------|
| <b>Assets:</b>                                   |         |           |    |           |
| Investment securities, available for sale        |         |           |    |           |
| US government agencies                           | \$      | \$107,297 | \$ | \$107,297 |
| Mortgage backed securities                       |         | 305,852   |    | 305,852   |
| Obligations of states and political subdivisions |         | 27,549    |    | 27,549    |
| Corporate debt securities                        |         | 21,873    |    | 21,873    |
| Equity securities                                | 2,090   | 22,446    |    | 24,536    |
| Total securities available for sale              | \$2,090 | \$485,017 | \$ | \$487,107 |

The following table sets forth the Company's assets subject to fair value adjustments (impairment) on a nonrecurring basis. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

| <u>March 31, 2011</u>                                | Quoted Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair Value |
|------------------------------------------------------|-------------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|---------------------|
| (in thousands)                                       |                                                                                     |                                                           |                                                    |                     |
| <b>Assets:</b>                                       |                                                                                     |                                                           |                                                    |                     |
| Impaired Loans and Leases                            |                                                                                     |                                                           |                                                    |                     |
|                                                      | \$                                                                                  | \$                                                        | \$ 35,477                                          | \$ 35,477           |
| Other real estate owned and other repossessed assets |                                                                                     |                                                           | 1,729                                              | 1,729               |

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December 31, 2010

**Assets:**

|                                                      |        |           |
|------------------------------------------------------|--------|-----------|
| Impaired Loans and Leases                            | 30,001 | \$ 30,001 |
| Other real estate owned and other repossessed assets | 1,592  | \$ 1,592  |

Impaired loans and leases are evaluated and valued at the time the loan is identified as impaired at the lower of cost or market value. Because most of Lakeland's impaired loans are collateral dependant, fair value is measured based on the value of the collateral securing these loans and leases and is classified at a level 3 in the fair value hierarchy. Collateral may be real estate, accounts receivable, inventory, equipment and/or other business assets. The value of the real estate is assessed based on appraisals by qualified third party licensed appraisers. The value of the equipment may be determined by an appraiser, if

**Table of Contents**

significant, inquiry through a recognized valuation resource, or by the value on the borrower's financial statements. Field examiner reviews on business assets may be conducted based on the loan exposure and reliance on this type of collateral. Appraised and reported values may be discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Impaired loans and leases are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors identified above.

Other real estate owned (OREO) and other repossessed assets, representing property acquired through foreclosure, are carried at fair value less estimated disposal costs of the acquired property.

Changes in the assumptions or methodologies used to estimate fair values may materially affect the estimated amounts. Also, management is concerned that there may not be reasonable comparability between institutions due to the wide range of permitted assumptions and methodologies in the absence of active markets. This lack of uniformity gives rise to a high degree of subjectivity in estimating financial instrument fair values.

Estimated fair values have been determined by the Company using the best available data and an estimation methodology suitable for each category of financial instruments. The estimation methodologies used, the estimated fair values, and recorded book balances at March 31, 2011 and December 31, 2010 are outlined below.

The net loan portfolio at March 31, 2011 and December 31, 2010 has been valued using a present value discounted cash flow where market prices were not available. The discount rate used in these calculations is the estimated current market rate adjusted for credit risk. The carrying value of accrued interest approximates fair value.

The estimated fair values of demand deposits (i.e. interest (checking) and non-interest bearing demand accounts, savings and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e. their carrying amounts). The carrying amounts of variable rate accounts approximate their fair values at the reporting date. For fixed maturity certificates of deposit, fair value was estimated using the rates currently offered for deposits of similar remaining maturities. The carrying amount of accrued interest payable approximates its fair value.

The fair value of federal funds purchased, securities sold under agreements to repurchase, long-term debt and subordinated debentures are based upon the discounted value of contractual cash flows. The Company estimates the discount rate using the rates currently offered for similar borrowing arrangements.

The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.



**Table of Contents**

The carrying values and estimated fair values of the Company's financial instruments are as follows:

|                                                                            | March 31,<br>2011 |                         | December 31,<br>2010 |                         |
|----------------------------------------------------------------------------|-------------------|-------------------------|----------------------|-------------------------|
|                                                                            | Carrying<br>Value | Estimated<br>fair value | Carrying<br>Value    | Estimated<br>fair value |
| (in thousands)                                                             |                   |                         |                      |                         |
| <b>Financial Assets:</b>                                                   |                   |                         |                      |                         |
| Cash and cash equivalents                                                  | \$61,962          | \$61,962                | \$49,278             | \$49,278                |
| Investment securities available for sale                                   | 469,969           | 469,969                 | 487,107              | 487,107                 |
| Investment securities held to maturity                                     | 70,072            | 72,231                  | 66,573               | 68,815                  |
| Loans, including leases held for sale                                      | 1,977,446         | 1,972,713               | 2,014,617            | 2,008,192               |
| <b>Financial Liabilities:</b>                                              |                   |                         |                      |                         |
| Deposits                                                                   | 2,238,512         | 2,241,051               | 2,195,889            | 2,199,018               |
| Federal funds purchased and securities sold under agreements to repurchase | 46,382            | 46,382                  | 52,123               | 52,123                  |
| Other borrowings                                                           | 130,000           | 144,424                 | 195,000              | 209,631                 |
| Subordinated debentures                                                    | 77,322            | 77,596                  | 77,322               | 78,707                  |
| <b>Commitments:</b>                                                        |                   |                         |                      |                         |
| Standby letters of credit                                                  |                   | 94                      |                      | 78                      |

**Note 11. Preferred Stock**

On March 16, 2011, the Company redeemed 20,000 shares of its Fixed Rate Cumulative Preferred Stock, Series A originally issued to the U.S. Department of the Treasury under the Troubled Asset Relief Program Capital Purchase Program. The Company paid to the Treasury \$20.1 million, which included \$20.0 million of principal and \$86,000 in accrued and unpaid dividends, on March 16, 2011. As a result of the early payment, the Company also accelerated the accretion of \$745,000 of the preferred stock discount during the three months ended March 31, 2011. The warrant previously issued to the Treasury to purchase 997,049 shares of common stock at an exercise price of \$8.88, subject to anti-dilution adjustments, remains outstanding.

**Note 12. Recent Accounting Pronouncements**

In December 2010, the Financial Accounting Standards Board (the "FASB") issued accounting guidance that modifies Step One of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step Two of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist such as if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. This guidance was effective for interim and annual reporting periods beginning on or after December 15, 2010 and did not have a significant impact on the Company's financial statements.

In April 2011, the FASB issued accounting guidance to help creditors in determining whether a creditor has granted a concession and whether a debtor is experiencing financial difficulties for purposes of determining whether a restructuring constitutes a troubled debt restructuring. The purpose of this guidance is to eliminate diversity in practice and provide greater comparability between companies' financial statements. This guidance is effective for interim and annual reporting periods beginning on or after June 15, 2011 and should be applied retrospectively to the beginning of the annual period of adoption. Adoption of this guidance is not expected to have a significant impact on the Company's financial statements.

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**Table of Contents**

**PART I ITEM 2**

**Management's Discussion and Analysis of  
Financial Condition and Results of Operations**

This section should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

**Statements Regarding Forward Looking Information**

The information disclosed in this document includes various forward-looking statements that are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 with respect to credit quality (including delinquency trends and the allowance for loan and lease losses), corporate objectives, and other financial and business matters. The words anticipates, projects, intends, estimates, expects, believes, plans, may, will, should, could, and other similar expressions are intended to identify such forward-looking statements. Company cautions that these forward-looking statements are necessarily speculative and speak only as of the date made, and are subject to numerous assumptions, risks and uncertainties, all of which may change over time. Actual results could differ materially from such forward-looking statements.

In addition to the risk factors disclosed elsewhere in this document, the following factors, among others, could cause the Company's actual results to differ materially and adversely from such forward-looking statements: changes in the financial services industry and the U.S. and global capital markets, changes in economic conditions nationally, regionally and in the Company's markets, the nature and timing of actions of the Federal Reserve Board and other regulators, the nature and timing of legislation affecting the financial services industry including, but not limited to, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, government intervention in the U.S. financial system, passage by the U.S. Congress of legislation which unilaterally amends the terms of the U.S. Treasury Department's preferred stock investment in the Company, changes in levels of market interest rates, pricing pressures on loan and deposit products, credit risks of the Company's lending and leasing activities, customers' acceptance of the Company's products and services and competition.

The above-listed risk factors are not necessarily exhaustive, particularly as to possible future events, and new risk factors may emerge from time to time. Certain events may occur that could cause the Company's actual results to be materially different than those described in the Company's periodic filings with the Securities and Exchange Commission. Any statements made by the Company that are not historical facts should be considered to be forward-looking statements. The Company is not obligated to update and does not undertake to update any of its forward-looking statements made herein.

**Critical Accounting Policies, Judgments and Estimates**

The accounting and reporting policies of the Company and its subsidiaries conform with accounting principles generally accepted in the United States of America and predominant practices within the banking industry. The consolidated financial statements include the accounts of the Company, Lakeland, Lakeland NJ Investment Corp., Lakeland Investment Corp., Lakeland Equity, Inc., and Lakeland Preferred Equity, Inc. All intercompany balances and transactions have been eliminated. Lakeland Preferred Equity, Inc. is a Real Estate Investment Trust formed by Lakeland in the fourth quarter of 2010.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. There have been no material changes in the Company's critical accounting policies, judgments and estimates, including assumptions or estimation techniques utilized, as compared to those disclosed in the Company's most recent Annual Report on Form 10-K.

The Company tests goodwill for impairment annually or when circumstances indicate a potential for impairment at the reporting unit level. The Company has determined that it has one reporting unit, Community Banking. The Company analyzes goodwill using various methodologies including an income approach and a market approach. The income approach calculates cash flows to a potential acquirer based on the anticipated financial results assuming a change in control transaction. The market approach includes a comparison of pricing multiples in recent acquisitions of similar companies and applies these multiples to the Company. The Company tested the goodwill as of November 30, 2010 and determined that it is not impaired. There were no triggering events since November 30, 2010 that would cause the Company to do an interim valuation.



**Table of Contents**

**Results of Operations**

**(First Quarter 2011 Compared to First Quarter 2010)**

**Net Income**

Net income for the first quarter of 2011 was \$4.8 million, compared to net income of \$4.6 million for the same period in 2010. Net income available to common shareholders was \$3.5 million compared to net income of \$3.7 million for the same period last year. Diluted earnings per share was \$0.14 for the first quarter of 2011, compared to diluted earnings per share of \$0.15 per share for the same period last year. As previously reported, the Company repaid \$20.0 million of the outstanding \$39.0 million in preferred stock to the U.S. Department of the Treasury under the Capital Purchase Program in the first quarter of 2011. In doing so, a non-cash charge of \$745,000 was recorded, reflecting the acceleration of the preferred stock discount accretion. The effect of this non-cash charge was (\$0.03) per diluted share.

**Net Interest Income**

Net interest income on a tax equivalent basis for the first quarter of 2011 was \$24.9 million, which was equivalent to net interest income earned in the first quarter of 2010. The net interest margin decreased from 3.99% in the first quarter of 2010 to 3.91% in the first quarter of 2011, primarily as a result of a 40 basis point decline in the yield on interest-earning assets, which was partially offset by a 36 basis point reduction in the cost of interest-bearing liabilities. The net interest spread as a result declined five basis points to 3.73%. Although the net interest spread declined, the decline was mitigated by an increase in income earned on free funds (interest earning assets funded by non-interest bearing liabilities) resulting from an increase in average non-interest bearing deposits of \$71.7 million. The components of net interest income will be discussed in greater detail below.

The following table reflects the components of the Company's net interest income, setting forth for the periods presented, (1) average assets, liabilities and stockholders' equity, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, (4) the Company's net interest spread (i.e., the average yield on interest-earning assets less the average cost of interest-bearing liabilities) and (5) the Company's net interest margin. Rates are computed on a tax equivalent basis using a tax rate of 35%.

**Table of Contents**

|                                                       | For the three months ended,<br>March 31, 2011 |                                |                                                               | For the three months ended,<br>March 31, 2010 |                                |                                     |
|-------------------------------------------------------|-----------------------------------------------|--------------------------------|---------------------------------------------------------------|-----------------------------------------------|--------------------------------|-------------------------------------|
|                                                       | Average<br>Balance                            | Interest<br>Income/<br>Expense | Average<br>rates<br>earned/<br>paid<br>(dollars in thousands) | Average<br>Balance                            | Interest<br>Income/<br>Expense | Average<br>rates<br>earned/<br>paid |
| <b>Assets</b>                                         |                                               |                                |                                                               |                                               |                                |                                     |
| Interest-earning assets:                              |                                               |                                |                                                               |                                               |                                |                                     |
| Loans and leases (A)                                  | \$ 2,000,057                                  | \$ 26,665                      | 5.41%                                                         | \$ 2,009,389                                  | \$ 28,252                      | 5.70%                               |
| Taxable investment securities                         | 476,688                                       | 2,713                          | 2.28%                                                         | 405,645                                       | 2,983                          | 2.94%                               |
| Tax-exempt securities                                 | 67,594                                        | 768                            | 4.54%                                                         | 62,493                                        | 800                            | 5.12%                               |
| Federal funds sold (B)                                | 32,896                                        | 12                             | 0.15%                                                         | 48,105                                        | 28                             | 0.23%                               |
| Total interest-earning assets                         | 2,577,235                                     | 30,158                         | 4.74%                                                         | 2,525,632                                     | 32,063                         | 5.14%                               |
| Noninterest-earning assets:                           |                                               |                                |                                                               |                                               |                                |                                     |
| Allowance for loan and lease losses                   | (28,874)                                      |                                |                                                               | (26,383)                                      |                                |                                     |
| Other assets                                          | 249,178                                       |                                |                                                               | 252,544                                       |                                |                                     |
| <b>TOTAL ASSETS</b>                                   | <b>\$ 2,797,539</b>                           |                                |                                                               | <b>\$ 2,751,793</b>                           |                                |                                     |
| <b>Liabilities and Stockholders' Equity</b>           |                                               |                                |                                                               |                                               |                                |                                     |
| Interest-bearing liabilities:                         |                                               |                                |                                                               |                                               |                                |                                     |
| Savings accounts                                      | \$ 322,225                                    | \$ 127                         | 0.16%                                                         | \$ 313,025                                    | \$ 186                         | 0.24%                               |
| Interest-bearing transaction accounts                 | 1,093,625                                     | 1,505                          | 0.56%                                                         | 1,075,203                                     | 2,364                          | 0.89%                               |
| Time deposits                                         | 413,481                                       | 1,299                          | 1.26%                                                         | 471,699                                       | 1,855                          | 1.57%                               |
| Borrowings                                            | 294,106                                       | 2,374                          | 3.23%                                                         | 279,086                                       | 2,791                          | 4.00%                               |
| Total interest-bearing liabilities                    | 2,123,437                                     | 5,305                          | 1.00%                                                         | 2,139,013                                     | 7,196                          | 1.36%                               |
| Noninterest-bearing liabilities:                      |                                               |                                |                                                               |                                               |                                |                                     |
| Demand deposits                                       | 400,891                                       |                                |                                                               | 329,152                                       |                                |                                     |
| Other liabilities                                     | 13,063                                        |                                |                                                               | 12,319                                        |                                |                                     |
| Stockholders' equity                                  | 260,148                                       |                                |                                                               | 271,309                                       |                                |                                     |
| <b>TOTAL LIABILITIES AND<br/>STOCKHOLDERS' EQUITY</b> | <b>\$ 2,797,539</b>                           |                                |                                                               | <b>\$ 2,751,793</b>                           |                                |                                     |
| Net interest income/spread                            |                                               | 24,853                         | 3.73%                                                         |                                               | 24,867                         | 3.78%                               |
| Tax equivalent basis adjustment                       |                                               | 269                            |                                                               |                                               | 280                            |                                     |
| <b>NET INTEREST INCOME</b>                            |                                               | <b>\$ 24,584</b>               |                                                               |                                               | <b>\$ 24,587</b>               |                                     |
| Net interest margin (C)                               |                                               |                                | 3.91%                                                         |                                               |                                | 3.99%                               |

(A) Includes non-accrual loans, the effect of which is to reduce the yield earned on loans, and deferred loan fees.

(B) Includes interest-bearing cash accounts.

(C) Net interest income divided by interest-earning assets.

Interest income on a tax equivalent basis decreased from \$32.1 million in the first quarter of 2010 to \$30.2 million in the first quarter of 2011, a decrease of \$1.9 million, or 6%. The decrease in interest income was due to a 40 basis point decrease in the yield on interest earning assets, as a result of the declining rate environment and a change in the mix of interest-earning assets. The yield on average loans and leases at 5.41% in the first quarter of 2011 was 29 basis points lower than the first quarter of 2010. The yield on average taxable and tax exempt investment securities decreased by 66 basis points and 58 basis points, respectively, in the first quarter of 2011. Average loans and leases as a percentage of interest-earning assets decreased from 80% in the first three months of 2010 to 78% in 2011, while average investment securities increased from 19% of interest-earning assets to 21%. Loans and leases typically earn higher yields than investment securities.

Total interest expense decreased from \$7.2 million in the first quarter of 2010 to \$5.3 million in the first quarter of 2011, a decrease of \$1.9 million, or 26%. The cost of average interest-bearing liabilities decreased from 1.36% in the first quarter of 2010 to 1.00% in 2011. The decrease in yield was due to the declining rate environment along with a change in the mix of interest-bearing liabilities. Average rates paid on interest-bearing liabilities declined in all categories. Savings and interest-bearing transaction accounts as a percent of interest-bearing liabilities increased from 65% in the first quarter of 2010 to 67% in the first quarter of 2011. Time deposits as a percent of interest-bearing liabilities declined from 22% in the first quarter of 2010 to 19% in the first quarter of 2011 as customers preferred to keep their deposits in short-term transaction accounts in the current low rate environment. Average borrowings increased from \$279.1 million in the first quarter of 2010 to \$294.1 million in 2011.

**Provision for Loan and Lease Losses**

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In determining the provision for loan and lease losses, management considers national and local economic conditions; trends in the portfolio including orientation to specific loan types or industries; experience, ability and depth of lending

**Table of Contents**

management in relation to the complexity of the portfolio; adequacy and adherence to policies, procedures and practices; levels and trends in delinquencies, impaired loans and leases; net charge-offs, and the results of independent third party loan and lease review.

In the first quarter of 2011, a \$4.9 million provision for loan and lease losses was recorded, which was comparable to the provision for the same period last year. During the first quarter of 2011, the Company charged off loans of \$5.7 million and recovered \$1.6 million in previously charged off loans and leases compared to \$4.1 million and \$535,000, respectively, during the same period in 2010. For more information regarding the determination of the provision, see Risk Elements below.

**Noninterest Income**

Noninterest income increased \$121,000, or 3%, to \$4.2 million in the first quarter of 2011 compared to the first quarter of 2010. The increase in noninterest income was due primarily to gains on leasing related assets, which were \$463,000 in the first quarter of 2011 compared to gains of \$304,000 in the first quarter of 2010. Commissions and fees totaled \$832,000 in the first quarter of 2011 and were \$53,000 or 6% lower than the same period last year due primarily to a reduction in investment commission income and loan fees. Income on bank owned life insurance at \$355,000 was \$31,000 less than the same period last year primarily as a result of decreases in rates for the underlying policies.

**Noninterest Expense**

Noninterest expense totaling \$17.0 million increased \$246,000, or 1%, in the first quarter of 2011 from the first quarter of 2010. Net occupancy expense at \$1.9 million increased \$116,000 compared to the first quarter of 2010 due primarily to increased snow removal costs. Stationery, supplies and postage at \$365,000 in the first quarter decreased \$61,000 primarily as a result of a reduction in postage expense due to the implementation of electronic statement delivery. Marketing expense totaling \$615,000 increased \$61,000, or 11%, compared to the first quarter of 2010 due primarily to an increase in incentives and the timing of media expenses incurred. Collection expense at \$65,000 and legal expense at \$295,000 decreased \$83,000 and \$46,000, respectively, while other real estate and repossessed asset expense at \$272,000 increased \$235,000. The Company's efficiency ratio, a non-GAAP financial measure, was 56.7% in the first quarter of 2011, compared to 56.9% for the same period last year reflecting continued management of expenses. The Company uses this ratio because it believes that the ratio provides a good comparison of period-to-period performance and because the ratio is widely accepted in the banking industry. The following table shows the calculation of the efficiency ratio:

|                                                             | For the three months ended<br>March 31, |           |
|-------------------------------------------------------------|-----------------------------------------|-----------|
|                                                             | 2011                                    | 2010      |
|                                                             | (dollars in thousands)                  |           |
| <b>Calculation of efficiency ratio</b>                      |                                         |           |
| Total noninterest expense                                   | \$ 17,026                               | \$ 16,780 |
| Less:                                                       |                                         |           |
| Amortization of core deposit intangibles                    | (265)                                   | (265)     |
| Other real estate owned and other repossessed asset expense | (272)                                   | (37)      |
| Noninterest expense, as adjusted                            | \$ 16,489                               | \$ 16,478 |
| Net interest income                                         | \$ 24,584                               | \$ 24,587 |
| Noninterest income                                          | 4,230                                   | 4,109     |
| Total revenue                                               | 28,814                                  | 28,696    |
| Plus: Tax-equivalent adjustment on municipal securities     | 269                                     | 280       |
| Less: gains on investment securities                        |                                         | (1)       |
| Total revenue, as adjusted                                  | \$ 29,083                               | \$ 28,975 |
| Efficiency ratio                                            | 56.70%                                  | 56.87%    |





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## **Table of Contents**

### **Income Taxes**

The Company's effective tax rate was 30.5% in the first quarter of 2011, compared to 35.1% in the first quarter of 2010. The decrease in the effective tax rate was driven by increased tax benefits attributable to the real estate investment trust ( REIT ) subsidiary established in December 2010.

### **Financial Condition**

The Company's total assets decreased \$41.1 million from \$2.79 billion at December 31, 2010, to \$2.75 billion at March 31, 2011 due primarily to a 2% reduction in total loans. Total deposits increased 2%, with non-interest bearing transaction accounts increasing 6%. A reduction in other borrowings of \$65.0 million resulted from the increase in deposits and the decline in loans.

### **Loans and Leases**

Gross loans and leases, including leases held for sale, at \$1.97 billion decreased by \$36.8 million from December 31, 2010. The decrease in gross loans and leases is primarily due to leases at \$46.1 million and residential mortgages at \$394.0 million decreasing \$21.1 million and \$9.6 million, respectively. Additionally, construction loans declined from \$70.8 million to \$65.5 million, a decline of \$5.1 million or 7% because repayments on construction loans have not been replaced with new construction loans due to the continued economic downturn. For more information on the loan portfolio, see Note 7 in Notes to the Consolidated Financial Statements in this Quarterly Report on Form 10-Q.

### **Risk Elements**

Non-performing assets increased from \$44.6 million, or 1.60% of total assets, on December 31, 2010 to \$50.4 million, or 1.83% of total assets, on March 31, 2011. The majority of the increase was due to real estate construction loan non-accruals, which increased \$6.5 million from December, 31 2010 as a result of one loan being placed on a non-accrual status which totaled \$6.6 million. Leases on non-accrual decreased \$978,000 from December 31, 2010 to \$5.3 million on March 31, 2011. Non-accrual leases include \$4.0 million in net receivables related to one lessee who has named the Company and other unrelated parties in a complaint in connection with the leases. For more information, please see Legal Proceedings in Item 1 of Part II of this Quarterly Report on Form 10-Q. Commercial loan non-accruals at March 31, 2011 included six loan relationships with balances over \$1.0 million, totaling \$16.8 million, and nine loan relationships between \$500,000 and \$1.0 million, totaling \$6.5 million.

Loans and leases past due ninety days or more and still accruing at March 31, 2011 increased \$1.3 million to \$2.5 million from \$1.2 million on December 31, 2010. Loans and leases past due 90 days or more and still accruing are those loans and leases that are considered both well-secured and in process of collection.

On March 31, 2011, the Company had \$8.4 million in loans that were troubled debt restructurings and still accruing interest income compared to \$9.1 million on December 31, 2010. Troubled debt restructurings are those loans where the Company has granted concessions to the borrower in payment terms, either in rate or in term, as a result of the financial condition of the borrower.

On March 31, 2011, the Company had \$35.5 million in impaired loans and leases (consisting primarily of non-accrual and restructured loans and leases) compared to \$30.0 million at year-end 2010. Impaired loans increased from year-end 2010 as a result of the increase in non-accrual construction loans. For more information on these loans and leases see Note 7 in Notes to the Consolidated Financial Statements of this Quarterly Report on Form 10-Q. The impairment of the loans and leases is measured using the present value of future cash flows on certain impaired loans and leases and is based on the fair value of the underlying collateral for the remaining loans and leases. Based on such evaluation, \$1.6 million has been allocated as a portion of the allowance for loan and lease losses for impairment at March 31, 2011. At March 31, 2011, the Company also had \$50.8 million in loans and leases that were rated substandard that were not classified as non-performing or impaired.

There were no loans and leases at March 31, 2011, other than those designated non-performing, impaired or substandard, where the Company was aware of any credit conditions of any borrowers or obligors that would indicate a strong possibility of the borrowers not complying with present terms and conditions of repayment and which may result in such loans

**Table of Contents**

and leases being included as non-accrual, past due or renegotiated at a future date. The following table sets forth for the periods presented, the historical relationships among the allowance for loan and lease losses, the provision for loan and lease losses, the amount of loans and leases charged-off and the amount of loan and lease recoveries:

| (dollars in thousands)                                                                   | Three months<br>ended<br>March 31,<br>2011 | Three months<br>ended<br>March 31,<br>2010 | Year ended<br>December 31,<br>2010 |
|------------------------------------------------------------------------------------------|--------------------------------------------|--------------------------------------------|------------------------------------|
| Balance of the allowance at the beginning of the year                                    | \$ 27,331                                  | \$ 25,563                                  | \$ 25,563                          |
| <b>Loans and leases charged off:</b>                                                     |                                            |                                            |                                    |
| Commercial, secured by real estate (1)                                                   | 2,959                                      | 2,241                                      | 9,266                              |
| Commercial, industrial and other                                                         | 698                                        | 198                                        | 3,298                              |
| Leases                                                                                   | 1,090                                      | 1,147                                      | 4,307                              |
| Real estate mortgage                                                                     | 295                                        |                                            | 397                                |
| Home Equity and consumer                                                                 | 633                                        | 555                                        | 2,250                              |
| <b>Total loans charged off</b>                                                           | <b>5,675</b>                               | <b>4,141</b>                               | <b>19,518</b>                      |
| <b>Recoveries:</b>                                                                       |                                            |                                            |                                    |
| Commercial, secured by real estate (1)                                                   | 958                                        |                                            | 134                                |
| Commercial, industrial and other                                                         | 100                                        |                                            | 62                                 |
| Leases                                                                                   | 503                                        | 483                                        | 1,391                              |
| Real estate mortgage                                                                     | 1                                          |                                            | 7                                  |
| Home Equity and consumer                                                                 | 47                                         | 52                                         | 411                                |
| <b>Total Recoveries</b>                                                                  | <b>1,609</b>                               | <b>535</b>                                 | <b>2,005</b>                       |
| <b>Net charge-offs:</b>                                                                  | <b>4,066</b>                               | <b>3,606</b>                               | <b>17,513</b>                      |
| Provision for loan and lease losses                                                      | 4,927                                      | 4,879                                      | 19,281                             |
| <b>Ending balance</b>                                                                    | <b>\$ 28,192</b>                           | <b>\$ 26,836</b>                           | <b>\$ 27,331</b>                   |
| Ratio of annualized net charge-offs to average loans and leases outstanding              | 0.81%                                      | 0.73%                                      | 0.88%                              |
| Ratio of allowance at end of period as a percentage of period end total loans and leases | 1.43%                                      | 1.34%                                      | 1.36%                              |

(1) Includes construction real estate loans

The ratio of the allowance for loan and lease losses to loans and leases outstanding reflects management's evaluation of the underlying credit risk inherent in the loan portfolio. The determination of the adequacy of the allowance for loan and lease losses and periodic provisioning for estimated losses included in the consolidated financial statements is the responsibility of management and the Board of Directors. The evaluation process is undertaken on a quarterly basis.

Methodology employed for assessing the adequacy of the allowance for loan and lease losses consists of the following criteria:

The establishment of reserve amounts for all specifically identified classified loans and leases that have been designated as requiring attention by the Company or its external loan review consultants.

The establishment of reserves for pools of homogeneous types of loans and leases not subject to specific review, including impaired commercial loans under \$250,000, 1-4 family residential mortgages and consumer loans.

The establishment of reserve amounts for the non-classified loans and leases in each portfolio based upon the historical average loss experience of these portfolios and management's evaluation of key factors described below. Consideration is given to the results of ongoing credit quality monitoring processes, the adequacy and expertise of the

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## **Table of Contents**

Company's lending staff, underwriting policies, loss histories, delinquency trends, and the cyclical nature of economic and business conditions. Since many of the Company's loans depend on the sufficiency of collateral as a secondary means of repayment, any adverse trend in the real estate markets could affect underlying values available to protect the Company against loss.

While non-performing loans and leases increased from \$43.0 million on December 31, 2010 to \$48.7 million on March 31, 2011, the allowance for loan and lease losses as a percent of total loans increased to 1.43% of total loans on March 31, 2011, compared to 1.36% as of December 31, 2010. As discussed above, the increase in non-performing loans was related primarily to one real estate construction loan. Management believes, based on appraisals and estimated selling costs, that its non-performing loans and leases are adequately secured and reserves on these loans are adequate. The preceding statement constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

Based upon the process employed and giving recognition to all accompanying factors related to the loan and lease portfolio, management considers the allowance for loan and lease losses to be adequate at March 31, 2011. The preceding statement constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

### **Investment Securities**

For detailed information on the composition and maturity distribution of the Company's investment securities portfolio, see the Notes to Consolidated Financial Statements contained in this Form 10-Q. Total investment securities decreased from \$553.7 million on December 31, 2010 to \$540.0 million on March 31, 2011, a decrease of \$13.6 million, or 2%.

### **Deposits**

Total deposits increased from \$2.20 billion on December 31, 2010 to \$2.24 billion on March 31, 2011, an increase of \$42.6 million, or 2%. Noninterest bearing deposits increased \$23.2 million, or 6%, to \$407.1 million, resulting primarily from an increase in commercial noninterest bearing deposits. Savings and interest-bearing transaction accounts totaling \$1.41 billion increased \$15.4 million from December 31, 2010.

### **Liquidity**

Liquidity relates to the Company's ability to meet the borrowing and cash withdrawal requirements of its customers, to meet current and planned expenditures and to satisfy its debt obligations. Lakeland funds its liquidity needs through its net income, through generating deposits, through sales of its available for sale securities, through loan repayments, and through use of overnight credit lines. Lakeland can also generate funds by utilizing long-term debt or securities sold through agreements to repurchase that would be collateralized by security or mortgage collateral. Management and the Board monitor the Company's liquidity through the Asset Liability Management Committee (the ALCO) which monitors the Company's compliance to certain regulatory ratios and various other liquidity guidelines.

The cash flow statements for the periods presented provide an indication of the Company's sources and uses of cash, as well as an indication of the ability of the Company to maintain an adequate level of liquidity. A discussion of the cash flow statement for the three months ended March 31, 2011 follows.

Cash and cash equivalents, totaling \$62.0 million on March 31, 2011, increased \$12.7 million from December 31, 2010. Operating activities provided \$16.5 million in net cash. Investing activities provided \$45.9 million in net cash, primarily reflecting maturities and repayments of securities, sales of leases and the net decrease in loans and leases. Financing activities used \$49.7 million in net cash, reflecting repayments of other borrowings and the redemption of \$20.0 million in preferred stock, partially offset by an increase in deposits. The Company anticipates that it will have sufficient funds available to meet its current loan commitments and deposit maturities. This constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

The following table sets forth contractual obligations and other commitments representing required and potential cash outflows as of March 31, 2011. Interest on subordinated debentures and long-term borrowed funds is calculated based on current contractual interest rates.

**Table of Contents**

| (dollars in thousands)                                    | Total               | Within<br>one year | After one<br>but within<br>three years | After three<br>but within<br>five years | After<br>five<br>years |
|-----------------------------------------------------------|---------------------|--------------------|----------------------------------------|-----------------------------------------|------------------------|
| Minimum annual rentals or noncancellable operating leases | \$13,712            | \$1,779            | \$3,004                                | \$2,515                                 | \$6,414                |
| Benefit plan commitments                                  | 5,055               | 185                | 370                                    | 300                                     | 4,200                  |
| Remaining contractual maturities of time deposits         | 416,809             | 321,637            | 77,314                                 | 16,700                                  | 1,158                  |
| Subordinated debentures                                   | 77,322              |                    |                                        |                                         | 77,322                 |
| Loan commitments                                          | 435,876             | 361,717            | 41,994                                 | 2,215                                   | 29,950                 |
| Long-term debt                                            | 130,000             | 15,000             | 30,000                                 | 40,000                                  | 45,000                 |
| Interest on long-term debt*                               | 121,026             | 9,178              | 16,442                                 | 13,082                                  | 82,324                 |
| Series A Preferred Stock                                  | 19,000              |                    |                                        |                                         | 19,000                 |
| Interest on Series A Preferred Stock                      | 11,398              | 950                | 1,997                                  | 3,539                                   | 4,912                  |
| Standby letters of credit                                 | 9,464               | 7,155              | 2,092                                  | 137                                     | 80                     |
| <b>Total</b>                                              | <b>\$ 1,239,662</b> | <b>\$ 717,601</b>  | <b>\$ 173,213</b>                      | <b>\$ 78,488</b>                        | <b>\$ 270,360</b>      |

\*Includes interest on long-term debt and subordinated debentures at a weighted rate of 4.47%.

**Capital Resources**

Total stockholders' equity decreased from \$260.7 million on December 31, 2010 to \$245.1 million on March 31, 2011, a decrease of \$15.6 million, or 6%. Book value per common share increased to \$8.90 on March 31, 2011 from \$8.82 on December 31, 2010. The decrease in stockholders' equity from December 31, 2010 to March 31, 2011 was primarily due to the \$20.0 million redemption of preferred stock and payment of cash dividends of \$1.8 million. This was partially offset by \$4.8 million in net income and a \$880,000 increase in accumulated other comprehensive income relating to an increase in market value in the Company's available for sale securities portfolio.

The Company and Lakeland are subject to various regulatory capital requirements that are monitored by federal banking agencies. Failure to meet minimum capital requirements can lead to certain supervisory actions by regulators; any supervisory action could have a direct material effect on the Company or Lakeland's financial statements. Management believes, as of March 31, 2011, that the Company and Lakeland meet all capital adequacy requirements to which they are subject.

The capital ratios for the Company and Lakeland at March 31, 2011 are as follows:

| Capital Ratios:                                     | Tier 1 Capital<br>to Total Average<br>Assets Ratio<br>March 31,<br>2011 | Tier 1 Capital<br>to Risk-Weighted<br>Assets Ratio<br>March 31,<br>2011 | Total Capital<br>to Risk-Weighted<br>Assets Ratio<br>March 31,<br>2011 |
|-----------------------------------------------------|-------------------------------------------------------------------------|-------------------------------------------------------------------------|------------------------------------------------------------------------|
| The Company                                         | 7.79%                                                                   | 10.72%                                                                  | 13.10%                                                                 |
| Lakeland Bank                                       | 8.07%                                                                   | 11.11%                                                                  | 12.36%                                                                 |
| Well capitalized institution under FDIC Regulations | 5.00%                                                                   | 6.00%                                                                   | 10.00%                                                                 |

**Non-GAAP Financial Measures**

Reported amounts are presented in accordance with U.S. GAAP. The Company's management believes that the supplemental non-GAAP information, which consists of measurements and ratios based on tangible equity and tangible assets, is utilized by regulators and market analysts to evaluate a company's financial condition and therefore, such information is useful to investors. These disclosures should not be viewed as a substitute for financial results determined in accordance with U.S. GAAP, nor are they necessarily comparable to non-GAAP performance measures which may be presented by other companies.

**Table of Contents**

| (dollars in thousands, except per share amounts)                               | March 31,<br>2011                                | December 31,<br>2010 |
|--------------------------------------------------------------------------------|--------------------------------------------------|----------------------|
| <b>Calculation of tangible book value per common share</b>                     |                                                  |                      |
| Total common stockholders' equity at end of period - GAAP                      | \$226,760                                        | \$223,235            |
| Less:                                                                          |                                                  |                      |
| Goodwill                                                                       | 87,111                                           | 87,111               |
| Other identifiable intangible assets, net                                      | 312                                              | 578                  |
| <b>Total tangible common stockholders' equity at end of period - Non- GAAP</b> | <b>\$139,337</b>                                 | <b>\$135,546</b>     |
| Shares outstanding at end of period                                            | 25,466                                           | 25,322               |
| <b>Book value per share - GAAP</b>                                             | <b>\$8.90</b>                                    | <b>\$8.82</b>        |
| <b>Tangible book value per share - Non-GAAP</b>                                | <b>\$5.47</b>                                    | <b>\$5.35</b>        |
| <b>Calculation of tangible common equity to tangible assets</b>                |                                                  |                      |
| Total tangible common stockholders' equity at end of period - Non- GAAP        | \$139,337                                        | \$135,546            |
| Total assets at end of period                                                  | \$2,751,576                                      | \$2,792,674          |
| Less:                                                                          |                                                  |                      |
| Goodwill                                                                       | 87,111                                           | 87,111               |
| Other identifiable intangible assets, net                                      | 312                                              | 578                  |
| <b>Total tangible assets at end of period - Non-GAAP</b>                       | <b>\$2,664,153</b>                               | <b>\$2,704,985</b>   |
| Common equity to assets - GAAP                                                 | 8.24%                                            | 7.99%                |
| <b>Tangible common equity to tangible assets - Non-GAAP</b>                    | <b>5.23%</b>                                     | <b>5.01%</b>         |
|                                                                                | For the three months ended,<br>March 31,<br>2011 | March 31,<br>2010    |
| <b>Calculation of return on average tangible common equity</b>                 |                                                  |                      |
| Net income - GAAP                                                              | \$4,771                                          | \$4,566              |
| Total average common stockholders' equity                                      | 226,051                                          | \$215,228            |
| Less:                                                                          |                                                  |                      |
| Average goodwill                                                               | 87,111                                           | 87,111               |
| Average other identifiable intangible assets, net                              | 460                                              | 1,521                |
| <b>Total average tangible common stockholders' equity - Non-GAAP</b>           | <b>\$138,480</b>                                 | <b>\$126,596</b>     |
| <b>Return on average common stockholders' equity - GAAP</b>                    | <b>8.56%</b>                                     | <b>8.60%</b>         |
| <b>Return on average tangible common stockholders' equity - Non-GAAP</b>       | <b>13.97%</b>                                    | <b>14.63%</b>        |

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

The Company manages interest rate risk and market risk by identifying and quantifying interest rate risk exposures using simulation analysis and economic value at risk models. Net interest income simulation considers the relative sensitivities of the balance sheet including the effects of interest rate caps on adjustable rate mortgages and the relatively stable aspects of core deposits. As such, net interest income simulation is designed to address the probability of interest rate changes and the

**Table of Contents**

behavioral response of the balance sheet to those changes. Market Value of Portfolio Equity represents the fair value of the net present value of assets, liabilities and off-balance-sheet items. Changes in estimates and assumptions made for interest rate sensitivity modeling could have a significant impact on projected results and conclusions. These assumptions could include prepayment rates, sensitivity of non-maturity deposits and other similar assumptions. Therefore, if our assumptions should change, this technique may not accurately reflect the impact of general interest rate movements on the Company's net interest income or net portfolio value.

The starting point (or "base case") for the following table is an estimate of the following year's net interest income assuming that both interest rates and the Company's interest-sensitive assets and liabilities remain at period-end levels. The net interest income estimated for the next twelve months (the base case) is \$97.2 million. The information provided for net interest income assumes that changes in interest rates of plus 200 basis points and minus 200 basis points change gradually in equal increments ("rate ramp") over the twelve month period.

| Rate Ramp                    | Changes in interest rates |         |         |         |
|------------------------------|---------------------------|---------|---------|---------|
|                              | +200 bp                   | +100 bp | -100 bp | -200 bp |
| Asset/Liability Policy Limit | -5.0%                     |         |         | -5.0%   |
| March 31, 2011               | -2.8%                     | -1.3%   | -1.8%   | -2.6%   |
| December 31, 2010            | -3.3%                     | -1.5%   | -1.9%   | -2.6%   |

The base case for the following table is an estimate of the Company's net portfolio value for the periods presented using current discount rates, and assuming the Company's interest-sensitive assets and liabilities remain at period-end levels. The net portfolio value at March 31, 2011 (the base case) was \$340.9 million. The information provided for the net portfolio value assumes fluctuations or "rate shocks" of plus 200 basis points and minus 200 basis points for changes in interest rates as shown in the table below. Rate shocks assume that current interest rates change immediately.

| Rate Shock                   | Changes in interest rates |        |        |        |
|------------------------------|---------------------------|--------|--------|--------|
|                              | +200bp                    | +100bp | -100bp | -200bp |
| Asset/Liability Policy Limit | -25.0%                    |        |        | -25.0% |
| March 31, 2011               | -6.8%                     | -1.4%  | -1.9%  | -7.7%  |
| December 31, 2010            | -7.9%                     | -2.0%  | -2.5%  | -8.6%  |

The information set forth in the above tables is based on significant estimates and assumptions, and constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995. For more information regarding the Company's market risk and assumptions used in the Company's simulation models, please refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

**ITEM 4. Controls and Procedures**

(a) **Disclosure controls and procedures.** As of the end of the Company's most recently completed fiscal quarter covered by this report, the Company carried out an evaluation, with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-15. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and are operating in an effective manner and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) **Changes in internal controls over financial reporting.** There have been no changes in the Company's internal control over financial reporting that occurred during the quarter ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.



**Table of Contents**

**PART II OTHER INFORMATION**

Item 1. Legal Proceedings

A complaint, dated February 24, 2010, was filed by the International Association of Machinists and Aerospace Workers, as plaintiff, against the Company and other unrelated parties in the Circuit Court of Maryland for Prince George's County. The plaintiff alleges fraudulent conduct in connection with certain equipment leases it entered into by a vendor and lease broker not affiliated with the Company. Certain of these leases were subsequently assigned to Lakeland resulting in the plaintiff amending its complaint to include all parties that were assignees. The Company believes that the claims asserted against it are without merit.

A complaint, dated April 6, 2011, was filed by the bankruptcy trustee appointed in the Sunbridge Capital, Inc. bankruptcy case pending before the United States Bankruptcy Court for the District of Kansas. The trustee alleges preferential payments and constructive fraudulent transfers under the Bankruptcy Code and Kansas law. Lakeland believes that the claims asserted against it are without merit.

Other than as described above, there are no pending legal proceedings involving the Company or Lakeland other than those arising in the normal course of business. Management does not anticipate that the potential liability, if any, arising out of such legal proceedings will have a material effect on the financial condition or results of operations of the Company and Lakeland on a consolidated basis.

Item 1A. Risk Factors

There have been no material changes in risk factors from those disclosed under Item 1A, Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

|                                                                     |                |
|---------------------------------------------------------------------|----------------|
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | Not Applicable |
| Item 3. Defaults Upon Senior Securities                             | Not Applicable |
| Item 4. Reserved                                                    |                |
| Item 5. Other Information                                           | Not Applicable |
| Item 6. Exhibits                                                    |                |

- 31.1 Certification by Thomas J. Shara pursuant to Section 302 of the Sarbanes Oxley Act.
- 31.2 Certification by Joseph F. Hurley pursuant to Section 302 of the Sarbanes Oxley Act.
- 32.1 Certification by Thomas J. Shara and Joseph F. Hurley pursuant to Section 906 of the Sarbanes Oxley Act.

**Table of Contents**

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Lakeland Bancorp, Inc.  
(Registrant)

/s/ Thomas J. Shara  
Thomas J. Shara  
President and Chief Executive Officer

/s/ Joseph F. Hurley  
Joseph F. Hurley  
Executive Vice President and  
Chief Financial Officer

Date: May 6, 2011