Welcome to America's Most Convenient Bank®

Pennsylvania Commerce Bancorp

2003 Annual Report

Building Our Brand...

Contents

Commerce Bank's prototype store is a hallmark of the Commerce brand and the Bank's unique retail approach. Each store is uniform in design and appearance, making Customers feel at home at any one they visit. Exteriors are neatly landscaped with ample parking and easy roadway access. Spacious interiors feature the Penny Arcade, a free coin counting machine, and an historic mural with local appeal.

One Brick at a Time

2003 At-a-Glance

Highlights

- Total assets surpassed $1 billion in 2003, double the assets held just three years ago
- Deposits rose by $180 million, a 25% increase over 2002
- Loans grew by $106 million, an increase of 29%
- Revenues were up 24%, reaching $43.9 million
- With an exceptional debut in Berks County, the Bank's footprint extended to five Pennsylvania counties
- Five offices were added to our convenient branch network, making 2003 a record-breaking year for new store openings

4th Quarter Financial Highlights

Total Assets	$ 1.1 Billion	+34%
Total Deposits	907 Million	+25%
Total Loans (Net)	470 Million	+29%
Total Revenues	12.9 Million	+34%
Total Expenses	9.8 Million	+42%
Net Income	1.7 Million	+10%

Recognition

- In June, *The Patriot-News* named Commerce Bank to its Superstar Leaders list for the second year in a row
- In July, *U.S. Banker* recognized Commerce Bank as the No. 1 performer in its footprint and one of the top-performing publicly traded community banks in the country
- In October, the *Central Penn Business Journal* named Commerce Bank to its Top Fifty Fastest Growing Companies list for the seventh year in a row

Letter to Shareholders

Gary L. Nalbandian
Chairman of the Board,
President and CEO

Dear Shareholders, Customers and Friends:

What began as a single-office bank at Erford Road and Senate Avenue in Camp Hill, Cumberland County, reached a major milestone in 2003. Through our one-of-a-kind model, an instantly identifiable brand and the opening of a record five new store locations – including our first stores in the Reading region – Pennsylvania Commerce Bancorp grew into a multi-regional bank with 23 offices and assets in excess of $1 billion.

Our expansion into the Reading Region of Berks County put us into a market which adjoins Montgomery County, where our sister bank, Commerce Bancorp, NA, operates stores as part of its Philadelphia region. Commerce Bancorp (NYSE: CBH) is headquartered in Cherry Hill, New Jersey and has $23 billion in assets and a network of more than 275 stores throughout New Jersey, New York, southeastern Pennsylvania and Delaware.

In 1985, at the foundation of our company, we entered into a special licensing agreement with Commerce Bancorp to utilize their unique retail business model. From distinctive facilities, to 7-day-a-week branch banking, to a relentless Customer focus, our affiliation with Commerce Bancorp in the operation of "America's Most Convenient Bank" coupled with our local ownership and management, have been the cornerstones of Commerce Bank Harrisburg's success.

Commerce's unique approach to banking continues to distinguish us as the only true financial services retailer in our footprint. From seven-day branch banking to our "WOW! the Customer" service philosophy, from state-of-the-art online banking to our SMART Principles, the Commerce banking experience remains beyond compare.

An Enduring Model

Year after year, Commerce Bank produces stellar financial results. Our exceptional performance derives from a simple concept … the value of a bank is its core deposits, which can be grown by combining unsurpassed Customer service with:

- Same-store deposit growth; and
- Aggressive expansion.

The success of the Commerce model is made possible by the Commerce Team — renowned for pulling out all the stops to provide a rewarding Customer experience.

A Distinct Brand

Commerce Bank is "America's Most Convenient Bank." This is the foundation of our brand. It defines us, unifies us and is our promise to Customers.

In the spirit of convenience, we pioneered seven-day branch banking nearly a decade ago. "Convenience" permeates our products, our services, our thinking, our actions and our culture. At Commerce Bank, we truly live our brand.

We offer free, state-of-the-art online banking with "pay anyone" bill pay, and 24/7 telephone banking with access to live Customer Service Representatives. Additionally, Customers can use the Commerce ATM/Visa® Check Card at any ATM worldwide or anywhere Visa is accepted — with no fees from us.

Growing More Convenient

Commerce Bank always has maintained that gaining and retaining Customers starts with convenient and unmatched face-to-face service. That's why opening more stores is a fundamental part of our strategy.

In 2003, we opened a record five new locations. Commerce debuted in Berks County with the opening of offices in Exeter and Muhlenberg townships. Our presence in the East Shore region of Harrisburg grew by three offices: the Progress Avenue and Union Deposit stores in Susquehanna Township and the Derry Street store in Swatara Township. At year-end, our convenient branch network grew to a total of 23 stores in five counties.

The Commerce Experience

Commerce employees at every level are encouraged to exceed Customer expectations at every opportunity. Among our ranks, we call our unique brand of personalized service "WOW! the Customer" service.

To continually reinforce this philosophy, we employ a variety of creative programs and incentives. For example, we reward employees for identifying "stupid rules." Anyone, in any position within the organization, is encouraged to point out policies or procedures that stand in the way of providing the best service possible. We also reward employees for winning ideas submitted to our "Idea Bank" that result in new ways to "WOW!" Customers.

Record Results

The Directors, management and staff of Pennsylvania Commerce Bancorp are pleased to report that our unique approach to banking produced a year of record results for 2003.

- Assets increased by 34% to $1.1 billion
- Deposits rose by $180 million, a 25% increase over 2002
- Loans grew by $106 million, an increase of 29%

Left to right: Chief Retail Officer David B. Skerpon, Chief Lending Officer Rory G. Ritrievi and Chief Financial Officer Mark A. Zody

Letter to Shareholders

- Revenues were up 24%, reaching $43.9 million
- Net income grew by 16% to $6.6 million
- Earnings per share on a diluted basis was $2.68, an increase of 13%

The Future

Now in our 19th year of service, we aim to double our assets to $2 billion and grow our branch network to 36 convenient offices by 2006.

We'll work toward that goal in 2004 by adding new stores in Central Pennsylvania and in Berks County. To accommodate our growing operations staff and training program, we also expect to begin construction on a new state-of-the-art Headquarters/Operations and Training Center in the TecPort Business Center in Harrisburg.

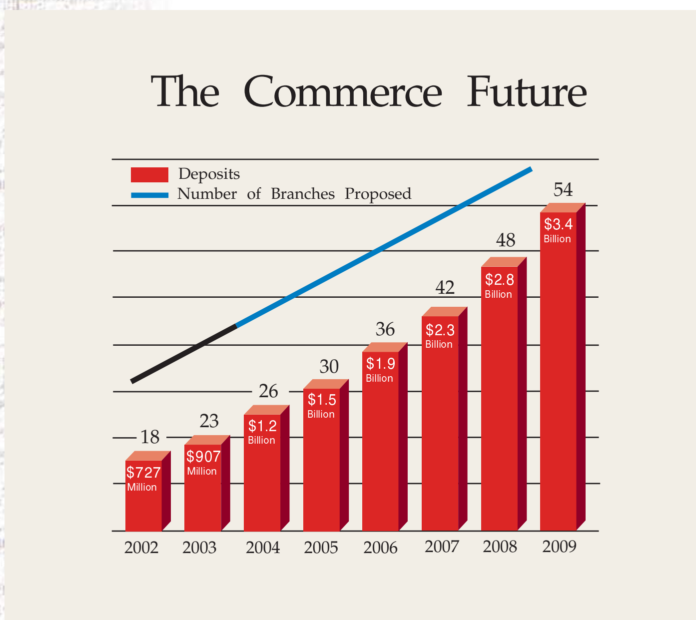
My thanks to the entire Commerce Team, who wholeheartedly embrace the Commerce culture and deliver the best possible banking experience every day. And my thanks to our Customers — our Commerce Fans — who are at the heart of the Commerce story.

Together, we will continue to build our brand. One relationship at a time. One Customer at a time. One brick at a time.

Thank you for your ongoing support.

Gary L. Nalbandian
Chairman of the Board, President and CEO

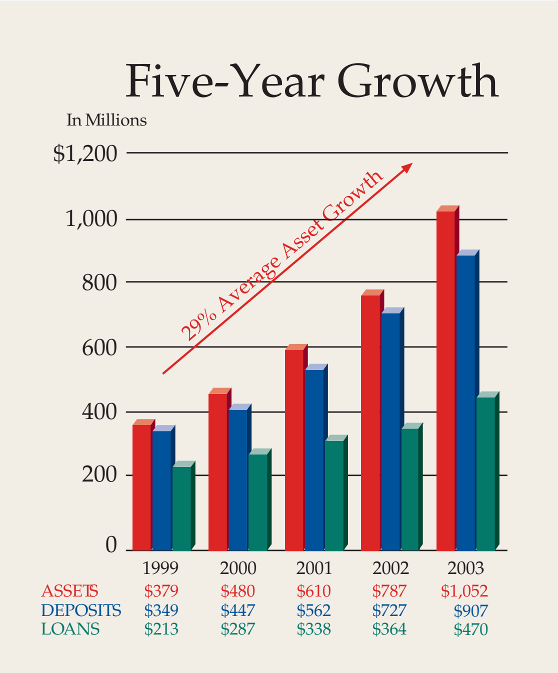
March 26, 2004

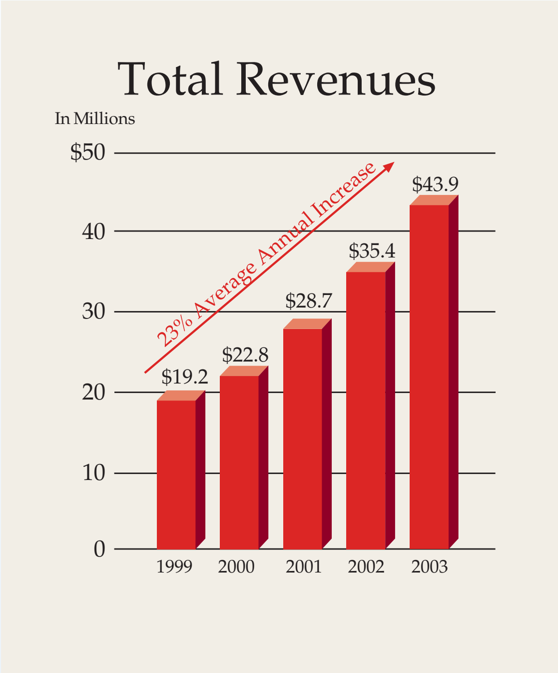


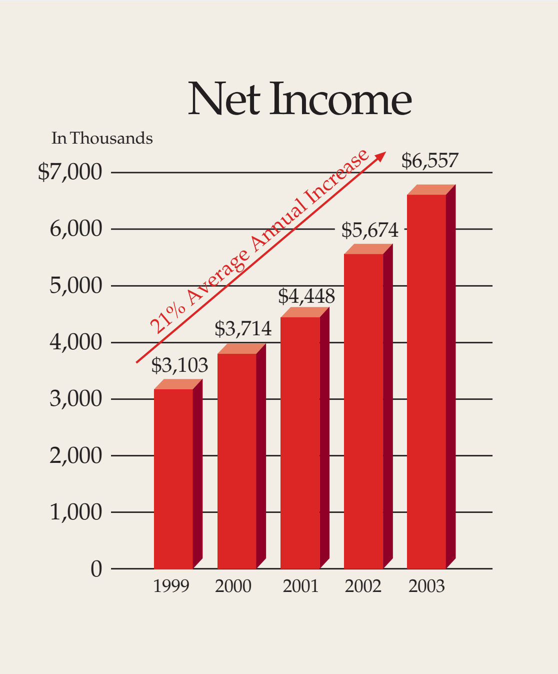
Annual Return	COBH	S&P 500
*One Year	**43%**	29%
Five Years	**18%**	-1%
Ten Years	**24%**	11%

*As of 12/31/03 – $48.57

A Growth Company







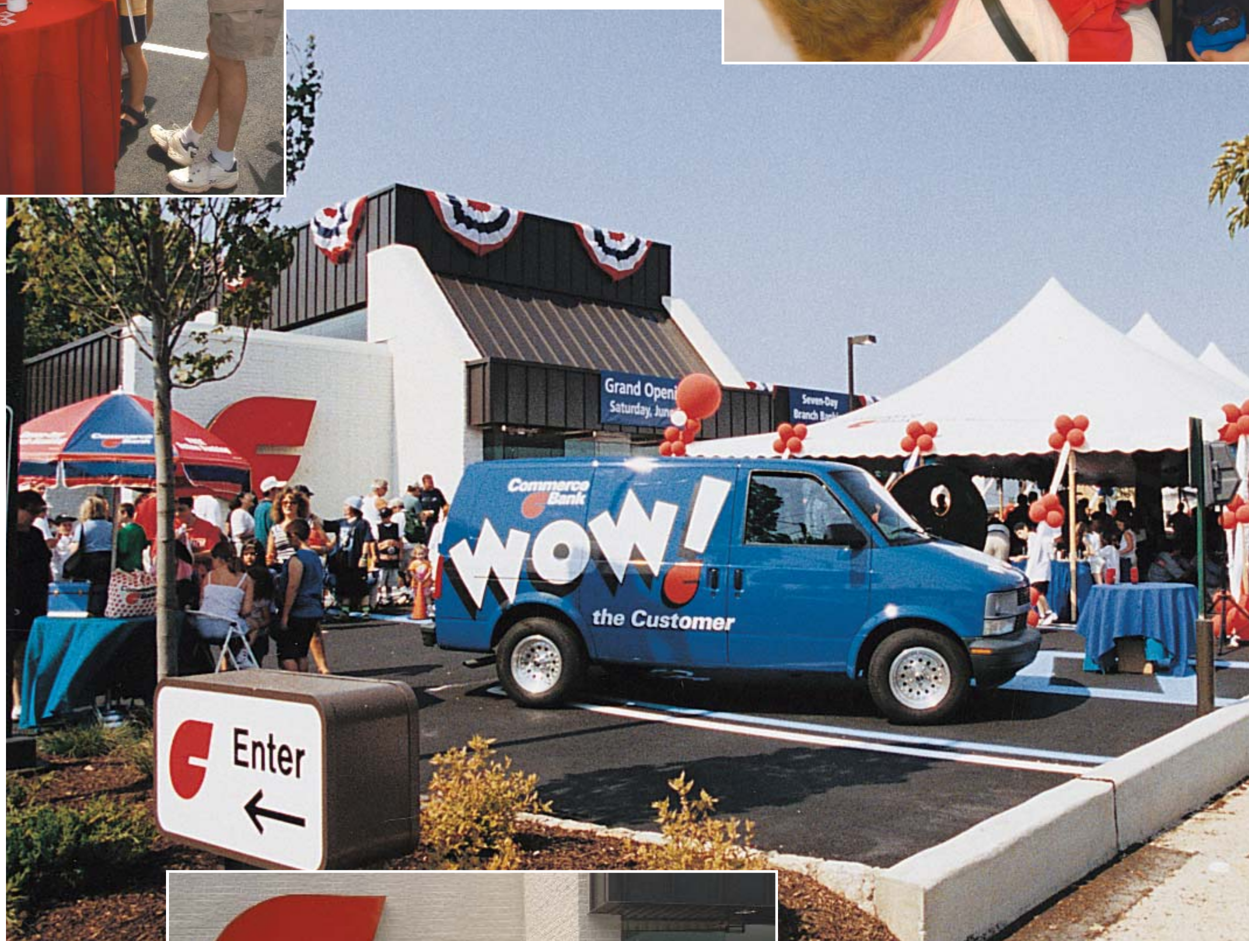
Pennsylvania Commerce Bancorp

Celebrating Our Brand...
Celebrating Our Growth

Commerce Bank opened a record five new stores in 2003, including its first two in Berks County. The Bank has doubled its number of locations in recent years, growing a network of 23 stores throughout Berks, Cumberland, Dauphin, Lebanon and York counties.

Commerce Bank is renowned for its spectacular grand opening parties. Free and open to the public, the celebrations feature free food and refreshments, exciting games and prizes, entertainment and activities for the kids and lively music. Commerce's approach to new store openings builds maximum public awareness and promotes swift deposit growth.

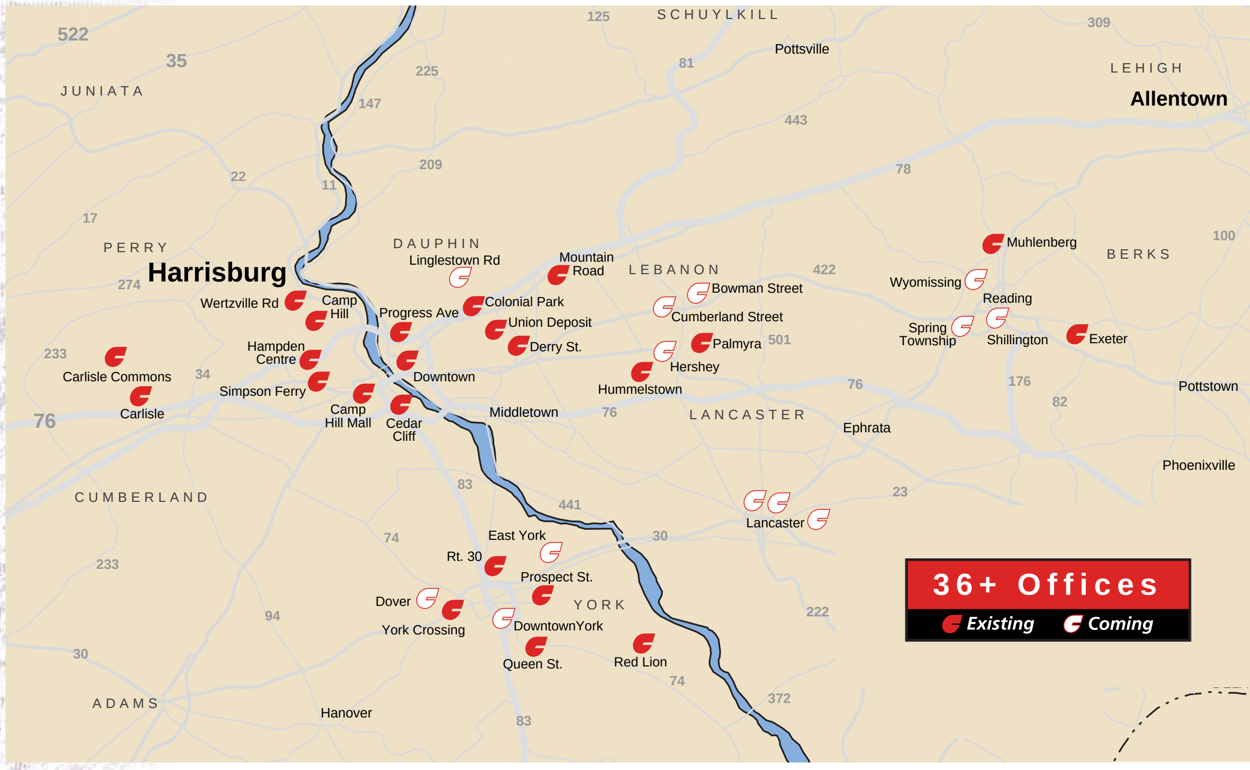

1-888-937-0004


Commerce Bank
WOW!
the Customer
Enter


Commerce Bank

Regions At-a-Glance

Commerce Bank's record growth in 2003 called for additions to the Bank's leadership team at the regional level. Services are now delivered through regional vice presidents who, in partnership with a retail market manager in selected markets, are responsible for all deposit and lending operations within their market.



Lisa Laudermilch
East Shore
Regional Vice President

Frank Fischer
West Shore
Regional Vice President

Kelly Neiderer
Carlisle
Regional Vice President & Retail Market Manager

Harry Zimmerman
York
Regional Vice President

Rory Ritrievi
Reading
Regional Vice President

Vicky LaCour
East Shore
Retail Market Manager

Leslie Meck
West Shore
Retail Market Manager

Cheryl Thoman
York
Retail Market Manager

Dorothy Krick
Reading
Retail Market Manager

Retail Banking

At Commerce Bank, our goal is to deliver a customer experience that's positively memorable.

We make a supreme effort to provide service so extraordinary that Customers are inclined to talk about the service they receive with neighbors, family and friends.

A core set of products and services helps empower the Commerce Team to provide the ultimate retail banking experience:

- Seven-day branch banking
- Totally free checking
- No-fee instant-issue ATM/Visa® Check Card
- America's Best Online Banking
- 24/7 Bank-by-Phone
- Free Penny Arcade coin counting machines

2003 Highlights

Commerce made numerous enhancements to retail banking in 2003.

With Quick Switch, opening an account is faster and easier than ever. A customized starter kit includes a Guide to "America's Most Convenient Bank®," which highlights everything Customers need to know about banking with us. And Customers can transfer existing pre-authorized transactions such as social security deposits with ease.

Customers can now use their Commerce ATM/Visa® Check Cards with no fees from us. Plus, new and replacement cards are issued instantly — in our stores, on the spot.

With upgrades to Commerce Online Banking, Customers enjoy free "pay anyone" bill pay and can easily download transactions to Quicken® or Microsoft® Money.

These and other enhancements to retail banking helped generate outstanding results:

Deposits

- Total deposits increased to $907 million, up 25% over 2002
- New account openings increased 71% over last year
- Average deposits per store increased $8.5 million in 2003
- Average Customer visits per store increased 13% over the past year

Consumer Loans

- Consumer loans outstanding increased to $71 million, up 105% over last year
- Residential mortgage originations were more than $140 million in 2003

Retail Banking (continued)

Seven-day Branch Banking

Commerce Bank is known for opening early and closing late every day of the week. In 2003, we grew even more convenient by extending our already renowned weekend hours. Commerce's seven-day schedule is now:

- Weekdays 7:30am-8pm
- Saturday 7:30am-6pm
- Sunday 11:00am-4pm

24/7 Convenience

Commerce Bank's web site at *commercepc.com* is a convenient complement to our branch network. With Commerce Online Banking, Customers can:

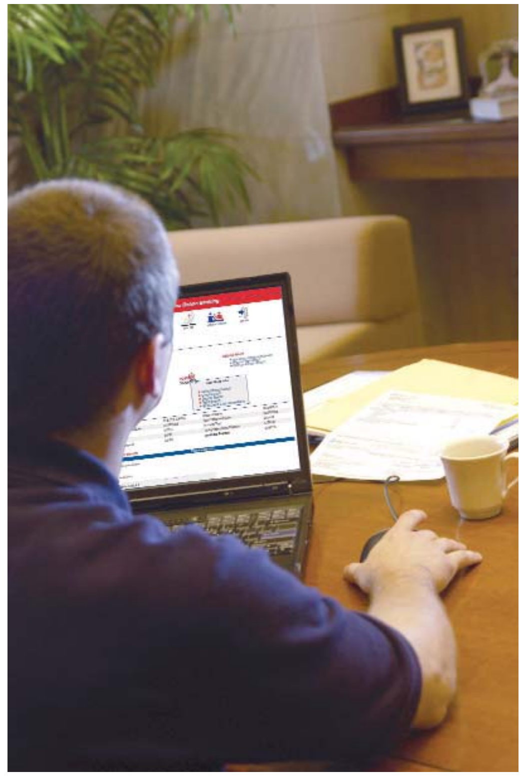
- Gain quick, real-time access to all their accounts
- Transfer funds between accounts
- Pay bills online with free "pay anyone" bill pay
- Download to Quicken® or Microsoft® Money
- Reorder checks
- Apply for a loan
- Apply for a no-fee Commerce ATM/Visa® Check Card online
- Check Commerce Visa® credit card balances and make payments online
- Visit CommerceWOW!Zone®, our free K-12 financial education site

Customers also benefit from our full-service, 24-hour telephone banking system at 1-800-937-2003. Knowledgeable Customer Service Representatives are available 365 days a year and provide the same exceptional service Customers enjoy at a Commerce store.

Interactive Penny Arcades

In 2003, Customers and non-Customers used Commerce's free Penny Arcade coin counting machines more than 99,000 times to count more than $8.4 million in change.

We're currently adding a twist to our popular coin counting service by installing new interactive Penny Arcade machines. The voice of Penny Arcade, a character from our CommerceWOW!Zone financial education web site, welcomes Customers when they approach the machine. There are two touch screens on the new machines, one for adults and a separate one for children at "kids-eye-level." Customers can even win prizes by correctly guessing the amount of coins counted.



Customers have a passion for Commerce Online Banking. In fact, Commerce Customers do their banking online more than four times the average Internet user, one of the highest rates in the nation.

The new interactive Penny Arcades already are featured in our newest stores and will be installed in all stores by the end of 2004.

Brand Awareness

Aggressive marketing plays a critical role in building brand recognition. A clear-cut multimedia advertising campaign unmistakably differentiates Commerce from the competition. Carefully targeted direct mail, coupon specials and extensive grand opening promotions also support Commerce's growth.

In 2003, we added an exciting element to our television advertising with the help of Julia Louis-Dreyfus, star of "Seinfeld." Julia (pictured at top of opposite page) appears in clever commercials showing Customers just how Commerce can provide them with a better banking experience. Julia's wit and humor makes her an ideal match for the "buck the trend" mentality that sets Commerce apart.

Assistant Store Manager Jacqueline Wiley provides "WOW!" service to a Commerce Fan. The Bank consistently adapts proven retail practices to enhance its Customers' banking experience, right down to Commerce's Teller uniform program, featuring custom navy blue vests embroidered with our recognizable red "C" logo.

Commercial Banking

*Commerce Commercial Loan Officer George Gunnett visits Joseph A. Rosi, Jr., owner of **Joseph A. Rosi Jewelers** in Harrisburg. Commerce provides Rosi Jewelers with an array of business banking services including deposit accounts and commercial loans.*

"America's Most Convenient Bank" also is "America's Best Business Bank"

Commerce offers a complete portfolio of products and services — for businesses, non-profits, government entities and other organizations — that can make banking easier, more rewarding and, ultimately, help our commercial Customers succeed.

Commercial Lending

Commerce knows that local bankers making local decisions are crucial to the success of the enterprises we serve. That's why Customers have direct access to locally based financial experts with authority to make prompt decisions.

Even in the face of a challenging economic climate, Commerce Bank's unique approach generated substantial commercial lending gains in 2003:

- 21% increase in commercial loans to $105 million
- The origination of $88 million in new commercial loans
- Outstanding credit quality, with non-performing assets of just 0.13% of total assets

Small Business Financing

Commerce Bank continues to be a Preferred Lender for the U.S. Small Business Administration in Pennsylvania. Preferred Lender status ensures that we can expedite the processing of SBA loan applications and meet the needs of most businesses that may not have access to conventional funding sources.

In 2003, Commerce provided more than $7 million in SBA financing.

Real Estate Lending

Commerce continues to extend the breadth of the financing services provided to developers of residential and commercial projects. We have a wealth of experience in the risks and opportunities associated with the real estate field — specifically those related to property acquisition, development, construction and sale, or the lease of a complete project.

In 2003, real estate loans increased 25% from $182 million to $227 million.

James Ridd
Senior Credit Officer

Debra Knox
Corporate Services

Thomas Bell
Government Banking

*Right: Commerce Regional Vice President Harry Zimmerman (center) and **H&H Castings, Inc.** Vice President and Owner Rod Haugh (left) and President and Owner Ken Haugh (right) at the company's York site. H&H Castings is leveraging a package of Commerce loan products to double the size of its facility.*

Commercial Banking (continued)

Left to right: ***Harrisburg School District*** *Business Manager William Gretton, Superintendent Dr. Gerald Kohn and Commerce Government Banking Officers Ken Miller and Audrey Hanna gather in a classroom at* ***Harrisburg High School****. With Commerce as its financial partner, the high school will undergo a major renovation beginning in 2004.*

Corporate Services

Commerce Bank's Corporate Services' experts assist organizations in managing cash flow in the most efficient way possible. Our cash management solutions help Customers save time and money while increasing their returns.

The centerpiece of Corporate Services is Commerce TreasuryDirect℠, a secure online banking system enabling Customers to obtain information on their accounts and initiate transactions including ACH and wire transfers.

Commerce also offers Commerce EscrowDirect℠, a deposit service that assists people who manage escrow accounts in tracking the activity of beneficiaries.

Commerce's menu of cash management services also includes:

- Next day availability of funds
- Automatic Investment Sweep
- Account Reconciliation
- Lockbox services
- ACH Direct Deposit Payroll
- ACH Direct Payments
- ACH Cash Concentration
- Merchant Payment Services

In 2003, total deposits driven through Corporate Services grew 55% to $66 million.

Government Banking

Commerce appreciates that government entities often have very specific requirements. Our government banking specialists are equipped to accommodate those needs for a variety of entities including:

- State government entities
- County governments and authorities
- Municipalities and municipal authorities
- Police and fire services
- School districts
- Community and state colleges and universities

Government Banking services include retail banking for employees, cash management and corporate trust services. We also provide a full range of insurance and public financing services through Commerce Insurance Services and Commerce Capital Markets.

In 2003, total public fund deposits grew 28% to $230 million. The Government Banking client base grew by 30%, and 100% of existing client relationships were retained.

Our WOW! Culture

While some organizations labor to be better than their competition, and others aim to be the best, Commerce Bank strives to be… LEGENDARY!

Leading us on the path to being a legendary organization is our "WOW! the Customer" service philosophy. Put simply, our foremost priority is to exceed Customer expectations — every time. We go all out to turn everyday Customers into Commerce Fans. Our goal is to make Customers literally say "WOW!" in response to the service they receive.

Guiding our "WOW! the Customer" philosophy day-to-day is our "SMART" Principles:

- Say "Yes" … 1 to Say Yes, 2 To Say NO!
- Make Each Customer Feel Special!
- Always Keep Customer Promises!
- Recover! To Err is Human; To Recover is Divine!
- Think Like Our Customers!

Employees learn the "SMART" Principles their very first day on the Commerce team. They know them. They put them into practice. They use them to "WOW!"

We keep our "WOW! the Customer" culture fresh and vibrant through a variety of employee recognition programs, the largest of which is our annual "WOW!" Awards event. The company-wide celebration salutes the "best of the best" among the Commerce team and helps to reinforce the power of "WOW!"

Events such as Commerce's Fall Festivals, free and open to the public, offer fun for Commerce Fans of all ages.

Commerce Bank's annual WOW! Awards event salutes the "best of the best" and celebrates the Power of WOW!

Training & Education

Commerce Trainer Cheryl Rhodes leads (foreground to background) Jodi Bezanilla, Stephanie Rydesky and Douglas Martin in classroom instruction.

The foundation for Commerce Bank's "WOW! the Customer" service and acclaimed culture is a world-class training and education program.

In 2003, training enrollment in all programs exceeded 2,500 through more than 240 class sessions. Enrollees included more than 270 Tellers and 140 Customer Service Representatives.

Patricia Noel
Director of Training

2003 Highlights

Compliance training, formerly presented in a classroom setting, is now delivered via a state-of-the-art Internet-based learning curriculum. The program has proven far more convenient and cost-effective than conventional training, as employees can complete courses and exams right from their desktops. Additionally, employees may reference training materials online anytime.

A Management Development series was introduced in 2003, beginning with a program entitled "Performance Management." The program advances managers' coaching and communication skills so they can maximize support, as their teams deliver "WOW!" service and pursue career development.

Commerce's Management Development Associates (MDA) program continued to produce new leaders within the organization. The program blends on-the-job training, classroom instruction and individualized mentoring. MDAs learn all facets of bank operations by working in stores — in every capacity — and assisting with special projects.

Customer Service Representative training was enhanced with the launch of a multi-tier training series. CSRs now receive training at regular intervals to broaden their depth of knowledge and expand their capabilities. The training covers virtually all aspects of consumer and commercial products and services.

Financial Education Outreach

Commerce Bank is leading efforts to improve financial literacy with CommerceWOW!Zone®, a free, one-of-a-kind program for K-12 students.

CommerceWOW!Zone® instructors provide lessons and activities for schools and community groups. In 2003, the program reached nearly 5,000 children through 111 classes in 70 schools. Lessons are customized for each grade level and meet National Council of Teachers of Mathematics standards.

Resources also are available on the CommerceWOW!Zone® web site at *commercepc.com*. Parents can find worksheets to help introduce the concept of money, banking and saving. Children can follow the adventures of Penny Arcade and her friends as they play and learn all about money. Teens can learn about the stock market by fantasy investing. Educators can download lessons and other financial education tools.

Community Partnerships

Commerce Bank is mindful that the workforce of tomorrow resides in the schoolrooms of today. That is why time and resources are invested in partnerships such as the Harrisburg School District School of Business and Industry (SBI) Prep Program. SBI introduces students to business through mentorships, job shadowing, internships and field trips. Commerce supports SBI by helping to enhance its curriculum and identify new learning opportunities within the educational and business communities.

Commerce also is one of five leading companies that — together with Capital Region Economic Development Corporation and Harrisburg Area Community College — participate in the Ready to Work program. Through Ready to Work, individuals learn skills to enhance their employment opportunities. As a program partner, Commerce provides customer service training, mock interviews and company tours.

Commerce's Management Development Associates learn all facets of bank operations by working at stores in every capacity.

Commercial Loan Officer Karen Ramm (center) and Wertzville Road Store Manager Rena Spicher (right) visit East Pennsboro High School (Enola, Cumberland County) business teacher Patricia Kacyon's classroom on "Get Smart About Credit Day."

Community Involvement

A strong sense of community is a significant piece of the Commerce culture — among ourselves as a company of professionals and within the cities and towns we serve.

Donations and Sponsorships

We invest in the neighborhoods where we live and work through initiatives such as the Commerce Bank Corporate Giving Program. Over the years, we've donated more than $1 million to local and regional charities and community service organizations. In 2003 alone, contributions exceeded $300,000.

Most of our support centers on civic and social improvement projects, health and human services, cultural and arts organizations and education.

In March of 2003, for example, Commerce affirmed a five-year commitment as title sponsor of the Central PA Jazz Festival. The three-day event is the annual centerpiece of Central Pennsylvania Friends of Jazz, a non-profit dedicated to fostering an appreciation of jazz as an original American art form.

In June, Commerce donated $8,000 to Crispus Attucks Association in York to support its Innovative Educational Program. The program offers technology training, distance education, career training and even employment to deserving public and charter school students.

Commerce also draws on the convenience of its store network for community causes.

Year round, Commerce teams up with Jump Street's Gift of Music program to collect band and orchestra instruments. Donated instruments are restored and distributed to disadvantaged students and at-risk youth to enrich their lives and education.

During the holiday season, Commerce participates in Toys for Tots, the U.S. Marine Corps Reserve's annual campaign to collect new, unwrapped toys and distribute them as holiday gifts to underprivileged children.

Giving Time and Talent

Commerce employees are tremendously giving in their own right. Through a companywide campaign, more than $53,000 was raised for United Way in 2003. The year also marked the first that Commerce served as a Pacesetter Organization, joining other leading companies to help United Way gain a head start before officially kicking off its campaign in the community.

Additionally, the Commerce Team lends time and talent to non-profit organizations, charitable groups and professional organizations. Employees bring their "WOW!" skills to WITF-TV to take pledges during the public television station's membership drive. They volunteer for United Cerebral Palsy Central PA's holiday gift wrap, which raises money from shoppers to support services that help children and adults with disabilities. They raise money for numerous health-related causes through events like The Leukemia & Lymphoma Society Light the Night Walk, American Cancer Society Making Strides Against Breast Cancer Walk and American Heart Association Heart Walk.

Commerce's support demonstrates that we are more than a top-notch organization that delivers the best banking experience found anywhere. Commerce genuinely cares about the communities we call home.

Commerce Bank's donation to Bell Socialization Services in York supports the organization's community-based mental health, mental retardation and emergency shelter programs.

Commerce employees bring their WOW! telephone skills to the studios of WITF-TV to take pledges during the public television station's membership drive.

Girls from Brownie Troop 429 visit the Commerce store at 903 East Main Street in Palmyra, Lebanon County, for a branch tour which included looking inside the vault and pouring change into the Penny Arcade.

Board of Directors

(Left to right): Peter J. Ressler, Douglas S. Gelder, Howell C. Mette, Alan R. Hassman, Gary L. Nalbandian, Michael A. Serluco, James R. Adair, Samir J. Srouji, MD

Gary L. Nalbandian
Chairman, President and CEO
Pennsylvania Commerce Bancorp, Inc.
Co-owner/President
Commercial Industrial Realty Co.

James R. Adair
President/CEO
Adair Construction Services, Inc.

Douglas S. Gelder
Owner/President
DSG Development

Alan R. Hassman
Owner/Operator
McDonald's Restaurants

Howell C. Mette
Senior Partner
Mette, Evans & Woodside

Peter J. Ressler (Secretary to the Board)
Attorney
Mette, Evans & Woodside

Michael A. Serluco
Owner
Consolidated Properties

Samir J. Srouji, MD
Owner
Plastic Surgery, P.C.

Pennsylvania Commerce Bancorp, Inc.
Selected Financial Data

(dollars in thousands, except per share data)	Year Ended December 31 **2003**	2002	2001	2000	1999
Balance Sheet Data:					
Total assets	**$1,051,989**	$ 786,598	$ 609,890	$ 480,086	$ 378,913
Loans held for sale	**9,164**	10,514	7,661	5,329	5,301
Loans receivable (net)	**469,937**	363,735	338,130	286,520	213,264
Securities available for sale	**275,400**	205,436	104,722	90,633	82,552
Securities held to maturity	**199,863**	97,625	103,349	33,812	29,039
Federal funds sold	**0**	44,500	4,300	22,800	0
Deposits	**906,527**	726,955	561,738	446,583	348,546
Short-term borrowings and long-term debt	**79,000**	0	0	0	8,300
Trust capital securities	**13,000**	13,000	13,000	5,000	0
Stockholders' equity	**49,724**	42,812	32,593	26,668	20,378
Income Statement Data:					
Net interest income	**$ 33,890**	$ 27,701	$ 22,054	$ 17,477	$ 14,676
Provision for loan losses	**1,695**	1,435	1,469	1,050	762
Noninterest income	**9,990**	7,707	6,607	5,362	4,558
Noninterest operating expenses	**32,510**	25,428	20,512	16,189	13,756
Income before income taxes	**9,675**	8,545	6,680	5,600	4,716
Net income	**6,557**	5,674	4,448	3,714	3,103
Per Common Share Data:					
Net income: *Basic*	**$ 2.88**	$ 2.58	$ 2.14	$ 1.81	$ 1.51
Diluted	**2.68**	2.37	1.94	1.69	1.42
Book value	**21.24**	18.79	15.21	12.66	9.68
Selected Performance Ratios:					
Return on average assets	**0.74 %**	0.82 %	0.82 %	0.88 %	0.89 %
Return on average stockholders' equity	**14.27**	14.86	14.85	16.59	15.18
Net interest margin	**4.20**	4.29	4.40	4.49	4.59
Selected Liquidity and Capital Ratios:					
Average loans to average deposits	**52.23 %**	56.91 %	63.25 %	65.12 %	60.24 %
Average stockholders' equity to average assets	**5.22**	5.49	5.54	5.29	5.86
Risk-based capital: *Tier 1*	**9.57**	11.16	10.22	9.90	9.91
Total	**10.49**	12.22	11.78	11.04	11.12
Leverage ratio	**6.19**	7.00	7.33	6.92	6.28
Asset Quality Ratios:					
Net charge-offs to average loans outstanding	**0.20 %**	0.23 %	0.21 %	0.06 %	0.08 %
Non-performing loans to total year-end loans	**0.25**	0.45	0.26	0.29	0.32
Non-performing assets to total year-end assets	**0.13**	0.23	0.15	0.18	0.18
Allowance for loan losses to total year-end loans	**1.26**	1.40	1.33	1.29	1.31
Allowance for loan losses to non-performing loans	**513**	311	519	448	404

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

Management's Discussion and Analysis of Financial Condition and Results of Operations analyzes the major elements of the Company's consolidated balance sheets and statements of income. This section should be read in conjunction with the Company's consolidated financial statements and accompanying notes.

Application of Critical Accounting Policies

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the industries in which it operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. The reporting of the Company's financial condition and results of operations is impacted by the application of accounting policies by management. Certain accounting policies are particularly sensitive and require significant judgments, estimates and assumptions to be made by management in matters that are inherently uncertain. The Company's accounting policies are detailed in Note 1 to the financial statements. The audit committee to the board of directors has approved these policies.

The Company's provision for loan losses and the level of the allowance for loan losses involve significant estimates by management in evaluating the adequacy of the allowance for loan losses. The allowance for loan losses is increased by a charge to the provision for loan losses. Management's evaluation is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. While management uses available information to make such evaluations, future adjustments to the allowance and the provision for loan losses may be necessary if economic conditions or loan credit quality differ substantially from the assumptions used in making the evaluation.

As permitted by SFAS No. 123, the Company accounts for stock-based compensation in accordance with Accounting Principles Board Opinion (APB) No. 25. Under APB No. 25, no compensation expense is recognized in the income statement related to any options granted under the Company's stock option plans. The pro forma impact to net income and earnings per share that would occur if compensation expense was recognized, based on the estimated fair value of the options on the date of grant, is disclosed in the notes to the consolidated financial statements. The Company intends to continue to account for stock-based compensation in this manner unless there is more specific guidance issued by the Financial Accounting Standards Board or unless a clear consensus develops in the financial services industry on the application of accounting methods.

2003 Overview

In 2003, the Company continued its strong financial performance by posting record levels of total assets, deposits and loans. Total assets grew by $265 million, or 34%, to $1.05 billion and total deposits increased $180 million, or 25%, to $907 million. Core deposit growth was exceptionally strong, increasing $171 million, or 25%, from $687 million to $858 million. The Company also experienced strong loan growth in 2003 as total loans outstanding increased by $106 million, or 29%, to $470 million.

Total revenues (net interest income plus noninterest income) increased by 24% to a record level of $43.9 million and net income was up 16% in 2003 to $6.6 million from $5.7 million for 2002. Diluted net income per common share increased 13% to $2.68 from $2.37 per share in 2002 (after adjusting for a 5% common stock dividend declared in January 2004).

In 2003, the Company opened five new branches in the Central Pennsylvania area, bringing the total number of full-service branches to 23. Two of the new offices opened in 2003 are located in Berks County, marking Commerce's initial entry into this market.

Results of Operations

Average Balances and Average Interest Rates

Table 1 on the following page sets forth balance sheet items on a daily average basis for the years ended December 31, 2003, 2002 and 2001 and presents the daily average interest rates earned on assets and the daily average interest rates paid on liabilities for such periods. During 2003, average interest-earning assets were $807.4 million, an increase of $162.3 million, or 25%, over 2002. This was the result of an increase in the average balance of investment securities of $119.5 million, an increase in the average balance of loans receivable of $53.9 million, offset by a decrease in the average balance of fed funds sold of $11.2 million. The growth in the average balance of interest earning assets was funded primarily by an increase in the average balance of deposits (including noninterest bearing demand deposits) of $160.8 million.

The yield on total interest-earning assets decreased by 87 basis points in 2003 from 6.51% to 5.64%. The decrease resulted primarily from decreased yields in the loan and investment portfolios due to the overall level and timing of changes in general market interest rates during 2003 as compared to 2002. As a result, the Company experienced lower yields on most interest-earning assets in 2003 from 2002 as well as a lower cost of funds in 2003 versus the prior year.

The aggregate cost of interest-bearing liabilities decreased 96 basis points from 2.65% in 2002 to 1.69% in 2003. The average rate paid on savings deposits decreased by 94 basis points, from 1.96% in 2002 to 1.02% in 2003 and the average rate paid on interest checking accounts decreased from 1.18% in 2002 to 0.70% in 2003. The average rate paid on money market accounts decreased from 1.32% in 2002 to 0.91% in 2003. For time deposits, the average rate paid was 3.46%, down 125 basis points from 2002 and public funds time deposits experienced a decrease of 69 basis points in 2003 on the average rate paid.

The majority of the Company's public funds are deposits of local school districts and municipalities.

The Company's aggregate cost of funding sources decreased 78 basis points in 2003 to 1.44% from 2.22% in 2002. This decrease resulted primarily from lower average rates paid on total interest bearing deposits as well as a $28.0 million increase in average noninterest-bearing demand deposits.

TABLE 1

	Year Ended December 31,								
(dollars in thousands)	**2003**			2002			2001		
Earning Assets	**Average Balance**	**Interest**	**Average Rate**	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Securities:									
Taxable	**$361,323**	**$17,108**	**4.74%**	$246,230	$14,514	5.89%	$165,013	$10,860	6.58%
Tax-exempt	**6,444**	**453**	**7.02**	1,995	107	5.36	1,743	94	5.38
Total securities	**367,767**	**17,561**	**4.78**	248,225	14,621	5.89	166,756	10,954	6.57
Federal funds sold	**20,653**	**220**	**1.07**	31,833	508	1.59	17,399	641	3.68
Loans receivable:									
Mortgage and construction	**263,581**	**18,290**	**6.94**	241,647	18,408	7.62	212,117	18,013	8.49
Commercial loans and lines of credit	**95,469**	**5,937**	**6.22**	83,971	5,670	6.75	69,815	5,810	8.32
Consumer	**54,840**	**3,318**	**6.05**	35,851	2,677	7.47	32,305	2,709	8.39
Tax-exempt	**5,093**	**216**	**4.25**	3,598	111	3.09	2,711	120	4.43
Total loans receivable	**418,983**	**27,761**	**6.63**	365,067	26,866	7.36	316,948	26,652	8.41
Total earning assets	**$807,403**	**$45,542**	**5.64%**	$645,125	$41,995	6.51%	$501,103	$38,247	7.63%
Sources of Funds									
Interest-bearing deposits:									
Regular savings	**$235,515**	**$ 2,392**	**1.02%**	$197,225	$ 3,857	1.96%	$141,350	$ 4,168	2.95%
Interest checking	**14,760**	**103**	**0.70**	10,590	125	1.18	7,955	165	2.07
Money market	**230,504**	**2,104**	**0.91**	145,851	1,923	1.32	100,394	2,261	2.25
Time deposits	**132,112**	**4,573**	**3.46**	118,899	5,595	4.71	126,389	7,133	5.64
Public funds time	**46,562**	**917**	**1.97**	54,165	1,440	2.66	33,642	1,693	5.03
Total interest-bearing deposits	**659,453**	**10,089**	**1.53**	526,730	12,940	2.46	409,730	15,420	3.76
Short-term borrowings	**16,964**	**207**	**1.22**	12	0	1.46	330	13	3.94
Long-term debt	**13,000**	**1,356**	**10.43**	13,000	1,354	10.41	7,082	760	10.73
Total interest-bearing liabilities	**689,417**	**11,652**	**1.69**	539,742	14,294	2.65	417,142	16,193	3.88
Noninterest-bearing funds (net)	**117,986**			105,383			83,961		
Total sources to fund earning assets	**$807,403**	**11,652**	**1.44**	$645,125	14,294	2.22	$501,103	16,193	3.23
Net interest income and margin		**$33,890**	**4.20%**		$27,701	4.29%		$22,054	4.40%
Other Balances									
Cash & due from banks	**$ 28,390**			$ 23,022			$ 18,904		
Other assets	**45,369**			27,190			20,951		
Total assets	**881,162**			695,337			540,958		
Noninterest-bearing demand deposits	**142,805**			114,758			91,352		
Other liabilities	**2,983**			2,657			2,508		
Stockholders' equity	**45,957**			38,180			29,956		

Notes: Nonaccrual loans have been included in the average loan balances. Securities include securities available for sale and securities held to maturity. Securities available for sale are carried at amortized cost for purposes of calculating the average rate received on taxable securities above. Yields on tax-exempt securities and loans are not computed on a taxable equivalent basis.

Net Interest Income and Net Interest Margin

Net interest income is the difference between interest income earned on assets and interest expense incurred on liabilities used to fund those assets. Interest earning assets primarily include loans and securities. Liabilities used to fund such assets include deposits and borrowed funds. Changes in net interest income and margin result from the interaction between the volume and composition of earning assets, related yields and associated funding costs.

Net interest income for 2003 increased $6.2 million, or 22%, over 2002 to $33.9 million. Interest income on earning assets totaled $45.5 million, an increase of $3.5 million, or 8%, over 2002. The majority of this increase was related to volume increases in the securities and loans receivable portfolios partially offset by lower interest rates on interest earning assets. Interest expense for 2003 decreased $2.6 million, or 18%, from $14.3 million in 2002 to $11.7 million in 2003. This decrease was primarily related to the reduction in interest rates paid on the deposit products partially offset by the increases in the Company's average level of deposits and other borrowed money.

Changes in net interest income are frequently measured by two statistics: net interest rate spread and net interest margin. Net interest rate spread is the difference between the average rate earned on earning assets and the average rate incurred on interest-bearing liabilities. Net interest margin represents the difference between interest income, including net loan fees earned, and interest expense, reflected as a percentage of average earning assets. The Company's net interest rate spread increased to 3.95% in 2003 from 3.86% in 2002 and the net interest margin decreased 9 basis points from 4.29% to 4.20%.

Table 2 demonstrates the relative impact on net interest income of changes in the volume of earning assets and interest-bearing liabilities and changes in rates earned and paid by the Company on such assets and liabilities. For purposes of this table, nonaccrual loans have been included in the average loan balances.

TABLE 2

	2003 v. 2002 Increase (Decrease) Due to Changes in (1)			2002 v. 2001 Increase (Decrease) Due to Changes in (1)		
(in thousands)	**Volume**	**Rate**	**Total**	Volume	Rate	Total
Interest on securities:						
Taxable	**$5,426**	**$(2,832)**	**$2,594**	$4,793	$(1,139)	$3,654
Tax-exempt	**313**	**33**	**346**	13	0	13
Federal funds sold	**(122)**	**(166)**	**(288)**	231	(364)	(133)
Interest on loans receivable:						
Mortgage and construction	**1,525**	**(1,643)**	**(118)**	2,240	(1,845)	395
Commercial	**712**	**(445)**	**267**	956	(1,096)	(140)
Consumer	**1,150**	**(509)**	**641**	265	(297)	(32)
Tax-exempt	**63**	**42**	**105**	27	(36)	(9)
Total interest income	**9,067**	**(5,520)**	**3,547**	8,525	(4,777)	3,748
Interest expense:						
Regular savings	**389**	**(1,854)**	**(1,465)**	1,088	(1,399)	(311)
Interest checking	**29**	**(51)**	**(22)**	31	(71)	(40)
Money market	**779**	**(598)**	**181**	596	(934)	(338)
Time deposits	**464**	**(1,486)**	**(1,022)**	(363)	(1,175)	(1,538)
Public funds	**(149)**	**(374)**	**(523)**	544	(797)	(253)
Short-term borrowings	**207**	**0**	**207**	(5)	(8)	(13)
Long-term debt	**0**	**2**	**2**	617	(23)	594
Total interest expense	**1,719**	**(4,361)**	**(2,642)**	2,508	(4,407)	(1,899)
Net increase (decrease)	**$7,348**	**$(1,159)**	**$6,189**	$6,017	$ (370)	$5,647

(1) *Changes due to both volume and rate have been allocated to volume changes.*

Noninterest Income

Noninterest income for 2003 increased by $2.3 million, or 30%, over 2002 to $10.0 million. The increase was primarily due to increased "core" other operating income attributable to service charges and fees associated with servicing a higher volume of deposit and loan accounts. Included in total noninterest income were gains of $765,000 in 2003 and $493,000 in 2002 on the sale of residential and student loans. Also included in noninterest income were securities gains of $880,000 for 2003 and $0 for 2002.

Noninterest Expenses

Noninterest expenses totaled $32.5 million for 2003, an increase of $7.1 million, or 28%, over 2002. Staffing levels, occupancy, furniture and equipment, and related expenses increased as a result of opening five full service branches in 2003. A comparison of noninterest expense for certain categories for 2003 and 2002 is presented below.

Salary expenses and employee benefits, which represent the largest component of noninterest expenses, increased by $4.2 million, or 34%, in 2003 over 2002. This increase was partially due to an increase in the level of full-time equivalent employees from 424 at December 31, 2002 to 503 at year-end 2003. The increased level of expenses includes the impact of salary and benefit costs associated with the additional staff for the new branch offices opened in June, July, and September and two in December 2003, respectively.

Occupancy expenses totaled $3.4 million in 2003, an increase of $1.0 million, or 42%, over 2002 while furniture and equipment expenses increased by $321,000, or 21%, to $1.8 million. The full year impact of the three branch offices opened in 2002 along with five additional branches opened in 2003 contributed to the increases in occupancy and furniture and equipment expenses in 2003 over 2002.

Advertising and marketing expenses were $2.4 million for 2003, an increase of $244,000, or 11%, over 2002. The increase was primarily the result of new branch opening expenses associated with the five new branches along with increased advertising efforts in each of the Company's markets. Two out of the five branches opened in 2003, were opened in Berks County, a new market for the Company. The Company's markets include Berks, Lebanon, Dauphin, Cumberland, and York Counties of South Central Pennsylvania. The Company will continue to have multiple markets in which to advertise its products.

Data processing expenses increased by $258,000, or 14%, in 2003 over 2002. The primary increase was due to costs associated with processing additional transactions as a result of growth in the number of accounts serviced.

Postage and supplies expenses of $986,000 were $124,000, or 14%, higher than the prior year. The increase in postage and supplies expense was attributed to the growth in the number of account statements mailed to customers.

Other noninterest expenses totaled $5.0 million for 2003, compared to $4.1 million for 2002. This includes increased loan expenses of $367,000, increased checkbook printing expense of $92,000, increased business development expenses of $191,000 and increased shares tax expense of $79,000.

The Company's current strategic plan calls for the construction of two or three additional new branch offices in 2004. The costs associated with these planned offices will continue to result in higher levels of staff, facilities, and related expenses in 2004 and in future periods.

One key measure used to monitor progress in controlling overhead expenses is the ratio of net noninterest expenses to average assets. For purposes of this calculation, net noninterest expenses equal noninterest expenses (excluding other real estate expenses) less noninterest income (exclusive of gains on sales of investment securities). This ratio equaled 2.66% for 2003, compared to 2.55% for 2002. Another productivity measure is the operating efficiency ratio. This ratio expresses the relationship of noninterest expenses (excluding other real estate expenses) to net interest income plus noninterest income (excluding gains on sales of investment securities). For 2003, the operating efficiency ratio was 75.7% compared to 71.9% for 2002. The Company's operating efficiency ratio remains above its peer group primarily due to its aggressive branch expansion activities.

Provision for Federal Income Taxes

The provision for federal income taxes was $3.1 million for 2003, compared to $2.9 million for 2002. The effective tax rate, which is the ratio of income tax expense to income before taxes, was 32.2% in 2003 and 33.6% in 2002. Reference should be made to Note 11 of the *Notes to Consolidated Financial Statements* for an additional analysis of the provision for income taxes for 2003 and 2002.

In accordance with Statement of Financial Accounting Standard No. 109 (SFAS No. 109), "Accounting for Income Taxes", income taxes are accounted for under the liability method. Under the liability method, deferred tax assets and liabilities are recognized for future tax consequences attributable to temporary differences between the financial statement and tax bases of existing assets and liabilities.

At December 31, 2003, deferred tax assets amounted to $2.1 million and deferred tax liabilities amounted to $1.5 million. Deferred tax assets are realizable primarily through carryback of existing deductible temporary differences to recover taxes paid in prior years, and through future reversal of existing taxable temporary differences. Management currently anticipates future earnings will be adequate to utilize the net deferred tax assets.

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

Net Income and Net Income Per Share

Net income for 2003 rose to a record $6.6 million, an increase of $883,000, or 16%, over the $5.7 million recorded in 2002. This increase was due to an increase in net interest income of $6.2 million, an increase in noninterest income of $2.3 million, partially offset by an increase in the provision for loan losses of $260,000, an increase in noninterest expenses of $7.1 million and an increase of $247,000 in the provision for income taxes.

Basic earnings per common share, after adjusting for a 5% common stock dividend declared in January 2004, increased by 12% to $2.88 per share, compared to $2.58 in 2002. Diluted earnings per common share were $2.68 for 2003 and $2.37 for 2002 after adjusting for the 5% common stock dividend declared in January 2004. Reference should be made to Note 13 in the *Notes to Consolidated Financial Statements* for an analysis of earnings per share.

Return on Average Assets and Average Equity

Return on average assets (ROA) measures the Company's net income in relation to its total average assets. The Company's ROA was 0.74% for 2003 and 0.82% for 2002. This decrease is the result of 34% growth in total assets combined with a 16% increase in net income. Contributing to these results was the addition of 5 new branch offices in 2003 and their related costs.

For purposes of calculating ROA, average assets have been adjusted to exclude the effect of net unrealized gains (losses) on securities available for sale.

The Company's ROE for 2003 was 14.27%, compared to 14.86% for 2002. Return on average equity (ROE) indicates how effectively the Company can generate net income on the capital invested by its stockholders. ROE is calculated by dividing net income by average stockholders' equity. For purposes of calculating ROE, average stockholders' equity includes the effect of unrealized gains (losses), net of income taxes, on securities available for sale. Reference should be made to Note 3 in the *Notes to Consolidated Financial Statements* for an analysis of securities available for sale.

Results of Operations

2002 versus 2001

Net income for 2002 rose to $5.7 million, an increase of $1.3 million, or 28%, over the $4.4 million recorded in 2001.

Diluted earnings per common share increased by 22% to $2.37 for 2002 over $1.94 for 2001 after adjusting for the 5% common stock dividends declared in January 2003 and 2004.

Net interest income for 2002 increased $5.6 million, or 26%, over 2001 to $27.7 million. Interest income on earning assets totaled $42.0 million, an increase of $3.7 million, or 10%, over 2001. Interest expense for 2002 decreased by $1.9 million, or 12%, from $16.2 million to $14.3 million.

The Company's net interest rate spread increased to 3.86% in 2002 from 3.75% in 2001 and the net interest margin decreased 11 basis points from 4.40% to 4.29%.

Noninterest income for 2002 increased by $1.1 million, or 17%, over 2001 to $7.7 million. Included in total noninterest income were gains of $493,000 in 2002 and $354,000 in 2001 on the sale of residential and student loans.

Noninterest expenses totaled $25.4 million for 2002, an increase of $4.9 million, or 24%, over 2001. Staffing levels, occupancy, furniture and equipment, and related expenses increased as a result of opening three full service branches in 2002.

Salary expenses and employee benefits increased by $3.0 million, or 32%, in 2002 over 2001. This increase was consistent with an increase in the level of full-time equivalent employees from 334 at December 31, 2001 to 424 at year-end 2002.

Occupancy expenses totaled $2.4 million in 2002, an increase of $270,000, or 13%, over 2001 while furniture and equipment expenses increased by $121,000, or 9%, to $1.5 million.

Advertising and marketing expenses were $2.2 million for 2002, an increase of $459,000, or 27%, over 2001. Data processing expenses increased by $577,000, or 44%, in 2002 over 2001. Postage and supplies expenses of $862,000 were $16,000, or 2%, higher than the prior year.

Other noninterest expenses totaled $4.1 million for 2002, compared to $3.6 million for 2001.

Financial Condition

Securities

Securities are purchased and sold as part of the overall asset and liability management function at Pennsylvania Commerce Bancorp, Inc. The classification of all securities is determined at the time of purchase. Securities expected to be held for an indefinite period of time are classified as securities available for sale and are carried at fair value. Decisions by management to purchase or sell these securities are based on an assessment of financial and economic conditions, including changes in prepayment risks and interest rates, liquidity needs, capital adequacy, collateral requirements for pledging, alternative asset and liability management strategies, tax considerations, and regulatory requirements.

Securities are classified as held to maturity if, at the time of purchase, management has both the intent and ability to hold the securities until maturity. Securities held to maturity are carried at amortized cost. Sales of securities in this portfolio should only occur in unusual and rare situations where significant unforeseeable changes in circumstances may cause a change in intent. Examples of such instances would include deterioration in the issuer's creditworthiness that is evidently supportable and significant or a change in tax law that eliminates or reduces the tax-exempt status of interest (but not the revision of marginal tax rates applicable to interest income). Held to maturity securities cannot be sold based upon any of the decisions used to sell securities available for sale as listed above. Reference should be made to Note 3 in the *Notes to Consolidated Financial Statements* for further analysis of the Company's securities portfolio.

The Company's investment securities portfolio consists primarily of U.S. Government agency and mortgage-backed obligations. These securities have very little, if any, credit risk because they are either backed by the full faith and credit of the U.S. Government or their principal and interest payments are guaranteed by an agency of the U.S. Government or are AAA rated. These investment securities carry fixed rate coupons that do not change over the life of the securities. Since most securities are purchased at premiums or discounts, their yield and average life will change depending on any change in the estimated rate of prepayments. The Company amortizes premiums and accretes discounts over the estimated average life of the securities. Changes in the estimated average life of the securities portfolio will lengthen or shorten the period in which the premium or discount must be amortized or accreted, thus affecting the Company's securities yields.

At December 31, 2003, the weighted average life and duration of the Company's securities portfolio was approximately 6.6 and 4.8 years, respectively, as compared to 2.5 years and 2.0 years, respectively, at December 31, 2002. The weighted average life of the portfolio is calculated by estimating the average rate of repayment of the underlying collateral of the security. Mortgage-backed obligations historically experience repayment rates in excess of the scheduled repayments, causing a shorter weighted average life of the security. The Company's securities portfolio contained no "high-risk" securities or derivatives as of December 31, 2003 or 2002.

Securities available for sale increased by $71.4 million in 2003 (excluding the effect of unrealized gains or losses) primarily as a result of purchases of $273.4 million, offset by principal repayments and maturities of $191.7 million and the sale of $8.3 million in securities. The securities available for sale portfolio is comprised of U.S. Government Agency securities, mortgage-backed securities, AAA Whole Loan CMO securities, and corporate debt securities. At December 31, 2003, the unrealized gains on securities available for sale included in stockholders' equity totaled $549,000, net of tax, compared to unrealized gains of $1.5 million, net of tax, at December 31, 2002.

During 2003, securities held to maturity increased by $102.3 million primarily as a result of purchases of $148.2 million offset by principal repayments of $45.9 million. The securities held in this portfolio include U.S. Government Agency securities, tax-exempt municipal bonds, AAA Whole Loan CMO securities, corporate debt securities and mortgage-backed securities. As of December 31, 2003, the Company had committed securities with a carrying value of $8.6 million and a fair market value of $9.2 million for sale. These securities are included as other assets on the balance sheet at December 31, 2003.

TABLE 3

December 31, 2003 *(dollars in thousands)*	**Due Under 1 Year** Amount	Yield	**Due 1–5 Years** Amount	Yield	**Due 5–10 Years** Amount	Yield	**Due Over 10 Years** Amount	Yield	**Total** Amount	Yield
Available for Sale										
U.S. Government										
Agency obligations					$ 5,000	4.05%	$ 19,000	5.79%	$ 24,000	5.43%
Mortgage-backed obligations			$ 734	4.80%	20,037	3.57	227,784	4.51	248,555	4.44
Corporate debt securities							2,013	7.80	2,013	7.80
Total available for sale	$ 0	—	$ 734	4.80%	$25,037	3.67%	$248,797	4.63%	$274,568	4.55%
Held to Maturity										
U.S. Government										
Agency obligations	$1,100	6.30%			$14,988	4.58%	$ 23,922	5.87%	$ 40,010	5.40%
Municipal obligations							6,845	7.05	6,845	7.05
Mortgage-backed obligations			$2,160	5.32%	243	4.75	133,522	5.15	135,925	5.15
Corporate debt securities			4,534	6.52	3,968	6.57	8,581	7.53	17,083	7.04
Total held to maturity	$1,100	6.30%	$6,694	6.13%	$19,199	4.99%	$172,870	5.44%	$199,863	5.43%

Note: Securities available for sale are carried at amortized cost in the table above for purposes of calculating the weighted average yield received on such securities.

The contractual maturity distribution and weighted average yield of the Company's available for sale and held to maturity portfolios at December 31, 2003 are summarized in Table 3. Weighted average yield is calculated by dividing income within each maturity range by the outstanding amount of the related investment and has not been tax affected on tax-exempt obligations.

Loan Portfolio

The following table summarizes the composition of the loan portfolio of the Company by type as of December 31, for each of the years 1999 through 2003.

The Company manages risk associated with its loan portfolio through diversification, sound underwriting policies and procedures that are reviewed and updated on at least an annual basis, and ongoing loan monitoring efforts. The commercial real estate portfolio includes owner-occupied (owner occupies greater than 50% of the property), other commercial real estate and construction loans. Owner-occupied and other commercial real estate loans generally have five-year call provisions and personal guarantees of the principals involved. Construction loans are primarily used for single-family residential properties. Financing is provided against firm agreements of sale, with speculative construction normally limited to one or two samples per project.

The commercial loan portfolio is comprised primarily of loans to small and mid-sized businesses primarily in the South Central Pennsylvania market area. Business assets, personal guarantees, and/or personal assets of the borrower generally secure these loans. The consumer loan portfolio is comprised primarily of loans secured by first and second mortgage liens on residential real estate. The Company's loan portfolio is generally non-homogeneous in that the loans have different interest rates, repayment options, maturities, collateral requirements, etc.

During 2003, total gross loans increased by $105.7 million from $379.4 million at December 31, 2002, to $485.1 million at December 31, 2003, including $9.2 million of loans held for sale on December 31, 2003 and $10.5 million of loans held for sale on December 31, 2002. The loans held for sale represent student loans and certain residential loans the Company's management intends to sell and reinvest in higher yielding loans and securities. The increase in loans receivable in 2003 was primarily in the commercial real estate and consumer loan portfolios. Total consumer loans increased by $36.4 million in 2003 to $71.0 million, an increase of 105%. The Company's 2003 Strategic Plan included a large effort to increase the size of the consumer loan portfolio across all markets of its branch footprint. Consumer loans represented 15% and 9% of total loans outstanding as of December 31, 2003 and 2002, respectively. Total loans outstanding represented 53% of total deposits and 45% of total assets at December 31, 2003, excluding the loans held for sale, compared to 51% and 47%, respectively, at December 31, 2002.

TABLE 4

	December 31,				
(in thousands)	**2003**	2002	2001	2000	1999
Commercial mortgage	**$194,609**	$144,959	$142,969	$127,931	$101,550
Construction and land development	**26,895**	31,034	32,863	30,776	18,458
Residential real estate mortgage loans	**72,713**	66,190	48,415	41,314	34,681
Tax-exempt loans	**5,720**	5,629	2,676	2,786	342
Commercial, industrial and other business loans	**58,894**	49,226	42,399	31,490	21,228
Consumer loans	**71,007**	34,598	36,551	30,691	22,764
Lines of credit	**46,106**	37,245	36,801	25,264	17,082
Total loans	**$475,944**	$368,881	$342,674	$290,252	$216,105

The maturity ranges of the loan portfolio and the amounts of loans with predetermined interest rates and floating interest rates in each maturity range, as of December 31, 2003, are presented in the following table.

TABLE 5

	December 31, 2003			
(in thousands)	**Due Under One Year**	**Due 1–5 Years**	**Due Over Five Years**	**Total**
Real estate:				
Commercial mortgage	**$ 16,934**	**$ 86,228**	**$ 91,447**	**$194,609**
Construction and land development	**20,309**	**4,630**	**1,956**	**26,895**
Residential mortgage	**3,407**	**9,780**	**59,526**	**72,713**
Tax-exempt	**554**	**1,906**	**3,260**	**5,720**
	41,204	**102,544**	**156,189**	**299,937**
Commercial	**26,847**	**25,344**	**6,703**	**58,894**
Consumer	**14,023**	**19,322**	**37,662**	**71,007**
Lines of credit	**46,106**	**0**	**0**	**46,106**
Total loans	**$128,180**	**$147,210**	**$200,554**	**$475,944**
Interest rates:				
Predetermined	**$ 39,775**	**$138,608**	**$161,054**	**$339,437**
Floating	**88,405**	**8,602**	**39,500**	**136,507**
Total loans	**$128,180**	**$147,210**	**$200,554**	**$475,944**

Concentrations of Credit Risk

The largest portion of loans, 41%, on the Company's balance sheet is for commercial mortgage related loans. The Company's commercial real estate loan portfolio is principally to borrowers throughout Cumberland, Dauphin, Lebanon, York and Berks counties of Pennsylvania where it has full-service branch locations. Commercial real estate, construction, and land development loans aggregated $221.5 million at December 31, 2003, compared to $176.0 million at December 31, 2002. Commercial real estate loans are collateralized by the related project (principally office building, multi-family residential, land development, and other properties) and the Company generally requires loan-to-value ratios of no greater than 80%. Collateral requirements on such loans are determined on a case-by-case basis based on managements' credit evaluations of the respective borrowers.

Non-Performing Loans and Assets

Total non-performing assets (non-performing loans and foreclosed real estate) at December 31, 2003, were $1.4 million, or 0.13%, of total assets as compared to $1.8 million, or 0.23%, of total assets at December 31, 2002. Total non-performing loans (non-accrual loans and restructured loans) at December 31, 2003 were $1.2 million compared to $1.7 million a year ago. Total delinquent loans (those loans 30 days or more delinquent) as a percentage of total loans were 0.38% at December 31, 2003, compared to 0.68% at December 31, 2002. The Company generally places a loan on nonaccrual status and ceases accruing interest when loan payment performance is deemed unsatisfactory and the loan is past due 90 days or more, unless the loan is both well-secured and in the process of collection. At December 31, 2003, loans past due 90 days and still accruing interest amounted to $385,000 compared to $55,000 at December 31, 2002.

Foreclosed real estate totaled $236,000 as of December 31, 2003 as compared to $118,000 as of December 31, 2002. These properties have been written down to the lower of cost or fair value less disposition costs. The Company obtains updated appraisals on non-performing loans secured by real estate. In those instances where appraisals reflect reduced collateral values, an evaluation of the borrower's overall financial condition is made to determine the need for possible write-downs or appropriate additions to the allowance for loan losses.

The following table summarizes information regarding non-performing loans and non-performing assets as of December 31, 1999 through 2003.

TABLE 6

	December 31,				
(dollars in thousands)	**2003**	2002	2001	2000	1999
Nonaccrual loans:					
Commercial	**$ 143**	$ 958	$ 127	$ 300	$ 119
Consumer	**68**	42	116	162	244
Real estate: Construction	**159**	0	0	0	0
Mortgage	**417**	599	633	371	321
Total nonaccrual loans	**787**	1,599	876	833	684
Loans past due 90 days or more and still accruing	**385**	55	0	0	20
Restructured loans	**0**	0	0	0	0
Total non-performing loans	**1,172**	1,654	876	833	704
Other real estate	**236**	118	12	42	12
Total non-performing assets	**$1,408**	$1,772	$ 888	$ 875	$ 716
Non-performing loans to total loans	**0.25%**	0.45%	0.26%	0.29%	0.32%
Non-performing assets to total assets	**0.13%**	0.23%	0.15%	0.18%	0.18%
Interest income received on nonaccrual loans	**$37**	$ 79	$ 33	$ 52	$ 38
Interest income that would have been recorded under the original terms of the loans	**$45**	$ 193	$ 89	$ 96	$ 66

Allowance for Loan Losses

The allowance for loan losses is a reserve established through charges to expense in the form of a provision for loan losses and reduced by loan charge-offs net of recoveries. Charge-offs occur when loans are deemed to be uncollectible. Management has established an allowance for loan losses that they believe is adequate for estimated inherent losses in the current loan portfolio. In conjunction with an internal loan review function that operates independently of the lending function, management monitors the loan portfolio to identify risks on a timely basis so that an appropriate allowance can be maintained. Based on an evaluation of the loan portfolio, management presents a quarterly review of the allowance for loan losses to the Board of Directors, indicating any changes in the allowance since the last review and any recommendations as to adjustments in the allowance. In making the evaluation, management considers the results of recent regulatory examinations, which typically include a review of the allowance for loan losses as an important part of the examination process.

In establishing the allowance, management evaluates individual large classified loans and nonaccrual loans, and determines an aggregate reserve for those loans based on that review. An allowance for the remainder of the loan portfolio is also determined based on historical loss experience within the components of the portfolio. These allocations may be modified if current conditions indicate that loan losses may differ from historical experience, based on factors and changes in portfolio mix and volume.

In addition, an unallocated portion of the allowance is established for losses inherent in the loan portfolio, which have not been identified by the more quantitative processes described above. This determination inherently involves a higher degree of subjectivity, and considers risk factors that may not have yet manifested themselves in the Company's historical loss experience. Those factors include changes in levels and trends of charge-offs, delinquencies and nonaccrual loans, trends in volume and term loans, changes in underwriting standards and practices, portfolio mix, tenure of the loan officers and management, changes in credit concentrations, and national and local economic trends and conditions.

While the allowance for loan losses is maintained at a level believed to be adequate by management for estimated losses in the loan portfolio, determination of the allowance is inherently subjective, as it requires estimates, all of which may be susceptible to significant change. Changes in these estimates may impact the provisions charged to expense in future periods.

The Company recorded provisions of $1.7 million to the allowance for loan losses for 2003 compared to $1.4 million for 2002. During 2003, net charge-offs amounted to $834,000, or 0.20%, of average loans outstanding for the year, compared to $833,000, or 0.23%, of average loans outstanding for 2002. The allowance for loan losses decreased as a percentage of loans receivable from 1.40% of total loans outstanding at December 31, 2002, to 1.26% of total loans outstanding at December 31, 2003 and provided coverage of 513% of non-performing loans. Based upon a consistent application of the Company's loan loss reserve methodology, the allowance level increased by $861,000 to $6.0 million or 1.26% of total loans at December 31, 2003, but decreased as a percentage of total loans due to 29% growth in the loan portfolio in 2003.

The table below presents, for the years 1999 through 2003, information regarding the Company's provision and allowance for loan losses.

Table 7

	Year Ended December 31,				
(dollars in thousands)	**2003**	2002	2001	2000	1999
Balance at beginning of year	**$5,146**	$4,544	$3,732	$2,841	$2,232
Provisions charged to operating expenses	**1,695**	1,435	1,469	1,050	762
	6,841	5,979	5,201	3,891	2,994
Recoveries of loans previously charged-off:					
Commercial	**66**	93	3	6	8
Consumer	**85**	2	21	8	4
Real estate	**115**	21	0	0	1
Total recoveries	**266**	116	24	14	13
Loans charged-off:					
Commercial	**(483)**	(561)	(475)	(1)	(150)
Consumer	**(331)**	(70)	(85)	(95)	(10)
Real estate	**(286)**	(318)	(121)	(77)	(6)
Total charged-off	**(1,100)**	(949)	(681)	(173)	(166)
Net charge-offs	**(834)**	(833)	(657)	(159)	(153)
Balance at end of year	**$6,007**	$5,146	$4,544	$3,732	$2,841
Net charge-offs (recoveries) to average loans outstanding	**0.20%**	0.23%	0.21%	0.06%	0.08%
Allowance for loan losses to year-end loans	**1.26%**	1.40%	1.33%	1.29%	1.31%

Allocation of the Allowance for Loan Losses

The following table details the allocation of the allowance for loan losses to the various categories. The allocation is made for analytical purposes and it is not necessarily indicative of the categories in which future credit losses may occur. The total allowance is available to absorb losses from any segment of loans.

TABLE 8

	Allowance for Loan Losses at December 31,									
	2003		2002		2001		2000		1999	
(dollars in thousands)	**Amount**	**% Gross Loans**	Amount	% Gross Loans	Amount	% Gross Loans	Amount	% Gross Loans	Amount	% Gross Loans
Commercial loans and lines of credit	**$2,636**	**21%**	$2,428	24%	$ 986	23%	$ 178	19%	$ 155	18%
Consumer	**717**	**15**	452	9	157	11	143	11	224	10
Real estate, construction and land development:										
Commercial	**2,157**	**47**	1,698	48	3,240	50	3,286	55	2,335	56
Residential	**497**	**17**	568	19	161	16	125	15	127	16
Total	**$6,007**	**100%**	$5,146	100%	$4,544	100%	$3,732	100%	$2,841	100%

Deposits

Total deposits at December 31, 2003, were $906.5 million, up $179.6 million, or 25%, over total deposits of $727.0 million at December 31, 2002. The Company remains a deposit-driven financial institution with emphasis on core deposit accumulation and retention as a basis for sound growth and profitability. The Company regards core deposits as all deposits other than public certificates of deposits. Deposits in the various core categories, increased $170.8 million, or 25%, in 2003 over 2002. Total deposits averaged $802.3 million for 2003, an increase of $160.8 million, or 25%, over the 2002 average of $641.5 million. The average balance on noninterest-bearing demand deposits increased in 2003 by $28.0 million, or 24%, compared to the prior year. The average balance of interest bearing demand accounts (money market and interest checking accounts) for 2003 increased by $88.8 million, or 57%, over the average balance for the prior year. The average total balance of all savings accounts was $235.5 million, a $38.3 million, or 19%, increase over the average balance for 2002. The average balance of all time deposits in 2003 was $178.7 million, an increase of $5.6 million, or 3%, over the average balance for 2002. For 2003, the cost of total deposits was 1.26% as compared to 2.02% in 2002.

The Company believes that its record of sustaining core deposit growth is reflective of the Company's retail approach to banking which emphasizes a combination of free checking accounts, convenient branch locations, extended hours of operation, unparalleled quality customer service, and active marketing.

The average balances and weighted average rates paid on deposits for 2003, 2002 and 2001 are presented below.

TABLE 9

	Year Ended December 31,					
(dollars in thousands)	**2003 Average Balance/Rate**		2002 Average Balance/Rate		2001 Average Balance/Rate	
Demand deposits:						
Noninterest-bearing	**$142,805**		$114,758		$ 91,352	
Interest-bearing (money market and checking)	**245,264**	**0.90%**	156,441	1.30%	108,349	2.24%
Savings	**235,515**	**1.02**	197,225	1.96	141,350	2.95
Time	**178,674**	**3.07**	173,064	4.06	160,031	5.52
Total deposits	**$802,258**		$641,488		$501,082	

The remaining maturity for certificates of deposit of $100,000 or more as of December 31, 2003, 2002 and 2001 is presented in Table 10.

TABLE 10

(in thousands)	**2003**	2002	2001
3 months or less	**$35,065**	$31,591	$32,092
3 to 6 months	**21,202**	20,462	17,493
6 to 12 months	**18,520**	16,390	9,028
Over 12 months	**16,612**	11,427	16,292
Total	**$91,399**	$79,870	$74,905

Interest Rate Sensitivity

The management of interest rate sensitivity seeks to avoid fluctuating net interest margins and to provide consistent net interest income through periods of changing interest rates.

The Company's risk of loss arising from adverse changes in the fair value of financial instruments, or market risk, is composed primarily of interest rate risk. The primary objective of the Company's asset/liability management activities is to maximize net interest income while maintaining acceptable levels of interest rate risk. The Company's Asset/Liability Committee (ALCO) is responsible for establishing policies to limit exposure to interest rate risk, and to ensure procedures are established to monitor compliance with those policies. The Company's Board of Directors reviews the guidelines established by ALCO.

An interest rate sensitive asset or liability is one that, within a defined time period, either matures or experiences an interest rate change in line with general market interest rates. Historically, the most common method of estimating interest rate risk was to measure the maturity and repricing relationships between interest-earning assets and interest-bearing liabilities at specific points in time ("GAP"), typically one year. Under this method, a company is considered liability sensitive when the amount of its interest-bearing liabilities exceeds the amount of its interest-earning assets within the one-year horizon. However, assets and liabilities with similar repricing characteristics may not reprice at the same time or to the same degree. As a result, the Company's GAP does not necessarily predict the impact of changes in general levels of interest rates on net interest income. Table 11 shows the GAP position for the Company as of December 31, 2003.

TABLE 11

	December 31, 2003					
(in thousands)	**1 – 90 Days**	**91 – 180 Days**	**181 – 365 Days**	**1 – 5 Years**	**Beyond 5 Years**	**Total**
Interest earning assets:						
Loans receivable	**$ 152,491**	**$ 8,978**	**$ 12,711**	**$132,706**	**$176,672**	**$483,558**
Securities	**41,222**	**34,919**	**59,118**	**243,552**	**102,041**	**480,852**
Federal funds sold	**0**	**0**	**0**	**0**	**0**	**0**
Total interest earning assets	**193,713**	**43,897**	**71,829**	**376,258**	**278,713**	**964,410**
Interest-bearing liabilities:						
Transaction accounts	**167,764**	**0**	**0**	**0**	**386,121**	**553,885**
Time deposits	**60,434**	**30,071**	**45,348**	**46,375**	**0**	**182,228**
Short-term borrowings	**79,000**	**0**	**0**	**0**	**0**	**79,000**
Trust capital securities	**0**	**0**	**0**	**0**	**13,000**	**13,000**
Total interest-bearing liabilities	**307,198**	**30,071**	**45,348**	**46,375**	**399,121**	**828,113**
Period GAP	**(113,485)**	**13,826**	**26,481**	**329,883**	**(120,408)**	**$136,297**
Cumulative GAP	**$(113,485)**	**$(99,659)**	**$(73,178)**	**$256,705**	**$136,297**	

Notes: Nonaccrual loans, deferred fees on loans and overdrafts have been excluded in the loans receivable balances. Securities are reported at current face for purposes of this table.

Management believes the simulation of net interest income in different interest rate environments provides a more meaningful measure of interest rate risk. Income simulation analysis captures not only the potential of all assets and liabilities to mature or reprice, but also the probability that they will do so. Income simulation also attends to the relative interest rate sensitivities of these items, and projects their behavior over an extended period of time. Finally, income simulation permits management to assess the probable effects on the balance sheet not only of changes in interest rates, but also of proposed strategies for responding to them.

The Company's income simulation model analyzes interest rate sensitivity by projecting net income over the next 24 months in a flat rate scenario versus net income in alternative interest rate scenarios. Management continually reviews and refines its interest rate risk management process in response to the changing economic climate. Currently, the Company's model projects a 200 basis point increase and a 100 basis point decrease during the next year, with rates remaining constant in the second year.

The Company's Asset/Liability Committee (ALCO) policy has established that income sensitivity will be considered acceptable if overall net income volatility in a plus 200 or minus 100 basis point scenario is within 15% of net income in a flat rate scenario in the first year and 30% using a two year planning window. At December 31, 2003, the Company's income simulation model indicates net income would be higher by 3.1%, or $309,000, in the first year and lower by 0.1%, or $33,000, over a two-year timeframe, if rates decreased 100 basis points as compared to lower by 0.5% and by 5.2%, respectively, at December 31, 2002. The model projects that net income would be lower by 1.0%, or $518,000, and lower by 3.4%, or $336,000, in the first year and over a two-year timeframe, respectively, if rates increased 200 basis points, as compared to higher by 5.4% and 16.8%, respectively, at December 31, 2002. All of these forecasts are within an acceptable level of interest rate risk per the policies established by ALCO.

Management also monitors interest rate risk by utilizing a market value of equity model. The model assesses the impact of a change in interest rates on the market value of all the Company's assets and liabilities, as well as any off balance sheet items. The model calculates the market value of the Company's assets and liabilities in excess of book value in the current rate scenario, and then compares the excess of market value over book value given an immediate 200 basis point increase in rates and a 100 basis point decrease in rates. The Company's ALCO policy indicates that the level of interest rate risk is unacceptable if the immediate change would result in the loss of 60% or more of the excess of market value over book value in the current rate scenario. At December 31, 2003, the market value of equity indicates an acceptable level of interest rate risk.

The market value of equity model reflects certain estimates and assumptions regarding the impact on the market value of the Company's assets and liabilities given an immediate 200 basis point change in interest rates. One of the key assumptions is the market value assigned to the Company's core deposits, or the core deposit premium. Using an independent consultant, the Company has completed and updated comprehensive core deposit studies in order to assign its own core deposit premiums as permitted by regulation. The studies have consistently confirmed management's assertion that the Company's core deposits have stable balances over long periods of time, are relatively insensitive to changes in interest rates and have significant longer average lives and durations than the Company's loans and investment securities. Thus, these core deposit balances provide an internal hedge to market fluctuations in the Company's fixed rate assets. Management believes the core deposit premiums produced by its market value of equity model at December 31, 2003 provide an accurate assessment of the Company's interest rate risk.

Liquidity

Liquidity management involves the Company's ability to generate cash or otherwise obtain funds at reasonable rates to support asset growth and reduce assets to meet deposit withdrawals, to maintain reserve requirements, and to otherwise operate the Company on an ongoing basis. Liquidity sources from asset categories are provided primarily by cash, federal funds sold, and the cash flow from the amortizing securities and loan portfolios. The primary source of liquidity from liability categories is the generation of additional core deposit balances. As previously mentioned, total core deposits increased by $170.8 million, or 25%, in 2003.

Additionally, the Company has established secondary sources of liquidity consisting of federal funds lines of credit, repurchase agreements, and borrowing capacity at the Federal Home Loan Bank, which can be drawn upon if needed. As of December 31, 2003, the total potential liquidity for the Company through these secondary sources was $270 million of which $191 million was available at December 31, 2003. In view of the primary and secondary sources as previously mentioned, management believes the Company is capable of meeting its anticipated liquidity needs.

Aggregate Contractual Obligations

The following table represents the Company's on-and–off balance sheet aggregate contractual obligations to make future payments as of December 31, 2003:

TABLE 12

	December 31, 2003				
(in thousands)	**1 Year or Less**	**Over 1 to 3 Years**	**Over 3 to 5 Years**	**Over 5 Years**	**Total**
Time Deposits	**$135,853**	**$23,811**	**$22,564**	**$ 0**	**$182,228**
Long-Term Debt	**0**	**0**	**0**	**13,000**	**13,000**
Operating Leases	**1,618**	**2,618**	**2,241**	**10,249**	**16,726**
Sponsorship Obligation [1]	**150**	**400**	**617**	**2,333**	**3,500**
Total	**$137,621**	**$26,829**	**$25,422**	**$25,582**	**$215,454**

[1] *Sponsorship Obligation was signed in January 2004.*

Off-Balance Sheet Arrangements

The Company, in the conduct of ordinary business operations routinely enters into contracts for services. These contracts may require payment for services to be provided in the future and may also contain penalty clauses for the early termination of the contract. Management is not aware of any additional commitments or contingent liabilities, which may have a material adverse impact on the liquidity or capital resources of the Company.

The Company is also party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. See Note 5 in the *Notes to the Consolidated Financial Statements* for additional information.

Short-Term Borrowings

Short-term borrowings, which consist of securities sold under agreement to repurchase and federal funds purchased, were used in 2003 and 2002 to meet short-term liquidity needs. For 2003, short-term borrowings averaged $11.7 million and repurchase agreements averaged $5.3 million. The average rate paid during 2003 on the Company's short-term borrowings was 1.23% and the average rate paid on repurchase agreements was 1.20%. Short-term borrowings and repurchase agreements totaled $39.0 million and $40.0 million, respectively at December 31, 2003. The maximum short-term borrowings outstanding at any month-end in 2003 were $50.0 million. The maximum repurchase agreements outstanding at any month-end in 2003 were $40.0 million. Amounts outstanding during 2002 and 2001 were not significant.

Long-Term Debt

Long-term debt consists of Trust Capital Securities through Commerce Harrisburg Capital Trust I and Commerce Harrisburg Capital Trust II, Delaware business trust subsidiaries of the Company. At December 31, 2003, all of the Capital Trust Securities qualified as Tier I capital for regulatory capital purposes. Proceeds of the trust capital securities are for general corporate purposes, including additional capitalization of the Company's wholly-owned banking subsidiary. Reference should be made to Note 10 in the *Notes to the Consolidated Financial Statement* for further analysis of the Company's long-term debt. Long-term debt totaled $13.0 million at December 31, 2003 and 2002.

Stockholders' Equity and Capital Adequacy

At December 31, 2003, stockholders' equity totaled $49.7 million, up $6.9 million, or 16%, over stockholders' equity at December 31, 2002. This increase was due to the Company's net income for the year, shares issued under stock purchase and stock option plans, offset by unrealized losses on securities available for sale. Stockholders' equity as a percent of total assets was 4.73% at December 31, 2003, compared to 5.44% at December 31, 2002.

Risk-based capital provides the basis for which all banks are evaluated in terms of capital adequacy. The risk-based capital standards require all banks to have Tier 1 capital of at least 4% and total capital, including Tier 1 capital, of at least 8% of risk-adjusted assets. Tier 1 capital includes common stockholders' equity and qualifying perpetual preferred stock together with related surpluses and retained earnings. Total capital may be comprised of total Tier 1 capital plus limited life preferred stock, qualifying debt instruments, and the allowance for loan losses.

Table 13 provides a comparison of the Bank's risk-based capital ratios and leverage ratios to the minimum regulatory requirements for the periods indicated.

TABLE 13

	Actual December 31, 2003	2002	For Capital Adequacy Purposes	To Be Well-Capitalized Under Prompt Corrective Action Provisions
Tier 1 Capital	**9.49%**	11.11%	4.00%	6.00%
Total Capital	**10.42**	12.17	8.00	10.00
Leverage ratio (to average assets)	**6.14**	6.97	4.00	5.00

At December 31, 2003, the consolidated capital levels of the Company and of the subsidiary bank (Commerce) met the definition of a "well-capitalized" institution, i.e., a leverage capital ratio exceeding 5%, a Tier 1 risk-based capital ratio exceeding 6%, and a total risk-based capital ratio exceeding 10%.

The Company's common stock is listed for trading on the NASDAQ Small Cap Market under the symbol COBH. The Company offers a Dividend Reinvestment and Stock Purchase Plan by which dividends on the Company's Common Stock and optional cash payments of up to $5,000 per quarter (subject to change) may be invested in Common Stock at a 3% discount (subject to change) to the market price and without payment of brokerage commissions.

Forward-Looking Statements

The Company may from time to time make written or oral "forward-looking statements," including statements contained in the Company's filings with the Securities and Exchange Commission (including this Annual Report and Form 10-K and the exhibits hereto and thereto), in its reports to stockholders and in other communications by the Company, which are made in good faith by the Company pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include statements with respect to the Company's beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties and are subject to change based on various factors (some of which are beyond the Company's control). The words "may", "could", "should", "would", "believe", "anticipate", "estimate", "expect", "intend", "plan" and similar expressions are intended to identify forward-looking statements. The following factors, among others, could cause the Company's financial performance to differ materially from that expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies, including interest rate policies of the Board of Governors of the Federal Reserve System (the "FRB"); inflation; interest rate, market and monetary fluctuations; the timely development of competitive new products and services by the Company and the acceptance of such products and services by customers; the willingness of customers to substitute competitors' products and services for the Company's products and services and vice versa; the impact of changes in financial services' laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes; future acquisitions; the expense savings and revenue enhancements from acquisitions being less than expected; the growth and profitability of the Company's noninterest or fee income being less than expected; unanticipated regulatory or judicial proceedings; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by or on behalf of the Company.

Impact of Inflation and Changing Prices

Interest rates have a more significant impact on the Company's performance than do the effects of general levels of inflation, since most of the Company's assets and liabilities are monetary in nature. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services as measured by the Consumer Price Index. The liquidity and maturity structure of the Company's assets and liabilities are critical to the maintenance of acceptable performance levels.

Consolidated Balance Sheets

(in thousands, except share amounts)	December 31, **2003**	2002
Assets		
Cash and due from banks	**$ 37,715**	$ 30,950
Federal funds sold	**0**	44,500
Cash and cash equivalents	**37,715**	75,450
Securities, available for sale at fair value	**275,400**	205,436
Securities, held to maturity at cost (fair value 2003: $201,568; 2002: $101,036)	**199,863**	97,625
Loans, held for sale	**9,164**	10,514
Loans receivable, net of allowance for loan losses (allowance 2003: $6,007; 2002: $5,146)	**469,937**	363,735
Restricted investments in bank stock	**5,227**	2,045
Premises and equipment, net	**38,178**	26,409
Other assets	**16,505**	5,384
Total assets	**$1,051,989**	$786,598
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	**$ 170,414**	$127,199
Interest-bearing	**736,113**	599,756
Total deposits	**906,527**	726,955
Short-term borrowings	**39,000**	0
Repurchase agreements	**40,000**	0
Trust capital securities	**13,000**	13,000
Other liabilities	**3,738**	3,831
Total liabilities	**1,002,265**	743,786
Stockholders' Equity:		
Preferred stock – Series A noncumulative; $10.00 par value; 1,000,000 shares authorized; 40,000 shares issued and outstanding	**400**	400
Common stock – $1.00 par value; 10,000,000 shares authorized; (issued and outstanding 2003: 2,291,805; 2002: 2,117,089)	**2,292**	2,117
Surplus	**38,725**	31,909
Retained earnings	**7,758**	6,866
Accumulated other comprehensive income	**549**	1,520
Total stockholders' equity	**49,724**	42,812
Total liabilities and stockholders' equity	**$1,051,989**	$786,598

See accompanying notes

Consolidated Statements of Income

(in thousands, except per share amounts)	Year Ended December 31, 2003	2002	2001
Interest Income			
Loans receivable, including fees:			
Taxable	**$27,545**	$26,755	$26,532
Tax-exempt	**216**	111	120
Securities:			
Taxable	**17,108**	14,514	10,860
Tax-exempt	**453**	107	94
Federal funds sold	**220**	508	641
Total interest income	**45,542**	41,995	38,247
Interest Expense			
Deposits	**10,089**	12,940	15,420
Short-term borrowings	**207**	0	13
Trust capital securities	**1,356**	1,354	760
Total interest expense	**11,652**	14,294	16,193
Net interest income	**33,890**	27,701	22,054
Provision for loan losses	**1,695**	1,435	1,469
Net interest income after provision for loan losses	**32,195**	26,266	20,585
Noninterest Income			
Service charges and other fees	**7,968**	6,766	5,660
Other operating income	**377**	448	541
Gains on sales of loans	**765**	493	354
Gains on sales of securities	**880**	0	52
Total noninterest income	**9,990**	7,707	6,607
Noninterest Expenses			
Salaries and employee benefits	**16,702**	12,491	9,486
Occupancy	**3,420**	2,403	2,133
Furniture and equipment	**1,844**	1,523	1,402
Advertising and marketing	**2,425**	2,181	1,722
Data processing	**2,148**	1,890	1,313
Postage and supplies	**986**	862	846
Other	**4,985**	4,078	3,610
Total noninterest expenses	**32,510**	25,428	20,512
Income before income taxes	**9,675**	8,545	6,680
Provision for federal income taxes	**3,118**	2,871	2,232
Net income	**$ 6,557**	$ 5,674	$ 4,448
Net Income per Common Share			
Basic	**$2.88**	$2.58	$2.14
Diluted	**$2.68**	$2.37	$1.94

See accompanying notes

Consolidated Statements of Stockholders' Equity

(dollars in thousands)	Preferred Stock	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
December 31, 2000	**$400**	**$1,749**	**$20,861**	**$4,334**	**$(676)**	**$26,668**
Comprehensive income:						
Net income	–	–	–	4,448	–	4,448
Change in unrealized gains (losses) on securities, net of taxes and reclassification adjustment	–	–	–	–	565	565
Total comprehensive income						5,013
Dividends declared on preferred stock	–	–	–	(80)	–	(80)
Common stock of 23,231 shares issued under stock option plans	–	24	193	–	–	217
Income tax benefit of stock options exercised		–	78	–	–	78
Common stock of 290 shares issued under employee stock purchase plan	–	–	9	–	–	9
Proceeds from issuance of 20,016 shares of common stock in connection with dividend reinvestment and stock purchase plan	–	20	678	–	–	698
5% common stock dividend and cash paid in lieu of fractional shares (89,378 shares issued)	–	89	3,444	(3,543)	–	(10)
December 31, 2001	**$400**	**$1,882**	**$25,263**	**$5,159**	**$ (111)**	**$32,593**
Comprehensive income:						
Net income	–	–	–	5,674	–	5,674
Change in unrealized gains (losses) on securities, net of taxes and reclassification adjustment	–	–	–	–	1,631	1,631
Total comprehensive income						7,305
Dividends declared on preferred stock	–	–	–	(80)	–	(80)
Common stock of 112,379 shares issued under stock option plans	–	113	1,625	–	–	1,738
Income tax benefit of stock options exercised	–		378	–	–	378
Common stock of 440 shares issued under employee stock purchase plan	–	–	19	–	–	19
Proceeds from issuance of 21,733 shares of common stock in connection with dividend reinvestment and stock purchase plan	–	22	846	–	–	868
5% common stock dividend and cash paid in lieu of fractional shares (100,577 shares issued)	–	100	3,778	(3,887)	-	(9)
December 31, 2002	**$400**	**$2,117**	**$31,909**	**$6,866**	**$ 1,520**	**$42,812**
Comprehensive income:						
Net income	–	–	–	6,557	–	6,557
Change in unrealized gains (losses) on securities, net of taxes and reclassification adjustment	–	–	–	–	(971)	(971)
Total comprehensive income						5,586
Dividends declared on preferred stock	–	–	–	(80)	–	(80)
Common stock of 48,226 shares issued under stock option plans	–	48	508	–	–	556
Income tax benefit of stock options exercised		–	178	–	–	178
Common stock of 110 shares issued under employee stock purchase plan	–	–	4	–	–	4
Proceeds from issuance of 16,950 shares of common stock in connection with dividend reinvestment and stock purchase plan	–	17	660	–	–	677
5% common stock dividend and cash paid in lieu of fractional shares (109,430 shares issued)	–	110	5,466	(5,585)	-	(9)
December 31, 2003	**$400**	**$2,292**	**$38,725**	**$7,758**	**$549**	**$49,724**

See accompanying notes

Consolidated Statements of Cash Flows

(in thousands)	Year Ended December 31, 2003	2002	2001
Operating Activities			
Net income	**$ 6,557**	$ 5,674	$ 4,448
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	**1,695**	1,435	1,469
Provision for depreciation and amortization	**1,831**	1,484	1,403
Deferred income taxes	**285**	68	(251)
Amortization of securities premiums and accretion of discounts, net	**3,036**	926	219
Gains on sales of securities	**(880)**	0	(52)
Proceeds from sales of loans	**106,950**	67,794	48,887
Loans originated for sale	**(104,835)**	(70,154)	(50,944)
Gains on sales of loans	**(765)**	(493)	(354)
(Increase) decrease in other assets	**(10,724)**	93	(733)
Increase (decrease) in other liabilities	**(93)**	1,272	724
Net cash provided by operating activities	**3,057**	8,099	4,816
Investing Activities			
Securities held to maturity:			
Proceeds from principal repayments and maturities	**45,855**	34,681	18,589
Purchases	**(148,228)**	(29,121)	(88,112)
Securities available for sale:			
Proceeds from principal repayments and maturities	**191,681**	77,946	43,922
Proceeds from sales	**8,294**	0	7,497
Purchases	**(273,431)**	(176,945)	(64,833)
Net (purchase) redemption of restricted investments in bank stock	**(3,182)**	548	(305)
Proceeds from sale of loans receivable	**0**	0	3,255
Net increase in loans receivable	**(107,897)**	(27,040)	(56,254)
Purchases of premises and equipment	**(13,600)**	(6,306)	(6,353)
Net cash used by investing activities	**(300,508)**	(126,237)	(142,594)
Financing Activities			
Net increase in demand, interest checking, money market, and savings deposits	**166,787**	159,992	102,383
Net increase in time deposits	**12,785**	5,225	12,772
Net increase in short-term borrowings	**79,000**	0	0
Proceeds from issuance of trust capital securities	**0**	0	8,000
Proceeds from common stock options exercised	**556**	1,738	217
Proceeds from dividend reinvestment and common stock purchase plan	**677**	868	698
Cash dividends on preferred stock and cash in lieu of fractional shares	**(89)**	(90)	(86)
Net cash provided by financing activities	**259,716**	167,733	123,984
Increase (decrease) in cash and cash equivalents	**(37,735)**	49,595	(13,794)
Cash and cash equivalents at beginning of year	**75,450**	25,855	39,649
Cash and cash equivalents at year-end	**$37,715**	$75,450	$25,855

See accompanying notes.

1. Significant Accounting Policies

Nature of Operations and Basis of Presentation

The consolidated financial statements include the accounts of Pennsylvania Commerce Bancorp, Inc. (the Company) and its wholly-owned subsidiaries Commerce Bank/ Harrisburg, N.A. (Commerce or Bank), Commerce Harrisburg Capital Trust I (Trust I) and Commerce Harrisburg Capital Trust II (Trust II). All material intercompany transactions have been eliminated. The Company was formed July 1, 1999 and is subject to regulation of the Federal Reserve Bank.

The Company is a one-bank holding company headquartered in Camp Hill, Pennsylvania and provides full banking services through its subsidiary Commerce Bank. As a national bank, Commerce is subject to regulation of the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation. The Bank serves primarily the Harrisburg, York, and Reading markets of South Central Pennsylvania.

Estimates

The financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. These principles require management to make estimates and assumptions that affect reported amounts of assets and liabilities and require disclosure of contingent assets and liabilities. In the opinion of management, all adjustments considered necessary for fair presentation have been included and are of a normal, recurring nature. Actual results could differ from those estimates.

Significant Group Concentrations of Credit Risk

Most of the Company's activities are with customers located within the South Central Pennsylvania Region. Note 3 discusses the types of securities that the Company invests in. Notes 4 and 6 discuss the types of lending that the Company engages in as well as loan concentrations. The Company does not have any significant concentrations to any one industry or customer.

Securities

Securities classified as held to maturity are those debt securities that the Company has both the intent and ability to hold to maturity regardless of changes in market conditions, liquidity needs, or general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the interest method over the estimated average life of the securities.

Securities classified as available for sale are those debt securities that the Company intends to hold for an indefinite period of time, but not necessarily to maturity. Any decision to sell a security classified as available for sale would be based on various factors, including significant movements in interest rates, changes in the maturity mix of the Company's assets and liabilities, liquidity needs, regulatory capital considerations, and other similar factors. Securities available for sale are carried at fair value. Unrealized gains or losses are reported in other comprehensive income, net of the related deferred tax effect. Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the estimated average life of the securities.

Management determines the appropriate classification of debt securities at the time of purchase and re-evaluates such designation as of each balance sheet date.

Loans Receivable

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees and costs. Interest income is accrued on the unpaid principal balance. Loan origination fees and costs are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Bank is generally amortizing these amounts over the contractual life of the loan.

The accrual of interest is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectibility of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectibility of the total contractual principal and interest is no longer in doubt.

Allowance for Loan Losses

The allowance for loan losses is established through provisions for loan losses charged against income. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

The allowance consists of specific and general components. The specific component relates to loans that are classified impaired. For such loans, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. Additionally, the general component is maintained to cover uncertainties that could affect management's estimates of probable losses. This component reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating losses in the portfolio.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on the Bank's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans. A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures.

Loans Held for Sale

Loans held for sale are comprised of residential loans and student loans that the Company originates with the intention of selling in the future. These loans are carried at the lower of cost or estimated fair value, calculated in the aggregate.

Restricted Investments in Bank Stock

Restricted investments in bank stocks include Federal Home Loan Bank (FHLB) and Federal Reserve Bank Stocks. Federal law requires a member institution of the FHLB system to hold stock of its district FHLB according to a predetermined formula. The stock is carried at cost.

Advertising Costs

The Company follows the policy of charging the costs of advertising to expense as incurred.

Income Taxes

Deferred income taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted through the provision for income taxes for the effects of changes in tax laws and rates on the date of enactment.

Bank Premises and Equipment

Bank premises and equipment are carried at cost less accumulated depreciation and amortization. Depreciation is charged to operations over the estimated useful lives of the respective assets. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Depreciation and amortization are determined on the straight-line methods for financial reporting purposes, and accelerated methods for income tax purposes.

Foreclosed Assets

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets. Foreclosed assets are included in other assets.

Transfers of Financial Assets

Transfers of financial assets, including sales of loans and loan participations, are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Per Share Data

Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued as well as any adjustments to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options, and are determined using the treasury stock method. Per share amounts have been adjusted to give retroactive effect to stock dividends declared through January 30, 2004.

Off Balance Sheet Financial Instruments

In the ordinary course of business, the Company has entered into off balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded on the balance sheet when they become payable by the borrower to the Company.

Cash Flow Information

For purposes of the statements of cash flows, the Company considers cash and due from banks and federal funds sold as cash and cash equivalents. Generally, federal funds are purchased and sold for one-day periods. Cash paid during the years ended December 31, 2003, 2002, and 2001 for interest was $12.0 million, $14.3 million, and $16.2 million respectively. Income taxes paid totaled $2.5 million, $2.6 million, and $2.4 million in 2003, 2002, and 2001, respectively.

Stock-Based Compensation

The Company accounts for stock awards issued to directors, officers, and key employees using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25. This method requires that compensation expense be recognized to the extent that the fair value of the stock exceeds the exercise price of the stock award at the grant date. The Company generally does not recognize compensation expense related to stock awards because the stock awards generally have fixed terms and exercise prices that are equal to or greater than the fair value of the Company's common stock at the grant date.

For purposes of pro-forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro-forma information is presented in the following table.

	Year Ended December 31,		
(in thousands)	**2003**	2002	2001
Net income:			
As reported	**$6,557**	$5,674	$4,448
Total stock-based compensation cost, net of tax, that would have been included in the determination of net income if the fair value based method had been applied to all awards	**(814)**	(1,434)	(952)
Pro-forma	**5,743**	4,240	3,496
Reported earnings per share:			
Basic	**$2.88**	$2.58	$2.14
Diluted	**2.68**	2.37	1.94
Pro-forma earnings per share:			
Basic	**$2.51**	$1.92	$1.67
Diluted	**2.34**	1.76	1.51

The fair value of each option grant is estimated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions for 2003, 2002, and 2001 respectively: risk-free interest rates of 3.4%, 4.7% and 4.8%; volatility factors of the expected market price of the Company's common stock of .21, .33, and .28; weighted-average expected life of the options of 10 years; and no cash dividends.

Had compensation costs for stock options granted in 2003, 2002 and 2001 been determined based on the fair value at the grant dates for awards under the plan consistent with the provisions of SFAS No. 123, the Company's net income and earnings per share for the years ended December 31, 2003, 2002 and 2001 would have been reduced to the proforma amounts indicated.

New Accounting Standards

In November 2002, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 45 (FIN 45), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." This Interpretation expands the disclosures to be made by a guarantor in its financial statements about its obligations under certain guarantees and requires the guarantor to recognize a liability for the fair value of an obligation assumed under certain specified guarantees. Under FIN 45, the Company does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit, as discussed in Note 5. Adoption of FIN 45 did not have a significant impact on the Company's financial condition or results of operations.

In January 2003, the Financial Accounting Standards Board issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." FIN 46 was revised in December 2003. This Interpretation provides new guidance for the consolidation of variable interest entities (VIEs) and requires such entities to be consolidated by their primary beneficiaries if the entities do not effectively disperse risk among parties involved. The Interpretation also adds disclosure requirements for investors that are involved with unconsolidated VIEs. The disclosure requirements apply to all financial statements issued after December 31, 2003. The consolidation requirements apply to companies that have interests in special-purpose entities for periods ending after December 15, 2003. Consolidation of other types of VIEs is required in financial statements for periods ending after March 15, 2004.

In its current form, FIN 46 will require the Company to deconsolidate its investment in Trust I and Trust II after the March 15, 2004 effective date. The deconsolidation of subsidiary trusts of bank holding companies formed in connection with the issuance of trust preferred securities, like Trust I and Trust II, appears to be an unintended consequence of FIN 46. Upon adoption of FIN 46 as of March 31, 2004, the trusts will be deconsolidated and the junior subordinated debentures will be reported in the balance sheet as "Long-term debt." The Company's equity interest in the trusts, which is not significant, will be reported in "Other assets." In July 2003, the Board of Governors of the Federal Reserve System issued a supervisory letter instructing bank holding companies to continue to include the trust preferred securities in their Tier 1 capital for regulatory capital purposes until notice is given to the contrary. The Federal Reserve intends to review the regulatory implications of any accounting treatment changes and, if necessary or warranted, provide further appropriate guidance. If the outcome is that Trust I and Trust II are no longer included in consolidated results, the Corporation will still meet all regulatory capital requirements to which they are subject.

In April 2003, the Financial Accounting Standards Board (FASB) issued Statement No. 149, "Amendment of Statement No. 133, Accounting for Derivative Instruments and Hedging Activities." This Statement clarifies the definition of a derivative and incorporates certain decisions made by the Board as part of the Derivatives Implementation Group process. This Statement is effective for contracts entered into or modified and for hedging relationships designated after June 30, 2003 and should be applied prospectively. The provisions of the Statement that relate to implementation issues addressed by the Derivatives Implementation Group that have been effective should continue to be applied in accordance with their respective dates. Adoption of this standard did not have an impact on the Company's financial condition or results of operations.

In May 2003, the Financial Accounting Standards Board issued Statement No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This Statement requires that an issuer classify a financial instrument that is within its scope as a liability. Many of these instruments were previously classified as equity. This Statement was effective for financial instruments entered into or modified after May 31, 2003 and otherwise was effective beginning July 1, 2003. The adoption of this standard did not have an impact on the Company's financial condition or results of operations.

Segment Reporting

Commerce acts as an independent community financial services provider, and offers traditional banking and related financial services to individual, business and government customers. Through its branches, the Company offers a full array of commercial and retail financial services.

Management does not separately allocate expenses, including the cost of funding loan demand, between the commercial and retail operations of the Company. As such, discrete financial information is not available and segment reporting would not be meaningful.

2. Restrictions on Cash and Due From Bank Accounts

The Bank is required to maintain average reserve balances with the Federal Reserve Bank. The average amount of those reserve balances maintained for 2003 and 2002 was approximately $6.5 million and $4.3 million, respectively.

3. Securities

The amortized cost and fair value of securities are summarized in the following tables.

	December 31, 2003			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale				
U.S. Government Agency securities	**$ 24,000**	**$ 10**	**$ (438)**	**$ 23,572**
Mortgage-backed securities	**248,555**	**1,726**	**(683)**	**249,598**
Corporate debt securities	**2,013**	**217**	**0**	**2,230**
Total	**$274,568**	**$1,953**	**$(1,121)**	**$275,400**
Held to Maturity				
U.S. Government Agency securities	**$ 40,010**	**$ 243**	**$ (734)**	**$ 39,519**
Municipal securities	**6,845**	**107**	**(198)**	**6,754**
Mortgage-backed securities	**135,925**	**1,609**	**(1,044)**	**136,490**
Corporate debt securities	**17,083**	**1,722**	**0**	**18,805**
Total	**$199,863**	**$3,681**	**$(1,976)**	**$201,568**

	December 31, 2002			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale				
U.S. Government Agency securities	$ 12,307	$ 204	$ 0	$ 12,511
Mortgage-backed securities	184,793	2,203	(526)	186,470
Corporate debt securities	6,033	422	0	6,455
Total	$203,133	$2,829	$ (526)	$205,436
Held to Maturity				
U.S. Government Agency securities	$ 10,005	$ 525	$ 0	$ 10,530
Municipal securities	1,996	79	0	2,075
Mortgage-backed securities	63,909	2,284	(8)	66,185
Corporate debt securities	21,715	795	(264)	22,246
Total	$ 97,625	$3,683	$ (272)	$101,036

The amortized cost and fair value of debt securities at December 31, 2003 by contractual maturity are shown in the following table. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations.

	Held to Maturity		Available for Sale	
(in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 1,100	$ 1,128	$ 0	$ 0
Due after one year through five years	4,534	4,901	0	0
Due after five years through ten years	18,956	18,910	5,000	4,899
Due after ten years	39,348	40,139	21,013	20,903
	63,938	65,078	26,013	25,802
Mortgage-backed securities	135,925	136,490	248,555	249,598
Total	$199,863	$201,568	$274,568	$275,400

Gross gains of $640,000 and gross losses of $0 were realized on sales of securities available for sale in 2003. Additionally, gross gains of $240,000 and gross losses of $0 were realized on sales of securities held to maturity. The sale of securities held to maturity consisted of $4.5 million of corporate bonds which were sold solely due to a continued deterioration in the issuer's creditworthiness over the past three years. The securities were sold prior to December 31, 2003 and settled in January 2004.

There were no sales of securities available for sale in 2002. Gross gains of $53,000 and gross losses of $1,000 were realized on sales of securities available for sale in 2001.

At December 31, 2003 and 2002 securities with a fair value of $257.1 million and $200.1 million respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

The following table shows the Company's investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available for Sale						
U.S. Government Agency securities	$ 13,562	$ (438)	$ –	$ –	$ 13,562	$ (438)
Mortgage-backed securities	84,564	(639)	4,684	(44)	89,248	(683)
Corporate debt securities	–	–	–	–	–	–
Held to Maturity						
U.S. Government Agency securities	29,272	(734)	–	–	29,272	(734)
Municipal securities	4,650	(198)	–	–	4,650	(198)
Mortgage-backed securities	53,408	(1,044)	–	–	53,408	(1,044)
Corporate debt securities	–	–	–	–	–	–
Total temporarily impaired securities	$185,456	$(3,053)	$4,684	$(44)	$190,140	$(3,097)

The table above represents 48 securities where the current fair value is less than the related amortized cost.

In management's opinion, the unrealized losses reflects changes in interest rates subsequent to the acquisition of specific securities and represent temporary impairment of the securities.

4. Loans Receivable and Allowance for Loan Losses

A summary of loans receivable is as follows:

	December 31,	
(in thousands)	**2003**	2002
Real Estate:		
Commercial Mortgage	**$194,609**	$144,959
Construction and land development	**26,895**	31,034
Residential Mortgage	**72,713**	66,190
Tax-Exempt	**5,720**	5,629
Commercial Business	**58,894**	49,226
Consumer	**71,007**	34,598
Lines of Credit	**46,106**	37,245
	475,944	368,881
Less: Allowance for Loan Losses	**6,007**	5,146
Net Loans Receivable	**$469,937**	$363,735

The following is a summary of the transactions in the allowance for loan losses.

	Year Ended December 31,		
(in thousands)	**2003**	2002	2001
Balance at beginning of year	**$5,146**	$4,544	$3,732
Provision charged to expense	**1,695**	1,435	1,469
Recoveries	**266**	116	24
Loans charged off	**(1,100)**	(949)	(681)
Balance at end of year	**$6,007**	$5,146	$4,544

At December 31, 2003 and 2002, the recorded investment in loans considered to be impaired under FASB Statement No. 114 "Accounting by Creditors for Impairment of a Loan" totaled $9.8 million and $1.5 million, respectively. At December 31, 2003, $2.5 million of impaired loans have a specific valuation allowance of $1.5 million as compared to $934,000 of impaired loans having a specific valuation allowance of $481,000 at December 31, 2002. Total non-accrual loans at December 31, 2003 and 2002 totaled $787,000 and $1.6 million, respectively. Loans past due 90 days or more and still accruing totaled $385,000 at December 31, 2003 and $55,000 at December 31, 2002.

Impaired loans averaged approximately $5.5 million, $1.5 million and $531,000 during 2003, 2002 and 2001, respectively. Interest income recognized on these loans amounted to $41,000, $79,000 and $33,000 during 2003, 2002 and 2001, respectively.

Certain directors and executive officers of the Company, including their associates and companies, have loans with the Bank. Such loans were made in the ordinary course of business at the Bank's normal credit terms including interest rate and collateralization, and do not represent more than a normal risk of collection. Total loans to these persons and companies amounted to approximately $14.0 million and $11.3 million at December 31, 2003 and 2002, respectively. During 2003, $7.8 million of new advances were made and repayments totaled $5.1 million.

5. Loan Commitments and Standby Letters of Credit

Loan commitments are made to accommodate the financial needs of Commerce's customers. Standby letters of credit commit the Bank to make payments on behalf of customers when certain specified future events occur. They primarily are issued to facilitate the customers' normal course of business transactions. Historically, almost all of the Bank's standby letters of credit expire unfunded.

Both types of lending arrangements have credit risk essentially the same as that involved in extending loans to customers and are subject to the Bank's normal credit policies. Letter of credit commitments are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Outstanding letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The majority of these standby letters of credit expire within the next twelve months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending other loan commitments. The Bank requires collateral supporting these letters of credit as deemed necessary. Management believes that the proceeds obtained through a liquidation of such collateral would be sufficient to cover the maximum potential amount of future payments required under the corresponding guarantees. The current amount of the liability as of December 31, 2003 for guarantees under standby letters of credit issued is not material.

The Bank's maximum exposure to credit loss for loan commitments (unfunded loans and unused lines of credit, including home equity lines of credit) and standby letters of credit outstanding were as follows:

	December 31,	
(in thousands)	**2003**	2002
Commitments to grant loans	**$ 452**	$ 1,628
Unfunded commitments of existing loans	**109,648**	68,105
Standby letters of credit	**8,426**	7,265
Total	**$118,526**	$76,998

6. Concentrations of Credit Risk

The Company's loan portfolio is principally to borrowers throughout Cumberland, Dauphin, York, Lebanon and Berks counties of Pennsylvania where it has full-service branch locations. Commercial real estate loans and loan commitments for commercial real estate projects aggregated $238 million at December 31, 2003.

Commercial real estate loans are collateralized by the related project (principally office buildings, multifamily residential, land development, and other properties) and the Company generally requires loan-to-value ratios of no greater than 80%. Collateral requirements on such loans are determined on a case-by-case basis based on management's credit evaluations of the respective borrowers.

7. Bank Premises, Equipment and Leases

Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the following estimated useful lives of the related assets:

	Years
Buildings and leasehold improvements	2 - 39.5
Furniture, fixtures and equipment	5 - 10
Computer equipment and software	3 - 5

A summary of premises and equipment is as follows:

	December 31,	
(in thousands)	**2003**	2002
Land	**$ 7,753**	$ 4,211
Buildings	**26,398**	19,941
Leasehold improvements	**2,618**	1,919
Furniture, fixtures, and equipment	**11,609**	8,956
	48,378	35,027
Less accumulated depreciation and amortization	**10,200**	8,618
	$38,178	$26,409

Land, buildings, and equipment are leased under non-cancelable operating lease agreements that expire at various dates through 2023. Total rental expense for operating leases in 2003, 2002, and 2001 was $1.4 million, $1.1 million, and $908,000, respectively. At December 31, 2003, future minimum lease payments for noncancelable operating leases are payable as follows:

(in thousands)	
2004	$ 1,618
2005	1,359
2006	1,259
2007	1,215
2008	1,026
Thereafter	10,249
Total minimum lease payments	$16,726

8. Deposits

The composition of deposits is as follows:

	December 31,	
(in thousands)	**2003**	2002
Demand	**$170,414**	$127,199
Interest checking and money market	**312,282**	214,293
Savings	**241,603**	216,020
Time certificates $100,000 or more	**91,399**	79,870
Other time certificates	**90,829**	89,573
	$906,527	$726,955

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

(in thousands)	
2003	$135,853
2004	15,635
2005	8,176
2006	14,257
2007	8,307
	$182,228

9. Short-term Borrowings

Short-term borrowings consist of securities sold under agreements to repurchase and lines of credit. The Bank has a line of credit commitment from the Federal Home Loan Bank (FHLB) for borrowings up to $215 million and certain qualifying assets of the Bank collateralize the line. At December 31, 2003, there was $39 million outstanding on this line of credit at a rate of 1.06%. The Bank has availability under two repurchase agreements to borrow up to $45 million of which $40 million was outstanding as of December 31, 2003 at a rate of 1.23%. The Company has $45 million in securities pledged at December 31, 2003 under the repurchase agreements. These securities are under the Company's control. In addition, the Bank has a line of credit of $10 million from another bank all of which was available as of December 31, 2003. There were no short-term borrowings outstanding at December 31, 2002.

10. Long-term Debt

On June 15, 2000, the Company issued $5 million of 11% Trust Capital Securities to Commerce Bancorp, Inc. through Trust I, a Delaware business trust subsidiary. The Trust Capital Securities evidence a preferred ownership interest in the Trust, of which the Company owns 100% of the common equity. The proceeds from the issuance of the Trust Capital Securities were invested in substantially similar Junior Subordinated Debt of the Company. The Company unconditionally guarantees the Trust Capital Securities. Interest on the debt is payable quarterly in arrears on March 31, June 30, September 30, and December 31 of each year. The Trust Capital Securities are scheduled to mature on June 15, 2030. The Trust Capital Securities may be redeemed in whole or in part at the option of the Company on or after June 15, 2010 at 105.50% of the principal plus accrued interest, if any. The redemption price declines by 0.55% on June 15 of each year from 2011 through 2020 at which time the securities may be redeemed at 100% of the principal plus accrued interest, if any, to the date fixed for redemption, subject to certain conditions. All $5 million of the Trust Capital Securities qualified as Tier 1 capital for regulatory capital purposes.

On September 28, 2001, the Company issued $8 million of 10% Trust Capital Securities to Commerce Bancorp, Inc. through Trust II, a Delaware business trust subsidiary. The issuance of the Trust Capital Securities has similar properties as the Trust I. The Trust Capital Securities evidence a preferred ownership interest in the Trust II of which the Company owns 100% of the common equity. The proceeds from the issuance of the Trust Capital Securities were invested in substantially similar Junior Subordinated Debt of the Company. The Company unconditionally guarantees the Trust Capital Securities. Interest on the debt is payable quarterly with similar terms as in the Trust I. The Trust Capital Securities are scheduled to mature on September 28, 2031. The Trust Capital Securities may be redeemed in whole or in part at the option of the Company on or after September 28, 2011 at 105.00% of the principal plus accrued interest, if any. The redemption price declines by 0.50% on September 28 of each year from 2012 through 2021 at which time the securities may be redeemed at 100% of the principal plus accrued interest, if any, to the date fixed for redemption, subject to certain conditions. All $8 million of the Trust Capital Securities qualified as Tier 1 capital for regulatory capital purposes.

11. Income Taxes

A reconciliation of the provision for income taxes and the amount that would have been provided at statutory rates is as follows:

	Year Ended December 31,		
(in thousands)	**2003**	2002	2001
Provision at statutory rate on pre-tax income	**$3,289**	$2,905	$2,271
Tax-exempt income on loans and investments	**(218)**	(76)	(73)
Other	**47**	42	34
	$3,118	$2,871	$2,232

The components of income tax expense are as follows:

	Year Ended December 31,		
(in thousands)	**2003**	2002	2001
Current	**$2,833**	$2,803	$2,483
Deferred	**285**	68	(251)
	$3,118	$2,871	$2,232

The components of the net deferred tax assets were as follows:

	December 31,	
(in thousands)	**2003**	2002
Deferred tax assets:		
Allowance for loan losses	**$2,042**	$1,749
Other	**59**	41
Total deferred tax assets	**$2,101**	$1,790
Deferred tax liabilities:		
Premises and equipment	**(1,178)**	(583)
Unrealized gains on securities	**(283)**	(783)
Prepaid expenses	**(84)**	(83)
Total deferred tax liabilities	**(1,545)**	(1,449)
Net deferred tax assets	**$ 556**	$ 341

Income taxes of $299,000, $0 and $18,000 were recognized on net securities gains in 2003, 2002, and 2001 respectively. During 2003, 2002 and 2001, the Company received a deduction on its federal income tax return totalling $178,000, $378,000, and $78,000, respectively for the exercise of non-qualified stock options and disqualified dispositions of employee stock from options exercised.

12. Stockholders' Equity

At December 31, 2003, Commerce Bancorp, Inc., owned 40,000 shares of the Company's Series A $10 par value noncumulative nonvoting preferred stock and warrants that entitle the holder to purchase 143,666 shares (adjusted for common stock dividends) of the Company's common stock, exercisable at $6.95 per share (adjusted for common stock dividends), in the event of a "change in control" (as defined in the Warrant Agreement). Such warrants are fully transferable and expire on October 7, 2008. None of these warrants were exercised during 2003 or 2002. The preferred stock is redeemable at the option of the Company at the price of $25 per share plus any unpaid dividends. Dividends on the preferred stock are payable quarterly at a rate of $2 per share per annum.

The Company has implemented a dividend reinvestment and stock purchase plan. Holders of common stock may participate in the plan in which reinvested dividends and voluntary cash payments of up to $5,000 per quarter (subject to change) may be reinvested in additional common shares at a 3% discount (subject to change) from the current market price. Employees who have been continuously employed for at least one year are also eligible to participate in the plan under the same terms as listed above for shareholders. A total of 17,060 and 22,173 common shares were issued pursuant to this plan in 2003 and 2002, respectively. At December 31, 2003, the Company had reserved approximately 430,000 common shares to be issued in connection with the plan.

On January 30, 2002, the Board of Directors declared a 5% common stock dividend payable on February 25, 2002, to stockholders of record on February 11, 2002. Payment of the stock dividend resulted in the issuance of approximately 89,000 additional common shares.

On January 24, 2003, the Board of Directors declared a 5% common stock dividend payable on February 24, 2003, to stockholders of record on February 7, 2003. Payment of the stock dividend resulted in the issuance of approximately 101,000 additional common shares.

On January 23, 2004, the Board of Directors declared a 5% common stock dividend payable on February 24, 2004, to stockholders of record on February 6, 2004. Payment of the stock dividend resulted in the issuance of approximately 109,000 additional common shares.

All common stock and per share data included in these financial statements have been restated for these stock dividends.

13. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share.

	For the Year Ended December 31,								
	2003			2002			2001		
(in thousands except per share amounts)	**Income**	**Shares**	**Per Share Amount**	Income	Shares	Per Share Amount	Income	Shares	Per Share Amount
Basic earnings per share:									
Net income	**$6,557**			$5,674			$4,448		
Preferred stock dividends	**(80)**			(80)			(80)		
Income available to common stockholders	**6,477**	**2,253**	**$2.88**	5,594	2,166	$2.58	4,368	2,043	$2.14
Effect of dilutive securities:									
Stock options		**165**			198			204	
Diluted earnings per share:									
Income available to common stockholders plus assumed conversions	**$6,477**	**2,418**	**$2.68**	$5,594	2,364	$2.37	$4,368	2,247	$1.94

All options outstanding were included in the computation of diluted EPS for the year ended December 31, 2003, and year ended December 31, 2002 because the options' exercise price was lower than the average market price of the common shares.

Options to purchase 91,742 shares of common stock at $31.10, which were outstanding during 2001, were not included in the computation of diluted EPS for the year ended December 31, 2001 because the options' exercise price was greater than the average market price of the common shares.

14. Stock Option Plans

The 1996 Employee Stock Option Plan covers 527,369 authorized shares of common stock reserved for issuance upon exercise of options granted or available for grant to officers and key employees and will expire on December 31, 2005. The Plan provides that the option price of qualified incentive stock options will be fixed by the Board of Directors, but will not be less than 100% of the fair market value of the stock at the date of grant. In addition, the Plan provides that the option price of nonqualified stock options (NQSO's) also will be fixed by the Board of Directors, however for NQSO's the option price may be less than 100% of the fair market value of the stock at the date of grant. Options granted are exercisable one year after the date of grant, subject to certain vesting provisions, and expire ten years after the date of grant.

In 2000, the Company's shareholders approved the adoption of the 2001 Directors' Stock Option Plan. The Plan commenced January 1, 2001 and replaced the 1990 Directors' Stock Option Plan, which expired December 31, 2000. The Plan covers 121,550 authorized shares of common stock reserved for issuance upon exercise of options granted or available for grant to directors and will expire on December 31, 2010. Under the Company's Directors' Stock Option Plan, each Director of the Company who is not regularly employed on a salaried basis by the Company may be entitled to an option to acquire shares, as determined by the Board of Directors, of the Company's common stock during each year in which the Director serves on the Board. The Plan provides that the option price will be fixed by the Board of Directors, but will not be less than 100% of the fair market value of the stock on the date of the grant. Options granted are exercisable from the earlier of (1) one year after the date of the option grant, or (2) the date of a change in control of the Bank.

The Company has adopted the disclosure-only provisions of Standards of Financial Accounting Standards (SFAS) No. 123 "Accounting for Stock-Based Compensation." Accordingly, no compensation costs have been recognized for options granted in 2003, 2002, or 2001.

Stock options transactions under the Plans were as follows:

	Year Ended December 31,					
	2003		2002		2001	
	Options	**Weighted Avg. Exercise Price**	Options	Weighted Avg. Exercise Price	Options	Weighted Avg. Exercise Price
Outstanding at beginning of year	**442,494**	**$18.81**	577,737	$17.83	507,071	$14.83
Granted	**93,720**	**35.96**	14,555	34.69	104,602	30.30
Exercised	**(53,289)**	**12.13**	(123,982)	14.03	(26,528)	8.11
Forfeited	**(8,791)**	**32.92**	(25,816)	29.13	(7,408)	22.89
Outstanding at end of year	**474,134**	**$22.67**	442,494	$18.81	577,737	$17.83
Exercisable at December 31	**367,393**	**$19.15**				
Options available for grant at December 31	**185,180**					
Weighted-average fair value of options granted during the year		**$12.54**		$17.94		$17.73

Exercise prices for options outstanding as of December 31, 2003 are presented in the following table.

	As of December 31, 2003				
	Options Outstanding	Weighted Avg. Exercise Price	Weighted Avg. Contractual Life	Options Exercisable	Weighted Avg. Exercise Price
Options with exercise prices ranging from $4.18 to $15.00	128,685	$ 9.35	2.6 Years	128,685	$ 9.35
Options with exercise prices ranging from $15.01 to $25.00	178,205	21.70	5.7 Years	172,882	21.63
Options with exercise prices ranging from $25.01 to $36.05	167,244	33.93	9.1 Years	65,826	31.76
Total options outstanding with exercise prices ranging from $4.18 to $36.05	474,134	$22.67	6.0 Years	367,393	$19.15

15. Regulatory Matters

Regulatory authorities restrict the amount of cash dividends the Bank can declare without prior regulatory approval. Presently, the Bank cannot declare a cash dividend in excess of its accumulated retained earnings.

The Company and the Bank are subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2003, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2003, the most recent notification from the Office of the Comptroller of the Currency categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the Bank's category.

The following table presents the risk-based and leverage capital amounts and ratios at December 31, 2003 and 2002 for the Company and the Bank.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
(dollars in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
Company						
As of December 31, 2003						
Risked based capital ratios:						
Total capital	**$68,191**	**10.49%**	**Ø $ 52,000**	**Ø 8.0%**	**Ø N/A**	**N/A**
Tier 1 capital	**62,184**	**9.57**	**Ø 26,000**	**Ø 4.0**	**Ø N/A**	**N/A**
Leverage ratio	**62,184**	**6.19**	**Ø 40,198**	**Ø 4.0**	**Ø N/A**	**N/A**
Bank						
As of December 31, 2003						
Risked based capital ratios:						
Total capital	**$67,714**	**10.42%**	**Ø $ 51,992**	**Ø 8.0%**	**Ø $64,990**	**Ø10.0%**
Tier 1 capital	**61,707**	**9.49**	**Ø 25,996**	**Ø 4.0**	**Ø 38,994**	**Ø 6.0**
Leverage ratio	**61,707**	**6.14**	**Ø 40,173**	**Ø 4.0**	**Ø 50,216**	**Ø 5.0**
Company						
As of December 31, 2002						
Risked based capital ratios:						
Total capital	$59,438	12.22%	Ø $ 38,907	Ø 8.0%	Ø N/A	N/A
Tier 1 capital	54,292	11.16	Ø 19,454	Ø 4.0	Ø N/A	N/A
Leverage ratio	54,292	7.00	Ø 31,012	Ø 4.0	Ø N/A	N/A
Bank						
As of December 31, 2002						
Risked based capital ratios:						
Total capital	$59,160	12.17%	Ø $ 38,897	Ø 8.0%	Ø $48,622	Ø10.0%
Tier 1 capital	54,014	11.11	Ø 19,449	Ø 4.0	Ø 29,173	Ø 6.0
Leverage ratio	54,014	6.97	Ø 30,988	Ø 4.0	Ø 38,735	Ø 5.0

16. Employee Benefit Plan

The Company has established a 401(k) Retirement Savings Plan for all of its employees who meet eligibility requirements. Employees may contribute up to 15% of their salary to the Plan. The Company will provide a discretionary matching contribution for up to 6% of each employee's salary. For 2003, 2002, and 2001, the Company's matching contribution was established at 25% of the employees' salary deferral. The amount charged to expense was $96,000, $98,000, and $84,000 in 2003, 2002, and 2001, respectively.

17. Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income are components of comprehensive income.

The only comprehensive income item that the Company presently has is unrealized gains (losses) on securities available for sale. The federal income taxes allocated to the unrealized gains (losses) are presented in the table below. The reclassification adjustments included in comprehensive income are also presented.

	Year Ended December 31,		
(in thousands)	**2003**	2002	2001
Unrealized holding gains (losses) arising during the year	**$ (831)**	$2,471	$ 908
Less reclassification adjustment for gains (losses) included in net income	**640**	0	52
Net unrealized gains (losses)	**(1,471)**	2,471	856
Tax (expense) benefit	**500**	(840)	(291)
Net of tax amount	**$ (971)**	$1,631	$ 565

18. Commitments and Contingencies

The Company has entered into an agreement to purchase the land located at the corner of Friendship Road and TecPort Drive in Swatara Township, Dauphin County, Pennsylvania. The Company plans to construct a Headquarters/Operations Facility on this property to be opened in 2005.

In January 2004, the Company entered into an agreement for naming rights to Commerce Bank Park (formerly known as Riverside Stadium) located on Harrisburg City Island, Harrisburg, Pennsylvania. Commerce Bank Park is home of the Harrisburg Senators, a AA team affiliated with Major League Baseball. The term of the naming rights agreement is 15 years with a total obligation of $3.5 million spread over the term.

In addition, the Company is also subject to certain routine legal proceedings and claims arising in the ordinary course of business. It is management's opinion that the ultimate resolution of these claims will not have a material adverse effect on the Company's financial position and results of operations.

19. Related Party Transactions

Commerce Bancorp, Inc. (an 8.4% shareholder of common stock and 100% shareholder of Series A preferred stock of the Company), through a subsidiary (Commerce Bank, N.A., a national bank located in Cherry Hill, New Jersey), provides various services to the Company. These services include maintenance to the branch LAN network, proof and encoding services, deposit account statement rendering, ATM/VISA card processing, data processing, and advertising support. The Company paid approximately $1.4 million, $1.2 million, and $622,000 for services provided by Commerce Bancorp, Inc. during 2003, 2002, and 2001, respectively. Insurance premiums and commissions, which are paid to a subsidiary of Commerce Bancorp, Inc., are included in the total amount paid. The Company routinely sells loan participations to Commerce Bank, N.A. and at December 31, 2003 and 2002, approximately $2.6 million and $8.6 million, respectively, of these participations were outstanding.

A federal funds line of credit was established with Commerce Bank N.A. in the amount of $10.0 million, which could be drawn upon if needed. The balance at December 31, 2003 and 2002 on this line was $0.

The Company has engaged in certain transactions with entities, which would be considered related parties. Payments for goods and services, including legal services, to these related parties totaled $271,000, $557,000 and $547,000, in 2003, 2002 and 2001, respectively. Management believes disbursements made to related parties were substantially equivalent to those that would have been paid to unaffiliated companies for similar goods and services.

20. Fair Value of Financial Instruments

FASB Statement No. 107, "Disclosures about Fair Value of Financial Instruments" (FAS 107), requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practical to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. These techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows.

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Company could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective year ends, and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each year-end.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The Company, in estimating its fair value disclosures for financial instruments, used the following methods and assumptions:

Cash and cash equivalents

The carrying amounts reported approximate those assets' fair value.

Securities

Fair values of securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Loans Receivable

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans receivable were estimated using discounted cash flow analysis, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loans with significant collectibility concerns were fair valued on a loan-by-loan basis utilizing a discounted cash flow method or the fair market value of the underlying collateral.

Accrued Interest Receivable and Payable

The carrying amount of accrued interest receivable and payable approximate their fair values.

Deposit Liabilities

The fair values disclosed for demand deposits (e.g., interest-bearing and noninterest-bearing checking, passbook 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). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates of deposit to a schedule of aggregated expected monthly maturities on time deposits.

Short-term Borrowings

The carrying amounts reported approximate those liabilities' fair value.

Long-term Debt

The fair values for long-term debt were estimated using the interest rate currently available from the related party that holds the existing debt.

Off-balance Sheet Instruments

Fair values for the Company's off-balance sheet instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

The carrying amounts and fair values of the Company's financial instruments as of December 31 are presented in the following table.

	2003		2002	
(in thousands)	**Carrying Amount**	**Fair Value**	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	**$ 37,715**	**$ 37,715**	$ 75,450	$ 75,450
Securities	**475,263**	**476,968**	303,061	306,472
Loans, net (including loans held for sale)	**479,101**	**496,026**	374,249	393,618
Restricted investments in bank stock	**5,227**	**5,227**	2,045	2,045
Accrued interest receivable	**4,998**	**4,998**	3,675	3,675
Financial liabilities:				
Deposits	**$906,527**	**$908,618**	$726,955	$726,070
Long-term debt	**13,000**	**15,610**	13,000	15,231
Short-term borrowings	**79,000**	**79,000**	0	0
Accrued interest payable	**470**	**470**	832	832
Off-balance sheet instruments:				
Standby letters of credit	**$ 0**	**$ 0**	$ 0	$ 0
Commitments to extend credit	**0**	**0**	0	0

21. Quarterly Financial Data (unaudited)

The following represents summarized unaudited quarterly financial data of the Company which in the opinion of management, reflects adjustments (comprising only normal recurring accruals) necessary for fair presentation (in thousands, except per share amounts):

	Three Months Ended			
	December 31	September 30	June 30	March 31
2003				
Interest income	**$12,798**	**$10,839**	**$11,127**	**$10,778**
Interest expense	**2,857**	**2,689**	**2,932**	**3,174**
Net interest income	**9,941**	**8,150**	**8,195**	**7,604**
Provision for loan losses	**495**	**350**	**525**	**325**
Gains on sales of investment securities	**592**	**288**	**0**	**0**
Provision for federal income taxes	**813**	**710**	**801**	**794**
Net income	**1,725**	**1,526**	**1,658**	**1,648**
Net income per share:				
Basic	**$ 0.75**	**$ 0.67**	**$ 0.73**	**$ 0.73**
Diluted	**0.69**	**0.62**	**0.68**	**0.68**
2002				
Interest income	$10,992	$10,788	$10,342	$9,873
Interest expense	3,505	3,615	3,599	3,575
Net interest income	7,487	7,173	6,743	6,298
Provision for loan losses	345	375	280	435
Gains on sales of investment securities	0	0	0	0
Provision for federal income taxes	799	741	682	649
Net income	1,570	1,467	1,347	1,290
Net income per share:				
Basic	$ 0.70	$ 0.65	$ 0.62	$ 0.61
Diluted	0.65	0.60	0.55	0.54

22. Condensed Financial Statements of Parent Company

Balance Sheets

(in thousands)	December 31, 2003	December 31, 2002
ASSETS		
Cash	**$ 518**	$ 252
Investment in subsidiaries:		
Banking subsidiary	**62,256**	55,534
Non-banking subsidiaries	**600**	600
Other assets	**107**	128
Total Assets	**$63,481**	$56,514
LIABILITIES		
Long-term debt	**$13,000**	$13,000
Other liabilities	**757**	702
Total liabilities	**13,757**	13,702
STOCKHOLDERS' EQUITY		
Preferred stock	**400**	400
Common stock	**2,292**	2,117
Surplus	**38,725**	31,909
Retained earnings	**7,758**	6,866
Accumulated other comprehensive loss	**549**	1,520
Total stockholders' equity	**49,724**	42,812
Total Liabilities & Stockholders' Equity	**$63,481**	$56,514

Statements of Income

(in thousands)	Year Ended December 31, 2003	2002	2001
Income:			
Dividends from bank subsidiary	**$1,396**	$1,226	$ 794
Interest income	**62**	62	32
	1,458	1,288	826
Expenses:			
Interest expense	**1,418**	1,416	793
Other	**349**	258	213
	1,767	1,674	1,006
Income (loss) before income (taxes) benefit and equity in undistributed net income of subsidiaries	**(309)**	(386)	(180)
Income (taxes) benefit	**580**	548	331
	271	162	151
Equity in undistributed net income of bank subsidiary	**6,286**	5,512	4,297
Net income	**$6,557**	$5,674	$4,448

Notes to Consolidated Financial Statements

Statements of Cash Flows

(in thousands)	Year Ended December 31, 2003	2002	2001
Operating Activities:			
Net Income	**$6,557**	$5,674	$4,448
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of financing costs	**6**	6	10
Increase in other liabilities	**55**	30	385
Equity in undistributed net income of bank subsidiary	**(6,286)**	(5,512)	(4,297)
Net cash provided by operating activities	**332**	198	546
Investing Activities:			
Investment in bank subsidiary	**(1,210)**	(2,610)	(8,786)
Investment in nonbank subsidiaries	**0**	0	(400)
Net cash (used) by investing activities	**(1,210)**	(2,610)	(9,186)
Financing Activities:			
Proceeds from common stock options exercised	**556**	1,738	217
Proceeds from issuance of long term debt	**0**	0	8,000
Proceeds from issuance of common stock under stock purchase plan	**677**	868	698
Costs of issuing long term debt	**0**	0	(53)
Cash dividends on preferred stock and cash in lieu of fractional shares	**(89)**	(90)	(86)
Net cash provided by financing activities	**1,144**	2,516	8,776
Increase in cash and cash equivalents	**266**	104	136
Cash and cash equivalents at beginning of the year	**252**	148	12
Cash and cash equivalents at end of year	**$ 518**	$ 252	$ 148

Independent Auditor's Report

To the Board of Directors
Pennsylvania Commerce Bancorp, Inc.
Camp Hill, Pennsylvania

We have audited the accompanying consolidated balance sheets of Pennsylvania Commerce Bancorp, Inc. and its subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

Beard Miller Company LLP

Harrisburg, Pennsylvania
January 30, 2004

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Corporate Information

Headquarters

Pennsylvania Commerce Bancorp, Inc.
100 Senate Avenue
Camp Hill, PA 17011

Annual Shareholders' Meeting

Pennsylvania Commerce Bancorp, Inc.'s annual shareholders' meeting will be held on Friday, May 21, 2004 at 9:00 am at the following location:

Radisson Penn Harris Hotel
1150 Camp Hill Bypass
Camp Hill, PA 17011

Contacts

Analysts, portfolio managers and others seeking financial information about Pennsylvania Commerce Bancorp, Inc. should contact:

Mark A. Zody
Chief Financial Officer
at (717) 975-5630

News media representatives and others seeking general corporate information should contact:

Jason Kirsch
Public Relations Manager
at (717) 975-5630

Shareholders seeking assistance with stock records should contact:

Sherry Richart
Shareholder Relations
at (717) 972-2879

Dividend Reinvestment and Stock Purchase Plan

Pennsylvania Commerce Bancorp, Inc. offers its shareholders a convenient plan to increase their investment in the Company. Through the Dividend Reinvestment and Stock Purchase Plan, holders of common stock may have their dividends and voluntary cash payments of up to $5,000 per month (subject to change) reinvested in additional common shares at a 3% discount (subject to change) from the market price and without brokerage fees, commissions or service charges. Shareholders not enrolled in this plan, as well as brokers and custodians who hold stock for clients, may receive a plan prospectus and enrollment card by contacting Sherry Richart at (717) 972-2879.

Annual Report and Form 10-K

Additional copies of Pennsylvania Commerce Bancorp, Inc.'s Annual Report and Form 10-K are available without charge by writing:

Pennsylvania Commerce Bancorp, Inc.
Shareholder Relations
100 Senate Avenue
Camp Hill, PA 17011

NASDAQ Symbol

Shares of Pennsylvania Commerce Bancorp, Inc. common stock are traded nationally under the symbol COBH in the Over-The-Counter Small Cap Market and are listed in NASDAQ Quotations.

Common Stock Prices

The following table sets forth the prices for which common stock has traded during the last two (2) fiscal years on the NASDAQ Small Cap Market. The prices per share have been adjusted to reflect common stock dividends of 5% with record dates of February 6, 2004 and February 7, 2003. As of December 31, 2003, there were approximately 630 holders of record of the Company's common stock.

	Sales Price	
Quarter Ended:	High	Low
March 31, 2003	$ 38.10	$ 32.38
June 30, 2003	37.83	33.50
September 30, 2003	39.37	35.12
December 31, 2003	48.57	39.49
March 31, 2002	$ 38.10	$ 32.18
June 30, 2002	48.98	37.46
September 30, 2002	43.81	33.79
December 31, 2002	40.02	31.42

Transfer and Dividend Paying Agent/Registrar

Registrar and Transfer Company
10 Commerce Drive
Cranford, NJ 07016-3572

Pennsylvania Commerce Bancorp

1-888-937-0004
commercepc.com