CENTRAL PACIFIC FINANCIAL CORP
Form 10-Q
May 09, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

(Mark One)

T QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2008

or

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

Commission file number 0-10777

CENTRAL PACIFIC FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Hawaii (State or other jurisdiction of incorporation or organization)	99-0212597 (I.R.S. Employer Identification No.)

220 South King Street, Honolulu, Hawaii 96813
(Address of principal executive offices) (Zip Code)

(808) 544-0500
(Registrant's telephone number, including area code)

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

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

Large accelerated filer T Accelerated filer £ Non-accelerated filer £

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

The number of shares outstanding of registrant's common stock, par value $.01 per share, on May 1, 2008 was 28,709,274 shares.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Forward-Looking Statements

This document may contain forward-looking statements concerning projections of revenues, income, earnings per share, capital expenditures, dividends, capital structure, or other financial items, concerning plans and objectives of management for future operations, concerning future economic performance, or concerning any of the assumptions underlying or relating to any of the foregoing. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts, and may include the words “believes”, “plans”, “intends”, “expects”, “anticipate “forecasts” or words of similar meaning. While we believe that our forward-looking statements and the assumptions underlying them are reasonably based, such statements and assumptions are by their nature subject to risks and uncertainties, and thus could later prove to be inaccurate or incorrect. Accordingly, actual results could materially differ from projections for a variety of reasons, to include, but not limited to: the impact of local, national, and international economies and events (including natural disasters such as wildfires, tsunamis and earthquakes) on the Company’s business and operations and on tourism, the military, and other major industries operating within the Hawaii market and any other markets in which the Company does business; the impact of legislation affecting the banking industry; the impact of competitive products, services, pricing, and other competitive forces; movements in interest rates; loan delinquency rates and changes in asset quality; adverse conditions in the public debt market, the stock market or other capital markets, including any adverse changes in the price of the Company's stock; and a general deterioration in economic conditions, including the continued slowing of the real estate market. For further information on factors that could cause actual results to materially differ from projections, please see the Company’s publicly available Securities and Exchange Commission filings, including the Company’s Form 10-K for the last fiscal year. The Company does not update any of its forward-looking statements.

Item 1. Financial Statements

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(Dollars in thousands)		March 31, 2008		December 31, 2007
Assets				
Cash and due from banks	$	84,462	$	79,088
Interest-bearing deposits in other banks		106		241
Federal funds sold		-		2,800
Investment securities:				
Held to maturity, at amortized cost (fair value of $27,098 at March 31, 2008 and $46,077 at December 31, 2007)		26,915		46,124
Available for sale, at fair value		852,655		835,130
Total investment securities		879,570		881,254
Loans held for sale		97,743		37,572
Loans and leases		4,176,596		4,141,705
Less allowance for loan and lease losses		72,108		92,049
Net loans and leases		4,104,488		4,049,656
Premises and equipment, net		83,504		82,841
Accrued interest receivable		25,541		26,041
Investment in unconsolidated subsidiaries		16,471		17,404
Other real estate		2,000		-
Goodwill		244,702		244,702
Core deposit premium		28,082		28,750
Mortgage servicing rights		11,536		11,222
Bank-owned life insurance		132,477		131,454
Federal Home Loan Bank stock		48,797		48,797
Other assets		40,558		38,564
Total assets	$	5,800,037	$	5,680,386
Liabilities and Shareholders' Equity				
Deposits:				
Noninterest-bearing demand	$	632,157	$	665,034
Interest-bearing demand		457,742		461,175
Savings and money market		1,112,312		1,178,855
Time		1,577,810		1,697,655
Total deposits		3,780,021		4,002,719
Short-term borrowings		368,375		16,000
Long-term debt		915,514		916,019
Minority interest		13,098		13,104
Other liabilities		48,366		58,141

Total liabilities		5,125,374		5,005,983
Shareholders' equity:				
Preferred stock, no par value, authorized 1,000,000 shares, none issued		-		-
Common stock, no par value, authorized 100,000,000 shares, issued and outstanding 28,707,985 shares at March 31, 2008 and 28,756,647 shares at December 31, 2007		402,844		403,304
Surplus		54,487		54,669
Retained earnings		216,755		222,644
Accumulated other comprehensive income (loss)		577		(6,214)
Total shareholders' equity		674,663		674,403
Total liabilities and shareholders' equity	$	5,800,037	$	5,680,386

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(Amounts in thousands, except per share data)	Three Months Ended March 31, 2008	2007
Interest income:		
Interest and fees on loans and leases	$ 70,294	$ 76,166
Interest and dividends on investment securities:		
Taxable interest	9,271	8,712
Tax-exempt interest	1,389	1,363
Dividends	24	33
Interest on deposits in other banks	4	35
Interest on Federal funds sold and securities purchased under agreements to resell	21	10
Dividends on Federal Home Loan Bank stock	122	98
Total interest income	81,125	86,417
Interest expense:		
Interest on deposits:		
Demand	137	138
Savings and money market	3,785	6,284
Time	14,729	15,835
Interest on short-term borrowings	1,923	505
Interest on long-term debt	9,694	9,968
Total interest expense	30,268	32,730
Net interest income	50,857	53,687
Provision for loan and lease losses	34,272	2,600
Net interest income after provision for loan and lease losses	16,585	51,087
Other operating income:		
Service charges on deposit accounts	3,543	3,444
Other service charges and fees	3,415	3,357
Income from fiduciary activities	1,005	761
Equity in earnings of unconsolidated subsidiaries	283	257
Fees on foreign exchange	194	221
Loan placement fees	153	259
Gains on sales of loans	1,798	1,367
Income from bank-owned life insurance	1,870	1,031
Other	2,018	455
Total other operating income	14,279	11,152
Other operating expense:		
Salaries and employee benefits	17,364	16,406
Net occupancy	2,853	2,504
Equipment	1,395	1,230
Amortization of core deposit premium	668	685
Amortization of mortgage servicing rights	501	510
Communication expense	1,085	1,148

Legal and professional services		2,413		2,327
Computer software expense		863		799
Advertising expense		682		623
Foreclosed asset expense		2,590		-
Other		1,046		4,244
Total other operating expense		31,460		30,476
Income (loss) before income taxes		(596)		31,763
Income taxes		(2,254)		11,628
Net income	$	1,658	$	20,135
Per share data:				
Basic earnings per share	$	0.06	$	0.66
Diluted earnings per share		0.06		0.65
Cash dividends declared		0.25		0.24
Shares used in computation:				
Basic shares		28,686		30,699
Diluted shares		28,801		30,988

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(Dollars in thousands)	Three Months Ended March 31, 2008	2007
Cash flows from operating activities:		
Net income	$ 1,658	$ 20,135
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and lease losses	34,272	2,600
Depreciation and amortization	1,864	1,742
Amortization of intangible assets	1,169	1,195
Net amortization of investment securities	462	564
Share-based compensation	612	1,262
Deferred income tax expense	6,776	4,572
Net gain on sale of loans	(1,798)	(1,367)
Proceeds from sales of loans held for sale	353,790	195,552
Originations of loans held for sale	(352,083)	(209,124)
Tax benefits from share-based compensation	(40)	-
Equity in earnings of unconsolidated subsidiaries	(283)	(257)
Increase in cash surrender value of bank-owned life insurance	(1,870)	(1,026)
Net change in other assets and liabilities	(18,274)	(6,304)
Net cash provided by operating activities	26,255	9,544
Cash flows from investing activities:		
Proceeds from maturities of and calls on investment securities held to maturity	19,187	12,386
Proceeds from maturities of and calls on investment securities available for sale	201,684	241,987
Purchases of investment securities available for sale	(213,065)	(221,038)
Net loan originations	(151,089)	(62,605)
Proceeds from bank-owned life insurance	843	-
Purchases of premises and equipment	(2,527)	(1,417)
Distributions from unconsolidated subsidiaries	620	527
Contributions to unconsolidated subsidiaries	-	(167)
Net cash used in investing activities	(144,347)	(30,327)
Cash flows from financing activities:		
Net increase (decrease) in deposits	(222,698)	1,138
Proceeds from long-term debt	30,000	100,000
Repayments of long-term debt	(30,365)	(35,344)
Net increase (decrease) in short-term borrowings	352,375	(54,269)
Cash dividends paid	(7,190)	(7,380)
Tax benefits from share-based compensation	40	-
Repurchases of common stock	(1,825)	(1,972)
Proceeds from issuance of common stock	194	95
Proceeds from stock option exercises	-	984
Net cash provided by financing activities	120,531	3,252
Net increase (decrease) in cash and cash equivalents	2,439	(17,531)
Cash and cash equivalents at beginning of period	82,129	135,648

Cash and cash equivalents at end of period	$	84,568	$	118,117
Supplemental disclosure of cash flow information:				
Cash paid during the period for:				
Interest	$	31,190	$	31,051
Income taxes		1,315		1,160
Cash received during the period for:				
Income taxes				
Supplemental disclosure of noncash investing and financing activities:				
Net change in common stock held by directors' deferred compensation plan	$	20	$	11
Reclassification of loans to other real estate		2,000		-
Transfer of loans to loans held for sale		60,080		-

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Central Pacific Financial Corp. (referred to herein as "the Company," "we," "us," or "our") have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. These interim condensed consolidated financial statements and notes should be read in conjunction with the Company's consolidated financial statements and notes thereto filed on Form 10-K for the fiscal year ended December 31, 2007. In the opinion of management, all adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

2. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). The standard defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America and expands disclosure about fair value measurements. The pronouncement applies under other accounting standards that require or permit fair value measurements. Accordingly, the statement does not require any new fair value measurement.

In February 2008, the FASB amended SFAS 157 through the issuance of FSP FAS 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13" and FSP FAS 157-2, "Effective Date of FASB Statement No. 157." FSP FAS 157-1 is effective upon the initial adoption of SFAS 157 and amends SFAS 157 to exclude from its scope certain accounting pronouncements that address fair value measurements associated with leases. FSP FAS 157-2 is effective upon issuance and delays the effective date of SFAS 157 to fiscal years beginning after November 15, 2008, for nonfinancial assets and nonfinancial liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). We adopted the provisions of SFAS 157 for financial assets and liabilities beginning January 1, 2008 and such adoption did not have a material impact on our consolidated financial statements (see Note 12). As permitted under SFAS 157, we plan to adopt the provisions of SFAS 157 for nonfinancial assets and nonfinancial liabilities that are not recognized or disclosed at fair value in our financial statements on a recurring basis effective January 1, 2009. We are evaluating the impact of the adoption of SFAS 157 for nonfinancial assets and nonfinancial liabilities on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We adopted the provisions of SFAS 159 beginning January 1, 2008 and such adoption did not have a material impact on our consolidated financial statements.

In March 2007, the FASB ratified EITF No. 06-10 "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements" ("EITF 06-10"). EITF 06-10 requires that an employer recognize a liability for the postretirement benefit obligation related to a collateral assignment arrangement in accordance with SFAS No. 106 "Employers' Accounting for Postretirement Benefits Other Than Pensions" (if deemed part of a postretirement plan) or Accounting Principles Board Opinion 12 "Omnibus Opinion-1967" (if not part of a plan). The consensus is applicable if, based on the substantive agreement with the employee, the employer has agreed to (a) maintain a life insurance policy during the postretirement period or (b) provide a death benefit. The EITF also reached a consensus that an employer should recognize and measure the associated asset on the basis of the terms of the collateral assignment arrangement. We adopted the provisions of EITF 06-10 beginning January 1, 2008 and such adoption did not have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations" ("SFAS 141(R)"). SFAS 141(R) establishes principles and requirements for how the acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest (minority interest) in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination or a gain from a bargain purchase and determining what information should be disclosed to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141(R) is to be applied prospectively to business combinations for which the acquisition date is on or after fiscal years beginning after December 15, 2008. We are currently assessing the impact of this statement on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51" ("SFAS 160"). SFAS 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. SFAS 160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. SFAS 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. We are evaluating the impact of this new pronouncement on our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement 133" ("SFAS 161"). SFAS 161 enhances required disclosures regarding derivatives and hedging activities, including enhanced disclosures regarding how (a) an entity uses derivative instruments; (b) derivative instruments and related hedged items are accounted for under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities; and (c) derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. Specifically, SFAS 161 requires (1) disclosure of the objectives for using derivative instruments be disclosed in terms of underlying risk and accounting designation; (2) disclosure of the fair values of derivative instruments and their gains and losses in a tabular format; (3) disclosure of information about credit-risk-related contingent features; and (4) cross-reference from the derivative footnote to other footnotes in which derivative-related information is disclosed. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008. We are evaluating the impact of this new pronouncement on our consolidated financial statements.

3. LOANS AND LEASES

Loans, excluding loans held for sale, consisted of the following at the dates indicated:

	March 31, 2008	December 31, 2007
	(Dollars in thousands)	
Commercial, Financial and Agricultural	$ 379,721	$ 385,521
Real Estate:		
Construction	1,196,297	1,226,138
Mortgage-Residential	1,074,721	1,036,779
Mortgage-Commercial	1,282,015	1,243,383
Consumer	202,871	209,166

Leases	53,373	53,303
	4,188,998	4,154,290
Unearned income	(12,402)	(12,585)
Total loans and leases	$ 4,176,596	$ 4,141,705

4. ALLOWANCE FOR LOAN AND LEASE LOSSES

The following table presents the changes in the allowance for loan and lease losses (the "Allowance") for the periods indicated:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
	(Dollars in thousands)	
Balance, beginning of period	$ 92,049	$ 52,280
Provision for loan and lease losses	34,272	2,600
	126,321	54,880
Charge-offs	(54,810)	(4,835)
Recoveries	597	569
Net charge-offs	(54,213)	(4,266)
Balance, end of period	$ 72,108	$ 50,614

The increase in the Allowance during the three months ended March 31, 2008 was primarily due to an increase in the number of loans that were downgraded, as well as an increase in specific reserves on certain impaired loans. As a result of the downturn in the California residential construction market, which began in 2007 and has continued through the first quarter of 2008, some of our borrowers are finding it increasingly difficult to repay amounts due on their outstanding balances as they primarily rely on the proceeds received from the sales of homes to repay their loans. Accordingly, our methodology for determining the adequacy of the Allowance required that these loans be downgraded. We also increased the amount of specific reserves for certain loans with direct exposure to this market. Deterioration of the economy in the United States generally as well as the economies of Hawaii and/or California, and any further deterioration in the California residential construction market or in our borrowers' ability to repay their loans, may require us to increase our Allowance in the future, increase our provision for loan and lease losses and may result in increased net charge-offs.

5. INTANGIBLE ASSETS

The following table presents changes in intangible assets for the three months ended March 31, 2008:

	Core Deposit Premium	Mortgage Servicing Rights
	(Dollars in thousands)	
Balance, beginning of period	$ 28,750	$ 11,222
Additions	-	815
Amortization	(668)	(501)
Balance, end of period	$ 28,082	$ 11,536

The gross carrying value and accumulated amortization related to the core deposit premium and mortgage servicing rights are presented below:

March 31, 2008			December 31, 2007		
Gross Carrying Value	Accumulated Amortization	Net	Gross Carrying Value	Accumulated Amortization	Net

(Dollars in thousands)

Core deposit premium	$	44,642	$	(16,560)	$	28,082	$	44,642	$	(15,892)	$	28,750
Mortgage servicing rights		21,335		(9,799)		11,536		20,520		(9,298)		11,222

Based on the core deposit premium and mortgage servicing rights held as of March 31, 2008, estimated amortization expense for the remainder of fiscal 2008, the next five succeeding fiscal years and all years thereafter are as follows:

	Estimated Amortization Expense	
	Core Deposit Premium	Mortgage Servicing Rights
	(Dollars in thousands)	
2008 (remainder)	$ 2,006	$ 1,276
2009	2,674	1,454
2010	2,674	1,250
2011	2,674	1,068
2012	2,674	916
2013	2,674	788
Thereafter	12,706	4,784
	$ 28,082	$ 11,536

Income generated as the result of new mortgage servicing rights is reported as gains on sales of loans and totaled $0.8 million and $0.3 million for the three months ended March 31, 2008 and 2007, respectively. The fair value of our mortgage servicing rights was $12.0 million and $12.4 million at March 31, 2008 and December 31, 2007, respectively.

6. DERIVATIVES

In January 2008, we entered into a derivative transaction to hedge future cash flows from a portion of our then existing variable rate loan portfolio. Effective January 2008 through January 2013, we will receive payments equal to a fixed interest rate of 6.25% from the counterparty on a notional amount of $400 million. In return, we will pay to the counterparty a floating rate, namely our prime rate, on the same notional amount. The purpose of this derivative transaction is to minimize the risk of fluctuations in interest payments received on our variable rate loan portfolio. The derivative transaction has been designated as a cash flow hedge.

As required by SFAS 133, “Accounting for Derivative Instruments and Hedging Activities”, we measure the derivative at fair value on our consolidated balance sheet. At each reporting period, depending on whether the derivative is in an asset or liability position, we record the derivative in other assets or other liabilities. We record the effective portion of the changes in the fair value of the derivative in accumulated other comprehensive income (loss), net of tax, until earnings are affected by the variability of cash flows of the hedged transaction. We immediately recognize the portion of the gain or loss in the fair value of the derivative that represents hedge ineffectiveness in current period earnings.

At March 31, 2008, the derivative was in an asset position and we recorded the derivative at its fair value of $4.9 million in other assets. At March 31, 2008, we also recorded an unrealized gain of $4.6 million for the effective portion of the change in fair value of the derivative in accumulated other comprehensive income. During the three months ended March 31, 2008, we recognized a gain related to hedge ineffectiveness of $0.3 million.

7. SHARE REPURCHASE

In January 2008, the Company’s board of directors authorized the repurchase and retirement of up to 1,200,000 shares of the Company’s common stock (the “2008 Repurchase Plan”). Repurchases may be made from time to time on the open market or in privately negotiated transactions. During the three months ended March 31, 2008, we repurchased and retired a total of 100,000 shares of common stock for approximately $1.8 million. At March 31, 2008, a total of 1,100,000 shares remained authorized for repurchase under the 2008 Repurchase Plan.

8. SHARE-BASED COMPENSATION

The following table reflects total share-based compensation recognized for the periods indicated:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
	(Dollars in thousands)	
Salaries and employee benefits	$ 612	$ 1,262
Income tax benefit	(245)	(506)
Net share-based compensation effect	$ 367	$ 756

In accordance with SFAS 123R, we are required to base initial share-based compensation expense on the estimated number of awards for which the requisite service and performance is expected to be rendered.

Stock Option Plans

We have adopted stock option plans for the purpose of granting options to purchase the Company's common stock to directors, officers and other key individuals. Option awards are granted with an exercise price equal to the market price of the Company's common stock at the date of grant; those option awards generally vest based on three or five years of continuous service and have 10-year contractual terms. Certain option and share awards provide for accelerated vesting if there is a change in control (as defined in the stock option plans below). We have historically issued new shares of common stock upon exercises of stock options and purchases of restricted awards.

In February 1997, we adopted the 1997 Stock Option Plan ("1997 Plan") basically as a continuance of the 1986 Stock Option Plan. In April 1997, the Company's shareholders approved the 1997 Plan, which provided 2,000,000 shares of the Company's common stock for grants to employees as qualified incentive stock options and to directors as nonqualified stock options.

In September 2004, we adopted and the Company's shareholders approved the 2004 Stock Compensation Plan ("2004 Plan") making available 1,989,224 shares for grants to employees and directors. Upon adoption of the 2004 Plan, all unissued shares from the 1997 Plan were frozen and no new options will be granted under the 1997 Plan. Optionees may exercise outstanding options granted pursuant to the 1997 Plan until the expiration of the respective options in accordance with the original terms of the 1997 Plan. To satisfy share issuances pursuant to the share-based compensation programs, we issue new shares from the 2004 Plan.

The following is a summary of option activity for the Company's stock option plans for the three months ended March 31, 2008:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2008	872,912	$ 27.90
Changes during the period:		
Granted	93,000	18.88
Forfeited	(17,163)	36.43
Outstanding at March 31, 2008	948,749	26.86

We estimate the fair value of stock options granted using the Black-Scholes option pricing formula and a single option award approach. This fair value is then amortized on a straight-line basis over the requisite service periods of the awards, which is generally the vesting period. The fair value of the Company's stock options granted to employees for the three months ended March 31, 2008 and 2007 was estimated using the following weighted-average assumptions:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Expected volatility	32.0%	33.3%
Risk free interest rate	2.8%	4.5%
Expected dividends	5.3%	2.8%
Expected life (in years)	6.5	7.5
Weighted average fair value	$ 3.50	$ 11.40

Restricted Stock Awards

Under the 1997 and 2004 Plans, we awarded restricted stock awards to our non-officer directors and certain senior management personnel. The awards typically vest over a three or five year period. Compensation expense is measured as the market price of the stock awards on the grant date, and is recognized over the specified vesting periods.

The table below presents the activity of restricted stock awards for the three months ended March 31, 2008:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2008	44,620	$ 34.87
Changes during the period:		
Forfeited	(2,500)	36.95
Nonvested at March 31, 2008	42,120	34.74

Performance Shares and Stock Appreciation Rights

In 2005, we established a Long Term Incentive Plan ("LTIP") that covers certain executive and senior management personnel. The LTIP is comprised of three components: performance shares, stock appreciation rights and cash awards.

Performance shares are granted under the 2004 Plan and vest based on achieving both performance and service conditions. Performance conditions require achievement of stated goals including earnings per share, credit quality and efficiency ratio targets. The service condition requires employees to be employed continuously with the Company through March 15, 2008. The fair value of the grant to be recognized over this service period is determined based on the market value of the stock on the grant date, multiplied by the probability of the granted shares being earned. This requires us to assess the expectation over the performance period of the performance targets being achieved as well as to estimate expected pre-vested cancellations.

The table below presents activity of performance shares for the three months ended March 31, 2008:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2008	45,957	$ 34.74
Changes during the period:		
Granted	97,907	18.88
Vested	(45,957)	34.74
Nonvested at March 31, 2008	97,907	18.88

Stock appreciation rights (“SARs”) are granted under the 2004 Plan. These SARs require the employee to achieve the same performance conditions as the performance shares described above as well as to satisfy service conditions that approximate three years from the date of grant. Upon exercise of the SAR, for each SAR exercised, the grantee shall be entitled to receive value equal to the difference between the market value of a share on the date of exercise minus the market value of a share on the date of grant. We shall pay the value owing to the grantee upon exercise in whole shares. No cash will be awarded upon exercise, and no fractional shares will be issued or delivered.

As the SARs plan is a stock-settled SAR, this plan is an equity-classified award under SFAS 123R. As such, the financial and income tax accounting for this type of award is identical to that of a nonqualified stock option plan. Therefore, the grant date fair value is determined at the grant date using the same method as would be used for determining the fair value of a grant of a nonqualified stock option, which has historically been the Black-Scholes formula. Similar to the performance shares addressed above, the amount of compensation cost to be recognized is the fair value of the SAR grant adjusted based on expectations of achieving the performance requirements and also the expected pre-vested cancellations. Compensation costs arising from the SARs will be recognized ratably over the requisite service period.

The fair value of SARs granted to employees were estimated using the Black-Scholes option pricing formula with the following weighted-average assumptions:

	Three Months Ended March 31,	
	2008	2007
Expected volatility	32.0%	31.7%
Risk free interest rate	2.8%	4.5%
Expected dividends	5.3%	2.8%
Expected life (in years)	6.5	6.5
Weighted average fair value	$ 3.50	$ 10.49

The table below presents activity of SARs for the three months ended March 31, 2008:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2008	56,549	$ 35.00

Changes during the period:		
Granted	210,963	18.88
Vested	(22,535)	34.48
Forfeited	(2,426)	35.20
Outstanding at March 31, 2008	242,551	21.03

9. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Components of accumulated other comprehensive income (loss), net of taxes, were as follows:

	March 31, 2008	December 31, 2007
	(Dollars in thousands)	
Unrealized holding gains (losses) on available-for-sale investment securities	$ 6,183	$ (401)
Unrealized holding gains on derivatives	4,564	-
Pension adjustments	(9,784)	(9,973)
Tax effect	(386)	4,160
Accumulated other comprehensive income (loss), net of tax	$ 577	$ (6,214)

Components of comprehensive income for the periods indicated were as follows:

	Three Months Ended March 31, 2008	2007
	(Dollars in thousands)	
Net income	$ 1,658	$ 20,135
Unrealized gain on investment securities, net of taxes	3,945	1,805
Unrealized gain on derivatives, net of taxes	2,735	-
Pension adjustments, net of taxes	111	-
Comprehensive income	$ 8,449	$ 21,940

10. PENSION PLANS

Central Pacific Bank, our bank subsidiary, has a defined benefit retirement plan (the “Pension Plan”) which covers certain eligible employees. The plan was curtailed effective December 31, 2002, and accordingly, plan benefits were fixed as of that date. The following table sets forth the components of net periodic benefit cost for the Pension Plan:

	Three Months Ended March 31, 2008	2007
	(Dollars in thousands)	
Interest cost	$ 451	$ 446
Expected return on assets	(574)	(560)
Amortization of unrecognized loss	186	264
Net periodic cost	$ 63	$ 150

Central Pacific Bank also established Supplemental Executive Retirement Plans (“SERPs”), which provide certain officers of Central Pacific Bank with supplemental retirement benefits. The following table sets forth the components of net periodic benefit cost for the SERPs:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
	(Dollars in thousands)	
Service cost	$ 75	$ 140
Interest cost	138	136
Amortization of unrecognized transition obligation	5	5
Amortization of prior service cost	5	1
Amortization of unrecognized (gain) loss	(8)	5
Net periodic cost	$ 215	$ 287

11. EARNINGS PER SHARE

The following table presents the information used to compute basic and diluted earnings per share for the periods indicated:

(In thousands, except per share data)	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Net income	$ 1,658	$ 20,135
Weighted average shares outstanding - basic	28,686	30,699
Dilutive effect of employee stock options and awards	115	289
Weighted average shares outstanding - diluted	28,801	30,988
Basic earnings per share	$ 0.06	$ 0.66
Diluted earnings per share	$ 0.06	$ 0.65

A total of 812,978 and 28,875 potentially dilutive securities have been excluded from the dilutive share calculation for the three months ended March 31, 2008 and 2007, respectively, as their effect was anti-dilutive.

12. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Effective January 1, 2008, we partially adopted the provisions of SFAS 157. The statement defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements for fair value measurements.

Under SFAS 157, we group our financial assets and liabilities at fair value into three levels based on the markets in which the financial assets and liabilities are traded and the reliability of the assumptions used to determine fair value as follows:

- Level 1 – Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities traded in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of discounted cash flow models and similar techniques that requires the use of significant judgment or estimation.

Under SFAS 157, we base our fair values on the price that we would expect to receive if an asset were sold or pay to transfer a liability in an orderly transaction between market participants at the measurement date. As required under SFAS 157, we maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

We use fair value measurements to record adjustments to certain financial assets and liabilities and to determine fair value disclosures. Available for sale securities and derivatives are recorded at fair value on a recurring basis. From time to time, we may be required to record other financial assets at fair value on a nonrecurring basis such as loans held for sale, impaired loans and mortgage servicing rights. These nonrecurring fair value adjustments typically involve application of the lower of cost or fair value accounting or write-downs of individual assets.

The following table below presents the balances of assets and liabilities measured at fair value on a recurring basis:

	March 31, 2008			
	Level 1	Level 2	Level 3	Total
	(Dollars in thousands)			
Available for sale securities	$ 935	$ 837,045	$ 14,675	$ 852,655
Derivatives	-	5,297	-	5,297
Total	$ 935	$ 842,342	$ 14,675	$ 857,952

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	March 31, 2008 Available For Sale Securities (Dollars in thousands)
Balance at January 1, 2008	$ 14,821
Principal payments received on mortgage revenue bonds	(146)
Balance at March 31, 2008	14,675

For assets measured at fair value on a nonrecurring basis that were recorded at fair value on our balance sheet at March 31, 2008, the following table provides the level of valuation assumptions used to determine the respective fair values:

	March 31, 2008			
	Level 1	Level 2	Level 3	Total
	(Dollars in thousands)			
Loans held for sale (1)	$ -	$ 47,929	$ -	$ 47,929
Impaired loans (1)	-	65,630	-	65,630

(1) Represents carrying value and related write-downs of loans for which adjustments are based on agreed upon purchase prices for the loans or the appraised value of the collateral.

13. SEGMENT INFORMATION

We have three reportable segments: Commercial Real Estate, Hawaii Market and Treasury. The segments reported are consistent with internal functional reporting lines. They are managed separately because each unit has different target markets, technological requirements, marketing strategies and specialized skills. The Commercial Real Estate segment includes construction and real estate development lending in Hawaii, California and Washington. The Hawaii Market segment includes retail branch offices, commercial lending, residential mortgage lending and servicing, indirect auto lending, trust services and retail brokerage services. A full range of deposit and loan products and various other banking services are offered. The Treasury segment is responsible for managing the Company's investment securities portfolio and wholesale funding activities.

The All Others category includes activities such as electronic banking, data processing and management of bank owned properties.

The accounting policies of the segments are consistent with the Company's accounting policies that are described in Note 1 to the consolidated financial statements in the Annual Report on Form 10-K for the year ended December 31, 2007 filed with the Securities and Exchange Commission. The majority of the Company's net income is derived from net interest income. Accordingly, management focuses primarily on net interest income, rather than gross interest income and expense amounts, in evaluating segment profitability.

Intersegment net interest income (expense) was allocated to each segment based upon a funds transfer pricing process that assigns costs of funds to assets and earnings credits to liabilities based on market interest rates that reflect interest rate sensitivity and maturity characteristics. All administrative and overhead expenses are allocated to the segments at cost. Cash, investment securities, loans and their related balances are allocated to the segment responsible for acquisition and maintenance of those assets. Segment assets also include all premises and equipment used directly in segment operations.

Segment profits and assets are provided in the following table for the periods indicated.

	Commercial Real Estate	Hawaii Market	Treasury	All Others	Total
			(Dollars in thousands)		
Three months ended March 31, 2008:					
Net interest income	$ 37,045	$ 17,111	$ (3,299)	$ -	$ 50,857
Intersegment net interest income (expense)	(24,463)	18,398	2,126	3,939	-
Provision for loan losses	(33,300)	(972)	-	-	(34,272)
Other operating income	58	10,958	2,979	284	14,279
Other operating expense	(5,274)	(17,499)	(609)	(8,078)	(31,460)
Administrative and overhead expense allocation	2,683	(9,528)	(91)	6,936	-
Income taxes	8,138	(5,174)	9	(719)	2,254
Net income (loss)	$ (15,113)	$ 13,294	$ 1,115	$ 2,362	$ 1,658
Three months ended March 31, 2007:					
Net interest income	$ 44,183	$ 12,237	$ (2,733)	$ -	$ 53,687
Intersegment net interest income (expense)	(26,714)	19,538	416	6,760	-
Provision for loan losses	-	(2,600)	-	-	(2,600)
Other operating income	14	9,083	1,896	159	11,152
Other operating expense	(1,862)	(17,487)	(649)	(10,478)	(30,476)
Administrative and overhead expense allocation	(1,785)	(7,060)	(84)	8,929	-
Income taxes	(5,065)	(5,019)	422	(1,966)	(11,628)
Net income (loss)	$ 8,771	$ 8,692	$ (732)	$ 3,404	$ 20,135
At March 31, 2008:					
Investment securities	$ -	$ -	$ 879,570	$ -	$ 879,570
Loans and leases (including loans held for sale)	2,275,510	1,998,829	-	-	4,274,339
Other	52,239	209,288	255,433	129,168	646,128
Total assets	$ 2,327,749	$ 2,208,117	$ 1,135,003	$ 129,168	$ 5,800,037
At December 31, 2007:					

Investment securities	$ -	$ -	$ 881,254	$ -	$ 881,254
Loans and leases (including loans held for sale)	2,228,739	1,950,538	-	-	4,179,277
Other	31,891	208,135	244,453	135,376	619,855
Total assets	$ 2,260,630	$ 2,158,673	$ 1,125,707	$ 135,376	$ 5,680,386

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

We are a Hawaii corporation and a bank holding company. Our principal business is to serve as a holding company for our bank subsidiary, Central Pacific Bank. We refer to Central Pacific Bank herein as "our Bank" or "the Bank," and when we say "the Company," "we," "us" or "our," we mean the holding company on a consolidated basis with the Bank and our other consolidated subsidiaries.

Central Pacific Bank is a full-service community bank with 39 branches and more than 95 ATMs located throughout the State of Hawaii. The Bank offers a broad range of products and services including accepting time and demand deposits and originating loans, including commercial loans, construction loans, commercial and residential mortgage loans, and consumer loans. The Bank also has four loan production offices serving customers in California.

Critical Accounting Policies

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires that management make certain judgments and use certain estimates and assumptions that affect amounts reported and disclosures made. Accounting estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period and would materially impact our consolidated financial statements as of or for the periods presented. Management has discussed the development and selection of the critical accounting estimates noted below with the Audit Committee of the Board of Directors, and the Audit Committee has reviewed the accompanying disclosures.

Allowance for Loan and Lease Losses

We maintain an allowance for loan and lease losses (the "Allowance") at an amount we expect to be sufficient to absorb probable losses inherent in our loan and lease portfolio based on a projection of probable net loan charge-offs. For loans classified as impaired, an estimated impairment loss is calculated. To estimate loan charge-offs on other loans, we evaluate the level and trend of nonperforming and potential problem loans and historical loss experience. We also consider other relevant economic conditions and borrower-specific risk characteristics, including current repayment patterns of our borrowers, the fair value of collateral securing specific loans, changes in our lending and underwriting standards and general economic factors, nationally and in the markets we serve, including the real estate market generally and the residential construction market. Estimated loss rates are determined by loan category and risk profile, and an overall required Allowance is calculated. Based on our estimate of the level of Allowance required, a provision for loan and lease losses (the "Provision") is recorded to maintain the Allowance at an appropriate level. We increased the loan loss factors assigned to outstanding balances with direct exposure to the California residential market and, accordingly, increased our Provision for those loan and lease losses in the first quarter of 2008 to account for our increased exposure in the California residential construction market.

Since we cannot predict with certainty the amount of loan and lease charge-offs that will be incurred, and because the eventual level of loan and lease charge-offs are impacted by numerous conditions beyond our control, a range of loss estimates could reasonably have been used to determine the Allowance and Provision. In addition, various regulatory agencies, as an integral part of their examination processes, periodically review our Allowance. Such agencies may require that we recognize additions to the Allowance based on their judgments about information available to them at the time of their examination. Accordingly, actual results could differ from those estimates.

Goodwill and Other Intangible Assets

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), we review the carrying amount of goodwill for impairment on an annual basis. Additionally, we perform an impairment assessment of goodwill and other intangible assets whenever events or changes in circumstances indicate that the carrying value of goodwill and other intangible assets may not be recoverable. Significant changes in circumstances can be both internal to our strategic and financial direction, as well as changes to the competitive and economic landscape.

Our impairment assessment of goodwill and other intangible assets involves the estimation of future cash flows and the fair value of reporting units to which goodwill is allocated. Estimating future cash flows and determining fair values of the reporting units is only an estimate and often involves the use of significant assumptions. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of the impairment charge.

During the first quarter of 2008, we determined that an impairment test was required under SFAS 142 due to our market capitalization continuing to be substantially less than our equity book value. As a result of our impairment test, we determined that goodwill was not impaired as of March 31, 2008.

Deferred Tax Assets and Tax Contingencies

We account for income taxes in accordance with SFAS 109, "Accounting for Income Taxes" and FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48").

Deferred tax assets and liabilities are recognized for the estimated future tax effects attributable to temporary differences and carryforwards. A valuation allowance may be required if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. In determining whether a valuation allowance is necessary, we consider the level of taxable income in prior years, to the extent that carrybacks are permitted under current tax laws, as well as estimates of future taxable income and tax planning strategies that could be implemented to accelerate taxable income if necessary. If our estimates of future taxable income were materially overstated, or if our assumptions regarding the tax consequences of tax planning strategies were inaccurate, some or all of our deferred tax assets may not be realized, which would result in a charge to earnings.

We have established income tax contingencies reserves for potential tax liabilities related to uncertain tax positions. Tax benefits are recognized when we determine that it is more likely than not that such benefits will be realized. Where uncertainty exists due to the complexity of income tax statutes, and where the potential tax amounts are significant, we generally seek independent tax opinions to support our positions. If our evaluation of the likelihood of the realization of benefits is inaccurate, we could incur additional income tax and interest expense that would adversely impact earnings, or we could receive tax benefits greater than anticipated which would positively impact earnings.

Defined Benefit Retirement Plan

Defined benefit plan obligations and related assets of our defined benefit retirement plan are presented in Note 14 to the Consolidated Financial Statements for the year ended December 31, 2007 included in the Company's Annual Report on Form 10-K. In 2002, the defined benefit retirement plan was curtailed and all plan benefits were fixed as of that date. Plan assets, which consist primarily of marketable equity and debt securities, are typically valued using market quotations. Plan obligations and the annual pension expense are determined by independent actuaries through the use of a number of assumptions. Key assumptions in measuring the plan obligations include the discount rate and the expected long-term rate of return on plan assets. In determining the discount rate, we utilize a yield that reflects the top 50% of the universe of bonds, ranked in the order of the highest yield. Asset returns are based upon the anticipated average rate of earnings expected on the invested funds of the plans. At December 31, 2007, we used a weighted-average discount rate of 6.5% and an expected long-term rate of return on plan assets of 8.0%, which affected the amount of pension liability recorded as of year-end 2007 and the amount of pension expense to be recorded in 2008. For both the discount rate and the asset return rate, a range of estimates could reasonably have been used which would affect the amount of pension expense and pension liability recorded. A 0.25% change in the discount rate assumption would impact 2008 pension expense by $0.1 million and year-end 2007 pension liability by $0.7 million, while a 0.25% change in the asset return rate would impact 2008 pension expense by $0.1 million.

Financial Summary

Net income for the first quarter of 2008 was $1.7 million, or $0.06 per diluted share, down 91.8% from $20.1 million, or $0.65 per diluted share, for the first quarter of 2007. The decrease in net income for the first quarter of 2008 was primarily due to the recognition of $34.3 million in provision for loan and lease losses as market conditions in the California residential construction market continued to deteriorate and collateral values have decreased. The effects of the increase in the provision were partially offset by a decrease in income tax expense resulting from the decrease in pre-tax income for the current period.

The following table presents annualized returns on average assets, average shareholders' equity, average tangible equity and basic and diluted earnings per share for the periods indicated. Average tangible equity is calculated as average shareholders' equity less average intangible assets which includes goodwill and core deposit premium. Average intangible assets were $273.2 million and $328.8 million for the three months ended March 31, 2008 and 2007, respectively.

	Three Months Ended March 31, 2008	2007
Return on average assets	0.12%	1.48%
Return on average shareholders' equity	0.96%	10.73%
Return on average tangible equity	1.59%	19.11%
Basic earnings per share	$ 0.06	$ 0.66
Diluted earnings per share	$ 0.06	$ 0.65

Material Trends

Hawaii's economy is expected to maintain moderate growth in 2008, but at a slower rate than experienced over the last several years, according to the latest Department of Business and Economic Development and Tourism forecast. Personal income is forecasted to increase 5.7% for 2008, while total wage and salary jobs are forecasted to increase 1.4% in 2008. Real gross state product is expected to increase by 2.5% in 2008 and 2009, as compared to the 2.7% increase in 2007.

Based upon the latest data and near term outlook, visitor industry growth has been revised downward from the prior forecast. Total arrivals are expected to decrease 1.4% in 2008, which is in contrast to a 1.0% projected increase in the previous November 2007 forecast. In 2008, visitor days are expected to decline 1.5% from fiscal 2007 and average daily spending is expected to increase 1.5% over the previous year.

Hawaii real personal income is expected to increase 1.6% in 2008, following a 1.3% increase in 2007. The state's unemployment rate, which was tied for the fourth lowest jobless rate in the nation, was 3.1% in March 2008 compared to 3.2% at December 31, 2007. The job growth forecast for 2008 remained unchanged at 1.4%.

The rate of home resales in the Hawaii housing market is expected to slow down through 2009, which is similar to the slowdown evident in the national housing market. In March 2008, the number of single-family home resales on Oahu decreased by 14.5% while the median sales price decreased by 2.4% from a year ago. Despite the anticipated slowdown in home resales, the Hawaii housing market is expected to experience lower levels of price declines compared to the national housing market.

California's economy is expected to remain relatively flat in 2008 as expected growth in technology, tourism, international trade and agriculture is estimated to offset declines in the housing and finance related industries. Job growth in 2008 is expected to be in excess of 0.5% of 2007 levels, while, California real personal income is expected to increase 4.7% in 2008, compared to 6.2% in 2007 and 6.5% in 2006. California's unemployment rate has increased to 6.2% in March 2008 from 6.1% in December 2007, further suggesting a weakening in the economy.

The residential real estate market in California has shown continued signs of weakness as tighter underwriting standards and the ongoing effects of the credit crisis have dampened sales activity. In March 2008, the number of single-family home resales in California decreased 24.5% and the median sales price decreased 29.0% from a year ago. Despite recent declines in the median sales price, affordability remains low and the inventory of unsold homes continues to grow. Accordingly, further declines in single-family home resales are expected for the remainder of 2008.

As we have seen in the past three fiscal quarters with the deteriorating market conditions of the California residential construction market, our results of operations in future periods may be significantly impacted by the economies in Hawaii, California or other markets we serve. Loan demand, deposit growth, provision for loan losses, noninterest income and noninterest expense may be affected by changes in economic conditions. If the California residential construction market does not improve or continues to deteriorate, or if the economic environments in Hawaii, California or other markets we serve suffer an adverse change such as a material decline in the real estate market, further declines in single-family home resales, or a material external shock, our results of operations may be negatively impacted.

Results of Operations

Net Interest Income

Net interest income, when expressed as a percentage of average interest earning assets, is referred to as "net interest margin." Interest income, which includes loan fees and resultant yield information, are expressed on a taxable equivalent basis using an assumed income tax rate of 35%. A comparison of net interest income on a taxable equivalent basis ("net interest income") for the three months ended March 31, 2008 and 2007 is set forth below.

	Three Months Ended March 31, 2008			Three Months Ended March 31, 2007		
(Dollars in thousands)	Average Balance	Average Yield/Rate	Amount of Interest	Average Balance	Average Yield/Rate	Amount of Interest
Assets						
Interest earning assets:						
Interest-bearing deposits in other banks	$ 495	3.17%	$ 4	$ 2,776	5.11%	$ 35
Federal funds sold & securities purchased under agreements to resell	2,641	3.20	21	778	5.20	10
Taxable investment securities (1)	739,033	5.03	9,295	743,018	4.71	8,745
Tax-exempt investment securities (1)	152,316	5.61	2,137	154,509	5.43	2,097
Loans and leases, net of unearned income (2)	4,247,369	6.65	70,294	3,899,826	7.90	76,166
Federal Home Loan Bank stock	48,797	1.00	122	48,797	0.80	98
Total interest earning assets	5,190,651	6.33	81,873	4,849,704	7.26	87,151
Nonearning assets	557,802			588,269		
Total assets	$ 5,748,453			$ 5,437,973		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing demand deposits	$ 451,058	0.12%	$ 137	$ 433,167	0.13%	$ 138
Savings and money market deposits	1,141,285	1.33	3,785	1,236,806	2.06	6,285
Time deposits under $100,000	532,517	3.38	4,481	627,268	3.74	5,784
Time deposits $100,000 and over	1,105,154	3.73	10,248	900,843	4.52	10,050
Short-term borrowings	229,455	3.37	1,923	37,021	5.55	505
Long-term debt	920,006	4.24	9,694	768,312	5.26	9,968
Total interest-bearing liabilities	4,379,475	2.78	30,268	4,003,417	3.32	32,730
Noninterest-bearing deposits	599,047			589,009		
Other liabilities	79,756			95,269		
Shareholders' equity	690,175			750,278		
Total liabilities and shareholders' equity	$ 5,748,453			$ 5,437,973		

Net interest income		$	51,605		$	54,421
Net interest margin	3.99%			4.52%		

(1) At amortized cost.
(2) Includes nonaccrual loans.

Net interest income of $51.6 million for the first quarter of 2008 decreased by $2.8 million, or 5.2%, from the first quarter of 2007. The decrease in net interest income for the first quarter of 2008 was primarily the result of a decrease in average loan yields as certain variable rate loans repriced downward over the past twelve months in connection with the Federal Reserve's actions to decrease interest rates. Net interest income was positively impacted by a decrease in interest expense as average rates on interest-bearing liabilities have decreased over the past twelve months, also reflective of the Federal Reserve's recent actions to decrease interest rates.

Interest Income

Taxable-equivalent interest income of $81.9 million for the first quarter of 2008 decreased by $5.3 million, or 6.1%, from the first quarter of 2007. The current quarter decrease in taxable-equivalent interest income was attributable to the reversal of $1.5 million of interest income on certain nonaccrual loans in the first quarter of 2008, as well as a decrease in average loan yields, which declined to 6.65% for the first quarter of 2008 from 7.90% in the comparable prior year period. The decrease in the average loan yield (including the effects of the reversal mentioned above) contributed to approximately $12.2 million of the current quarter decrease in taxable-equivalent interest income. Partially offsetting the decrease in interest income was the $347.5 million, or 8.9%, increase in average loans and leases in the first quarter of 2008 over the comparable prior year period. This increase in volume resulted in a $6.9 million increase in taxable-equivalent interest income for the first quarter of 2008 when compared to the comparable prior year period. The increase in average loans and leases for the current quarter was primarily driven by an increase in residential mortgage originations as competition in this market has diminished with the departure of several national residential mortgage lenders from the Hawaii market.

Interest Expense

Taxable-equivalent interest expense of $30.3 million for the first quarter of 2008, decreased by $2.5 million, or 7.5%, from the comparable quarter one year ago. The change in interest expense was attributable to the decrease in average rates paid on average interest-bearing liabilities, particularly on savings and money market deposits, which decreased by 73 basis points ("bp"); time deposits $100,000 and over, which decreased by 79 bp and long-term debt, which decreased by 102 bp. The decreases in average rates contributed to $2.3 million, $1.8 million and $2.0 million of the decrease in taxable-equivalent interest expense, respectively. Partially offsetting the decrease in taxable-equivalent interest expense were increases in average balances on time deposits $100,000 and over, which increased by $204.3 million, or 22.7%, from the comparable prior year period and short-term borrowings, which increased by $192.4 million, or 519.8%, from the comparable prior year period. These volume increases resulted in higher taxable-equivalent interest expense of $2.3 million and $2.7 million, respectively, for the first quarter of 2008. The increase in average balances of time deposits $100,000 and over was reflective of the continued shift in our deposit base from lower rate checking and savings accounts to higher rate time deposit accounts. The increase in short term borrowings was attributable to loan growth outpacing deposit growth.

Net Interest Margin

Our net interest margin was 3.99% for the first quarter of 2008 compared to 4.52% for the first quarter of 2007. The compression in our net interest margin is primarily attributable to the aforementioned decrease in net income. In addition, average yields earned on interest earning assets have declined faster than the average rates paid on interest-bearing liabilities, as the rate of downward repricing of interest-bearing liabilities has been tempered by the continued strong competition for deposits in the Hawaii market.

Nonperforming Assets, Accruing Loans Delinquent for 90 Days or More, Restructured Loans Still Accruing Interest

The following table sets forth nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest at the dates indicated.

	March 31, 2008	December 31, 2007
	(Dollars in thousands)	
Nonperforming Assets:		
Nonaccrual loans (including loans held for sale):		
Commercial, financial and agricultural	$ 251	$ 231
Real estate:		
Construction	116,342	61,017
Mortgage-residential	162	-
Mortgage-commercial	-	293
Total non accrual loans	116,755	61,541
Other real estate	2,000	-
Total nonperforming assets	118,755	61,541
Accruing loans delinquent for 90 days or more:		
Commercial, financial and agricultural	69	18
Real estate:		
Mortgage-residential	57	-
Mortgage-commercial	-	586
Consumer	355	273
Leases	51	26
Total accruing loans delinquent for 90 days or more	532	903
Restructured loans still accruing interest:		
Total restructured loans still accruing interest	-	-
Total nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest	$ 119,287	$ 62,444
Total nonperforming assets as a percentage of loans and other real estate	2.81%	1.48%
Total nonperforming assets and accruing loans delinquent for 90 days or more as a percentage of loans and other real estate	2.82%	1.51%
Total nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest as a percentage of loans and other real estate	2.82%	1.51%

Nonperforming assets, which includes nonaccrual loans and leases, foreclosed real estate and other nonperforming investments totaled $118.8 million at March 31, 2008, compared to $61.5 million at fiscal 2007 year-end. Nonperforming assets at March 31, 2008 were comprised of nonaccrual loans of $68.9 million, loans classified as held for sale that were nonperforming of $47.9 million and other real estate of $2.0 million. The increase in nonperforming assets during the first quarter of 2008 was primarily attributable to the inclusion of 13 California residential construction loans totaling $76.5 million, as market conditions in the California residential construction market continued to deteriorate, partially offset by partial charge-offs of six California residential constructions loans to five borrowers totaling $16.4 million.

As indicated above, the Company's credit risk position declined further during the current quarter as the deterioration in the California residential construction market continued. Lower absorption rates in many of the California residential tract lending projects that we financed resulted in the continued decline of California home prices. These conditions adversely impacted a number of our California borrowers with exposure to this sector and led to further reductions in collateral values.

An increase in impaired loans combined with the reduced collateral values described above contributed to the $34.3 million Provision during the current quarter, compared to a Provision of $2.6 million one year ago. The increased Provision was necessary to ensure that our Allowance was appropriate and reflects the current, reduced value of the collateral supporting our impaired loans with exposure to the California residential construction market.

In light of the significant negative impact our exposure to the California residential construction market had on our overall credit risk position, additional information regarding our exposure to this sector follows:

	March 31, 2008	December 31, 2007
	(Dollars in thousands)	
Total loans outstanding - California residential construction market:		
Loans held for sale	$ 47,929	$ 5,400
Loan portfolio	197,936	305,230
Total	$ 245,865	$ 310,630
Percentage of California residential construction loan portfolio to total loans	4.7%	7.4%
Non performing assets - California residential construction market:		
Nonaccrual loans	$ 63,502	$ 52,334
Nonaccrual loans held for sale	47,929	5,400
Other real estate	2,000	-
	$ 113,431	$ 57,734
Total nonperforming assets with exposure to the California residential construction market assets as a percentage of total assets	1.96%	1.02%

Beginning in fourth quarter of 2007, we engaged the services of seasoned real estate professionals to assist us in assessing and managing our risk exposure to the California residential construction market. As a result of these efforts and given the uncertainties in the short-term outlook for this market, we have initiated loan sale proceedings on several California residential construction loans and are pursuing a variety of options to reduce our credit risk exposure to this market.

Allowance and Provision for Loan and Lease Losses

A discussion of our accounting policy regarding the Allowance is contained in the Critical Accounting Policies section of this report. The following table sets forth certain information with respect to the Allowance as of the dates and for the periods indicated:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
	(Dollars in thousands)	
Allowance for loan and lease losses:		
Balance at beginning of period	$ 92,049	$ 52,280
Provision for loan and lease losses	34,272	2,600
Charge-offs:		
Commercial, financial and agricultural	199	3,424
Real estate:		
Construction	53,722	-
Mortgage-residential	-	358
Consumer	889	1,053
Leases	-	-
Total charge-offs	54,810	4,835
Recoveries:		
Commercial, financial and agricultural	55	39
Real estate:		
Mortgage-residential	52	35
Mortgage-commercial	2	3
Consumer	488	492
Leases	-	-
Total recoveries	597	569
Net charge-offs	54,213	4,266
Balance at end of period	$ 72,108	$ 50,614
Annualized ratio of net charge-offs to average loans	5.11%	0.44%

Our Allowance at March 31, 2008 totaled $72.1 million, a decrease of $19.9 million, or 21.7%, from year-end 2007. The current quarter decrease was primarily attributable to $54.2 million in net charge-offs in the first quarter of 2008, concentrated in loans with direct exposure to the California residential construction market. As previously mentioned, the Provision of $34.3 million recognized in the first quarter of 2008 was attributed to the decline in collateral values for many loans with exposure to this sector.

The Allowance, expressed as a percentage of total loans, was 1.73% at March 31, 2008, compared to 2.22% at year-end 2007. The sequential quarter decrease in this percentage was primarily due to current quarter charge-offs totaling $54.8 million combined with the current quarter transfer of non-performing California residential construction loans totaling $42.5 million from our loan portfolio to the loans held for sale category. Because a significant amount of our non-performing California residential construction loans were charged off and/or transferred to held for sale, the Allowance as a percentage of the remaining portfolio decreased during the quarter. As we have seen with the downturn in the California residential construction market, continued economic deterioration in the areas we serve could adversely affect our borrowers' ability to repay their loans or the value of collateral securing those loans and, consequently, the level of net loan charge-offs and the Provision.

Other Operating Income

Total other operating income of $14.3 million for the first quarter of 2008 increased by $3.1 million, or 28.0%, from the comparable quarter one year ago. The change was largely due to increases in miscellaneous operating income of $1.6 million, income from bank-owned life insurance of $0.8 million, and gains on sales of loans of $0.4 million. The increase in miscellaneous operating income resulted from the mandatory partial redemption of our shares in Visa, Inc., which resulted in a gain of $0.9 million, while the increase in bank-owned life insurance was primarily the result of $0.8 million in net death benefits recognized during the first quarter of 2008. The increase in gains on sales of loans was reflective of the increase in loan origination activity reported in the first quarter of 2008. Several factors have lead to the increased loan origination activity, including our establishment of strategic alliances with real estate brokers and developers that provide additional loan origination opportunities and decreased competition as several national lenders have recently exited the Hawaii market.

Other Operating Expense

Total other operating expense was $31.5 million for the first quarter of 2008, up $1.0 million, or 3.2%, from the comparable quarter one year ago. The increase in other operating expense was attributable to an increase in foreclosed asset expense of $2.6 million, which represented the writedown of foreclosed property to its estimated fair value, and an increase in salaries and employee benefits of $1.0 million as salaries and employee benefits for the first quarter of 2007 included the effects of a $1.8 million reversal of certain incentive compensation accruals. The aforementioned increases were partially offset by a decrease in miscellaneous operating expense of $3.2 million, primarily due to a $4.5 million reduction in the reserve for unfunded commitments recognized in the first quarter of 2008. The decrease in reserves for unfunded commitments was primarily attributable to the termination of several outstanding commitments to certain borrowers with exposure to the California residential construction market.

Given the current economic conditions under which we operate, we expect to continue to tightly manage our operating expenses and anticipate expenses for the remainder of 2008 to remain relatively consistent with current levels.

Income Taxes

In the first quarter of 2008, the Company recognized an income tax benefit of $2.3 million on a pre-tax net loss of $0.6 million. In the comparable prior year period, the Company recorded income tax expense of $11.6 million on pre-tax income of $31.8 million. The current quarter’s tax benefit was impacted by the disproportionate recognition of federal and state tax credits and the generation of tax-exempt income compared to taxable income.

Factors that may affect the effective tax rate for the remainder of 2008 include the level of tax-exempt income recognized, the amount of nondeductible expenses incurred and the amount of federal and state tax credits available to offset future taxable income.

Financial Condition

Total assets at March 31, 2008 grew to $5.8 billion, increasing by $119.7 million, or 2.1%, compared to year-end 2007.

Loans and leases, net of unearned income, grew to $4.2 billion, increasing slightly by $34.9 million, or 0.8%, over year-end 2007. The increase was primarily attributable to increases in our residential and commercial real estate mortgage portfolios, partially offset by decreases in our commercial, financial and agricultural and real estate construction loan portfolios. Further reducing our loans and leases balance was the current quarter reclassification of $42.5 million (net of related charge-offs) of California residential construction loans and $17.5 million of Hawaii residential mortgage loans from the held to maturity loan portfolio to loans held for sale. The reclassification of the California residential construction loans to held for sale reflects our continued effort to minimize our exposure to this sector, while the reclassification of the Hawaii residential mortgage loans was done to generate additional liquidity. After considering the effects of the current quarter's loan growth and the reclassification of certain loans to held for sale, our Hawaii operations grew by approximately $104.7 million while our mainland loan portfolio decreased by $69.8 million.

Total deposits at March 31, 2008 of $3.8 billion decreased by $222.7 million, or 5.6%, from year-end 2007. Interest-bearing deposits at March 31, 2008, decreased by $189.8 million, or 5.7%, while noninterest-bearing deposits decreased by $32.9 million, or 4.9% from year-end 2007. The decrease in deposits was reflective of customers seeking higher returns from other investment vehicles as deposit rates have decreased in the current quarter and the overall softening of the economy.

Capital Resources

Shareholders' equity was $674.7 million at March 31, 2008, compared to $674.4 million at year-end 2007. Book value per share at March 31, 2008 was $23.50, compared to $23.45 at year-end 2007.

On January 30, 2008, the Company's board of directors declared a first quarter cash dividend of $0.25 per share, an increase of 4.2% over the $0.24 per share dividend declared in the first quarter of 2007.

In January 2008, the Company's board of directors authorized the repurchase and retirement of up to 1,200,000 shares of the Company's common stock (the "2008 Repurchase Plan"). Repurchases under the 2008 Repurchase Plan may be made from time to time on the open market or in privately negotiated transactions. During the three months ended March 31, 2008, we repurchased and retired a total of 100,000 shares of common stock for approximately $1.8 million under the 2008 Repurchase Plan. At March 31, 2008, a total of 1,100,000 shares remained authorized for repurchase under the 2008 Repurchase Plan.

We have five statutory trusts: CPB Capital Trust I, CPB Capital Trust II, CPB Statutory Trust III, CPB Capital Trust IV and CPB Statutory Trust V, which issued a total of $105.0 million in trust preferred securities. The statutory trusts are not consolidated in the consolidated financial statements as of September 30, 2007. However, the Federal Reserve Board (the "FRB") has determined that certain cumulative preferred securities, such as the trust preferred securities issued by the capital and statutory trusts, qualify as minority interest, and are included in the calculation of Tier 1 capital up to 25% of total risk-based capital with the excess includable as Tier 2 capital.

Our objective with respect to capital resources is to maintain a level of capital that will support sustained asset growth and anticipated risks. Furthermore, we seek to ensure that regulatory guidelines and industry standards for well-capitalized institutions are met or exceeded.

Regulations on capital adequacy guidelines adopted by the FRB and the Federal Deposit Insurance Corporation (the "FDIC") are as follows. An institution is required to maintain a minimum ratio of qualifying total capital to risk-adjusted assets of 8% and a minimum ratio of Tier 1 capital to risk-adjusted assets of 4%. In addition to the risk-based guidelines, federal banking regulators require banking organizations to maintain a minimum amount of Tier 1 capital to total assets, referred to as the leverage ratio. For a banking organization rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio of Tier 1 capital to total assets must be 3%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

The following table sets forth the Company's capital ratios and capital adequacy requirements applicable as of the dates indicated. In addition, FDIC-insured institutions such as our principal banking subsidiary, Central Pacific Bank, must maintain leverage, Tier 1 and total risk-based capital ratios of at least 5%, 6% and 10%, respectively, to be considered "well capitalized" under the prompt corrective action provisions of the FDIC Improvement Act of 1991.

	Actual		Minimum Required for Capital Adequacy Purposes		Minimum Required to be Well Capitalized	
(Dollars in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
Company						
At March 31, 2008:						
Leverage capital	$ 529,491	9.6%	$ 219,794	4.0%	$ 274,743	5.0%
Tier 1 risk-based capital	529,491	10.9	193,702	4.0	290,553	6.0
Total risk-based capital	590,192	12.2	387,403	8.0	484,253	10.0
At December 31, 2007:						
Leverage capital	$ 535,670	9.8%	$ 218,477	4.0%	$ 273,096	5.0%
Tier 1 risk-based capital	535,670	11.5	187,049	4.0	280,574	6.0
Total risk-based capital	594,620	12.7	374,098	8.0	467,623	10.0

Central Pacific Bank								
At March 31, 2008:								
Leverage capital	$	500,395	9.2%	$	218,831	4.0%	$	273,539	5.0%
Tier 1 risk-based capital		500,395	10.4		193,328	4.0		289,992	6.0
Total risk-based capital		560,981	11.6		386,656	8.0		483,320	10.0
At December 31, 2007:									
Leverage capital	$	518,923	9.5%	$	218,143	4.0%	$	272,679	5.0%
Tier 1 risk-based capital		518,923	11.1		186,743	4.0		280,115	6.0
Total risk-based capital		577,779	12.4		373,487	8.0			