

BANK OF HAWAII CORP  
Form 10-Q  
October 31, 2008

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

*Washington, D.C. 20549*



## FORM 10-Q

(Mark One)

☒ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended September 30, 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: 1-6887**

## BANK OF HAWAII CORPORATION

(Exact name of registrant as specified in its charter)

**Delaware**  
(State of incorporation)

**99-0148992**  
(I.R.S. Employer Identification No.)

**130 Merchant Street, Honolulu, Hawaii**  
(Address of principal executive offices)

**96813**  
(Zip Code)

**1-888-643-3888**

(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 ☒ No ☐

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

Large accelerated filer ☒

Accelerated filer ☐

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Non-accelerated filer ☐ (Do not check if a smaller reporting company)

Smaller reporting company ☐

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

Yes ☐ No ☒

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

As of October 24, 2008, there were 47,711,974 shares of common stock outstanding.

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|   | <b>Three Months Ended</b> |                  | <b>Nine Months Ended</b> |                   |
|---|---------------------------|------------------|--------------------------|-------------------|
|   | <b>September 30,</b>      |                  | <b>September 30,</b>     |                   |
| (dollars in thousands, except per share amounts)      | <b>2008</b>               | <b>2007</b>      | <b>2008</b>              | <b>2007</b>       |
| Interest Income                                       |                           |                  |                          |                   |
| Interest and Fees on Loans and Leases                 | \$ 92,744                 | \$ 112,787       | \$ 295,116               | \$ 335,111        |
| Income on Investment Securities                       |                           |                  |                          |                   |
| Trading   | 1,174                     | 1,114            | 3,543                    | 4,089             |
| Available-for-Sale                                    | 35,152                    | 33,486           | 104,724                  | 96,010            |
| Held-to-Maturity                                      | 2,870                     | 3,616            | 9,142                    | 11,495            |
| Deposits  | 33                        | 1,086            | 432                      | 1,240             |
| Funds Sold  | 141                       | 1,103            | 1,553                    | 2,694             |
| Other   | 490                       | 364              | 1,405                    | 1,061             |
| Total Interest Income                                 | 132,604                   | 153,556          | 415,915                  | 451,700           |
| Interest Expense                                      |                           |                  |                          |                   |
| Deposits  | 17,736                    | 37,613           | 65,439                   | 104,689           |
| Securities Sold Under Agreements to Repurchase        | 7,675                     | 11,726           | 25,780                   | 35,277            |
| Funds Purchased                                       | 507                       | 1,654            | 1,410                    | 4,029             |
| Short-Term Borrowings                                 | 13                        | 87               | 59                       | 265               |
| Long-Term Debt  | 3,098                     | 3,920            | 10,304                   | 11,869            |
| Total Interest Expense                                | 29,029                    | 55,000           | 102,992                  | 156,129           |
| <b>Net Interest Income</b>                            | <b>103,575</b>            | <b>98,556</b>    | <b>312,923</b>           | <b>295,571</b>    |
| Provision for Credit Losses                           | 20,358                    | 4,070            | 41,957                   | 10,064            |
| Net Interest Income After Provision for Credit Losses | 83,217                    | 94,486           | 270,966                  | 285,507           |
| Noninterest Income                                    |                           |                  |                          |                   |
| Trust and Asset Management                            | 14,193                    | 15,146           | 44,739                   | 47,114            |
| Mortgage Banking                                      | 621                       | 3,848            | 7,656                    | 9,698             |
| Service Charges on Deposit Accounts                   | 13,045                    | 11,919           | 37,539                   | 33,958            |
| Fees, Exchange, and Other Service Charges             | 16,991                    | 16,465           | 50,268                   | 49,082            |
| Investment Securities Gains, Net                      | 159                       | 789              | 446                      | 1,380             |
| Insurance   | 5,902                     | 7,446            | 18,622                   | 18,548            |
| Other   | 6,075                     | 5,629            | 44,380                   | 20,450            |
| <b>Total Noninterest Income</b>                       | <b>56,986</b>             | <b>61,242</b>    | <b>203,650</b>           | <b>180,230</b>    |
| Noninterest Expense                                   |                           |                  |                          |                   |
| Salaries and Benefits                                 | 46,764                    | 44,944           | 148,221                  | 134,937           |
| Net Occupancy   | 11,795                    | 10,267           | 33,581                   | 29,773            |
| Net Equipment   | 4,775                     | 4,871            | 13,570                   | 14,529            |
| Professional Fees                                     | 3,270                     | 2,369            | 8,471                    | 7,511             |
| Other   | 20,186                    | 18,999           | 60,241                   | 56,655            |
| <b>Total Noninterest Expense</b>                      | <b>86,790</b>             | <b>81,450</b>    | <b>264,084</b>           | <b>243,405</b>    |
| Income Before Provision for Income Taxes              | 53,413                    | 74,278           | 210,532                  | 222,332           |
| Provision for Income Taxes                            | 6,004                     | 26,499           | 57,626                   | 79,489            |
| <b>Net Income</b>                                     | <b>\$ 47,409</b>          | <b>\$ 47,779</b> | <b>\$ 152,906</b>        | <b>\$ 142,843</b> |
| Basic Earnings Per Share                              | \$ 1.00                   | \$ 0.98          | \$ 3.20                  | \$ 2.90           |
| Diluted Earnings Per Share                            | \$ 0.99                   | \$ 0.96          | \$ 3.17                  | \$ 2.86           |
| Dividends Declared Per Share                          | \$ 0.44                   | \$ 0.41          | \$ 1.32                  | \$ 1.23           |
| Basic Weighted Average Shares                         | 47,518,078                | 48,913,293       | 47,738,245               | 49,204,295        |
| Diluted Weighted Average Shares                       | 48,057,965                | 49,663,049       | 48,295,901               | 50,001,594        |

The accompanying notes are an integral part of the Consolidated Financial Statements (Unaudited).



Table of Contents**Bank of Hawaii Corporation and Subsidiaries****Consolidated Statements of Condition (Unaudited)**

| (dollars in thousands)   | September 30,<br>2008 | December 31,<br>2007 | September 30,<br>2007 |
|--|-----------------------|----------------------|-----------------------|
| <b>Assets</b>  |                       |                      |                       |
| Interest-Bearing Deposits  | \$ 13,845             | \$ 4,870             | \$ 35,471             |
| Funds Sold   |                       | 15,000               |                       |
| Investment Securities  |                       |                      |                       |
| Trading  | 90,993                | 67,286               | 92,831                |
| Available-for-Sale   | 2,572,111             | 2,563,190            | 2,591,982             |
| Held-to-Maturity (Fair value of \$245,720; \$287,644; and \$299,191)   | 249,083               | 292,577              | 307,653               |
| Loans Held for Sale  | 14,903                | 12,341               | 8,016                 |
| Loans and Leases   | 6,539,458             | 6,580,861            | 6,599,915             |
| Allowance for Loan and Lease Losses  | (115,498)             | (90,998)             | (90,998)              |
| Net Loans and Leases   | 6,423,960             | 6,489,863            | 6,508,917             |
| Total Earning Assets   | 9,364,895             | 9,445,127            | 9,544,870             |
| Cash and Noninterest-Bearing Deposits  | 285,762               | 368,402              | 344,267               |
| Premises and Equipment   | 118,333               | 117,177              | 120,318               |
| Customers' Acceptances   | 1,250                 | 1,112                | 1,967                 |
| Accrued Interest Receivable  | 41,061                | 45,261               | 52,652                |
| Foreclosed Real Estate   | 293                   | 184                  | 105                   |
| Mortgage Servicing Rights  | 27,707                | 27,588               | 28,407                |
| Goodwill   | 34,959                | 34,959               | 34,959                |
| Other Assets   | 460,787               | 433,132              | 422,050               |
| <b>Total Assets</b>  | <b>\$ 10,335,047</b>  | <b>\$ 10,472,942</b> | <b>\$ 10,549,595</b>  |
| <b>Liabilities</b>   |                       |                      |                       |
| Deposits   |                       |                      |                       |
| Noninterest-Bearing Demand   | \$ 1,592,251          | \$ 1,935,639         | \$ 1,894,933          |
| Interest-Bearing Demand  | 1,750,297             | 1,634,675            | 1,530,982             |
| Savings  | 2,738,684             | 2,630,471            | 2,711,169             |
| Time   | 1,577,252             | 1,741,587            | 1,738,082             |
| Total Deposits   | 7,658,484             | 7,942,372            | 7,875,166             |
| Funds Purchased  | 189,700               | 75,400               | 191,900               |
| Short-Term Borrowings  | 10,621                | 10,427               | 10,749                |
| Securities Sold Under Agreements to Repurchase   | 1,109,431             | 1,029,340            | 1,087,511             |
| Long-Term Debt (includes \$120,598 carried at fair value as of September 30, 2008)   | 204,616               | 235,371              | 235,350               |
| Bankers' Acceptances   | 1,250                 | 1,112                | 1,967                 |
| Retirement Benefits Payable  | 22,438                | 29,984               | 41,125                |
| Accrued Interest Payable   | 12,702                | 20,476               | 18,526                |
| Taxes Payable and Deferred Taxes   | 240,795               | 278,218              | 271,089               |
| Other Liabilities  | 104,990               | 99,987               | 84,515                |
| <b>Total Liabilities</b>   | <b>9,555,027</b>      | <b>9,722,687</b>     | <b>9,817,898</b>      |
| <b>Shareholders' Equity</b>  |                       |                      |                       |
| Common Stock (\$.01 par value; authorized 500,000,000 shares; issued / outstanding: September 2008 - 57,022,797 / 47,707,629; December 2007 - 56,995,447 / 48,589,645; and September 2007 - 57,005,602 / 49,068,275) | 568                   | 567                  | 567                   |
| Capital Surplus  | 491,419               | 484,790              | 482,586               |
| Accumulated Other Comprehensive Loss   | (18,643)              | (5,091)              | (28,359)              |
| Retained Earnings  | 770,373               | 688,638              | 671,451               |
| Treasury Stock, at Cost (Shares: September 2008 - 9,315,168; December 2007 - 8,405,802; and September 2007 - 7,937,327)  | (463,697)             | (418,649)            | (394,548)             |

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|   |                      |                      |                      |
|---|----------------------|----------------------|----------------------|
| <b>Total Shareholders' Equity</b>                 | 780,020              | 750,255              | 731,697              |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>\$ 10,335,047</b> | <b>\$ 10,472,942</b> | <b>\$ 10,549,595</b> |

The accompanying notes are an integral part of the Consolidated Financial Statements (Unaudited).

Table of Contents**Bank of Hawaii Corporation and Subsidiaries****Consolidated Statements of Shareholders' Equity (Unaudited)**

|  |              |                         |                            | Accum.<br>Other<br>Compre-<br>hensive<br>Loss | Retained<br>Earnings | Treasury<br>Stock | Compre-<br>hensive<br>Income |
|--|--------------|-------------------------|----------------------------|---|----------------------|-------------------|------------------------------|
| (dollars in thousands)   | <b>Total</b> | <b>Common<br/>Stock</b> | <b>Capital<br/>Surplus</b> |   |                      |                   |                              |
| <b>Balance as of December 31, 2007</b>   | \$750,255    | \$ 567                  | \$484,790                  | \$ (5,091)                                    | \$688,638            | \$(418,649)       |                              |
| Cumulative-Effect Adjustment of a Change in Accounting Principle, Net of Tax:  |              |                         |                            |   |                      |                   |                              |
| SFAS No. 159, <i>The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115</i>                      | (2,736)      |                         |                            |   | (2,736)              |                   |                              |
| Comprehensive Income:  |              |                         |                            |   |                      |                   |                              |
| Net Income   | 152,906      |                         |                            |   | 152,906              |                   | \$152,906                    |
| Other Comprehensive Income, Net of Tax:  |              |                         |                            |   |                      |                   |                              |
| Change in Unrealized Gains and Losses on Investment Securities   |              |                         |                            |   |                      |                   |                              |
| Available-for-Sale   | (13,699)     |                         |                            | (13,699)                                      |                      |                   | (13,699)                     |
| Amortization of Net Loss for Pension Plans and Postretirement Benefit Plan   | 147          |                         |                            | 147   |                      |                   | 147                          |
| <b>Total Comprehensive Income</b>  |              |                         |                            |   |                      |                   | <b>\$139,354</b>             |
| Share-Based Compensation   | 4,480        |                         | 4,480                      |   |                      |                   |                              |
| Net Tax Benefits related to Share-Based Compensation   | 1,728        |                         | 1,728                      |   |                      |                   |                              |
| Common Stock Issued under Purchase and Equity Compensation Plans (378,382 shares)  | 12,000       | 1                       | 421                        |   | (5,075)              | 16,653            |                              |
| Common Stock Repurchased (1,260,398 shares)  | (61,701)     |                         |                            |   |                      | (61,701)          |                              |
| Cash Dividends Paid  | (63,360)     |                         |                            |   | (63,360)             |                   |                              |
| <b>Balance as of September 30, 2008</b>  | \$780,020    | \$ 568                  | \$491,419                  | \$(18,643)                                    | \$770,373            | \$(463,697)       |                              |
| <b>Balance as of December 31, 2006</b>   | \$719,420    | \$ 566                  | \$475,178                  | \$(39,084)                                    | \$630,660            | \$(347,900)       |                              |
| Cumulative-Effect Adjustment of a Change in Accounting Principle, Net of Tax:  |              |                         |                            |   |                      |                   |                              |
| SFAS No. 156, <i>Accounting for Servicing of Financial Assets, an amendment of FASB Statement No. 140</i>  | 5,126        |                         |                            | 5,279   | (153)                |                   |                              |
| FSP No. 13-2, <i>Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction</i> | (27,106)     |                         |                            |   | (27,106)             |                   |                              |
| FIN 48, <i>Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109</i>   | (7,247)      |                         |                            |   | (7,247)              |                   |                              |
| Comprehensive Income:  |              |                         |                            |   |                      |                   |                              |
| Net Income   | 142,843      |                         |                            |   | 142,843              |                   | \$142,843                    |
| Other Comprehensive Income, Net of Tax:  |              |                         |                            |   |                      |                   |                              |
| Change in Unrealized Gains and Losses on Investment Securities   |              |                         |                            |   |                      |                   |                              |
| Available-for-Sale   | 4,809        |                         |                            | 4,809   |                      |                   | 4,809                        |
| Amortization of Net Loss for Pension Plans and Postretirement Benefit Plan   | 637          |                         |                            | 637   |                      |                   | 637                          |
| <b>Total Comprehensive Income</b>  |              |                         |                            |   |                      |                   | <b>\$148,289</b>             |
| Share-Based Compensation   | 4,464        |                         | 4,464                      |   |                      |                   |                              |
| Net Tax Benefits related to Share-Based Compensation   | 2,624        |                         | 2,624                      |   |                      |                   |                              |
| Common Stock Issued under Purchase and Equity Compensation Plans (628,252 shares)  | 16,321       | 1                       | 320                        |   | (6,611)              | 22,611            |                              |
| Common Stock Repurchased (1,335,305 shares)  | (69,259)     |                         |                            |   |                      | (69,259)          |                              |
| Cash Dividends Paid  | (60,935)     |                         |                            |   | (60,935)             |                   |                              |
| <b>Balance as of September 30, 2007</b>  | \$731,697    | \$ 567                  | \$482,586                  | \$(28,359)                                    | \$671,451            | \$(394,548)       |                              |

The accompanying notes are an integral part of the Consolidated Financial Statements (Unaudited).



Table of Contents**Bank of Hawaii Corporation and Subsidiaries****Consolidated Statements of Cash Flows (Unaudited)**

|   | <b>Nine Months Ended</b> |                   |
|---|--------------------------|-------------------|
|   | <b>September 30,</b>     |                   |
|   | <b>2008</b>              | <b>2007</b>       |
| (dollars in thousands)  |                          |                   |
| <b>Operating Activities</b>   |                          |                   |
| Net Income  | \$ 152,906               | \$ 142,843        |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities: |                          |                   |
| Provision for Credit Losses   | 41,957                   | 10,064            |
| Depreciation and Amortization   | 10,878                   | 11,006            |
| Amortization of Deferred Loan and Lease Fees                                      | (1,563)                  | (1,354)           |
| Amortization and Accretion of Premiums/Discounts on Investment Securities, Net    | 1,117                    | 2,250             |
| Share-Based Compensation  | 4,480                    | 4,464             |
| Benefit Plan Contributions  | (8,403)                  | (8,404)           |
| Deferred Income Taxes   | (32,559)                 | (81,991)          |
| Net Gain on Investment Securities   | (446)                    | (1,380)           |
| Net Change in Trading Securities  | (23,707)                 | 71,349            |
| Proceeds from Sales of Loans Held for Sale  | 327,331                  | 253,217           |
| Originations of Loans Held for Sale   | (329,893)                | (249,291)         |
| Tax Benefits from Share-Based Compensation  | (1,813)                  | (2,624)           |
| Net Change in Other Assets and Other Liabilities                                  | (21,944)                 | 2,753             |
| <b>Net Cash Provided by Operating Activities</b>                                  | <b>118,341</b>           | <b>152,902</b>    |
| <b>Investing Activities</b>   |                          |                   |
| Investment Securities Available-for-Sale:   |                          |                   |
| Proceeds from Prepayments and Maturities  | 601,213                  | 418,107           |
| Proceeds from Sales   | 233,085                  | 50,012            |
| Purchases   | (864,985)                | (611,015)         |
| Investment Securities Held-to-Maturity:   |                          |                   |
| Proceeds from Prepayments and Maturities  | 43,184                   | 63,193            |
| Net Change in Loans and Leases  | 25,509                   | (28,176)          |
| Premises and Equipment, Net   | (12,034)                 | (5,399)           |
| <b>Net Cash Provided by (Used in) Investing Activities</b>                        | <b>25,972</b>            | <b>(113,278)</b>  |
| <b>Financing Activities</b>   |                          |                   |
| Net Change in Deposits  | (283,888)                | (148,228)         |
| Net Change in Short-Term Borrowings   | 194,585                  | 171,138           |
| Repayments of Long-Term Debt  | (32,425)                 | (25,000)          |
| Tax Benefits from Share-Based Compensation  | 1,813                    | 2,624             |
| Proceeds from Issuance of Common Stock  | 11,998                   | 16,442            |
| Repurchase of Common Stock  | (61,701)                 | (69,259)          |
| Cash Dividends Paid   | (63,360)                 | (60,935)          |
| <b>Net Cash Used in Financing Activities</b>                                      | <b>(232,978)</b>         | <b>(113,218)</b>  |
| Net Change in Cash and Cash Equivalents   | (88,665)                 | (73,594)          |
| Cash and Cash Equivalents at Beginning of Period                                  | 388,272                  | 453,332           |
| <b>Cash and Cash Equivalents at End of Period</b>                                 | <b>\$ 299,607</b>        | <b>\$ 379,738</b> |
| <b>Supplemental Information</b>   |                          |                   |
| Cash Paid for:  |                          |                   |
| Interest  | \$ 110,766               | \$ 160,321        |
| Income Taxes  | 75,758                   | 73,989            |
| Non-cash Investing and Financing Activities:                                      |                          |                   |
| Transfers from Investment Securities-Available-for-Sale to Trading                |                          | 164,180           |
| Transfers from Loans to Foreclosed Real Estate                                    | 174                      | 243               |

The accompanying notes are an integral part of the Consolidated Financial Statements (Unaudited).



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**Bank of Hawaii Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**(Unaudited)**

**Note 1. Summary of Significant Accounting Policies**

*Basis of Presentation*

Bank of Hawaii Corporation (the *Parent* ) is a bank holding company headquartered in Honolulu, Hawaii. Bank of Hawaii Corporation and its Subsidiaries (the *Company* ) provide a broad range of financial products and services to customers in Hawaii and the Pacific Islands (Guam, nearby islands, and American Samoa). The *Parent* 's principal and only operating subsidiary is Bank of Hawaii (the *Bank* ). All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements of the *Company* 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, they do not include all of the information and accompanying notes required by *GAAP* for complete financial statements. In the opinion of management, the consolidated financial statements reflect normal recurring adjustments necessary for a fair presentation of the results for the interim periods.

The preparation of financial statements in conformity with *GAAP* requires management to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. Actual results may differ from those estimates and such differences could be material to the financial statements.

Certain prior period amounts have been reclassified to conform to current period classifications.

These statements should be read in conjunction with the audited consolidated financial statements and related notes included in the *Company* 's Annual Report on Form 10-K for the year ended December 31, 2007. Operating results for the nine months ended September 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

*Fair Value Measurements*

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Statement of Financial Accounting Standards ( SFAS ) No. 157, *Fair Value Measurements*, which became effective for the Company on January 1, 2008, established a framework for measuring fair value, while expanding fair value measurement disclosures. SFAS No. 157 established a fair value hierarchy that distinguishes between independent observable inputs and unobservable inputs based on the best information available. SFAS No. 157 expands disclosures about the use of fair value to measure assets and liabilities, the effect of these measurements on earnings for the period, and the inputs used to measure fair value. In February 2008, the Financial Accounting Standards Board ( FASB ) issued Staff Position ( FSP ) FAS 157-1 to exclude SFAS No. 13, *Accounting for Leases*, and its related interpretive accounting pronouncements that address leasing transactions, from the scope of SFAS No. 157. In February 2008, the FASB also issued FSP FAS 157-2 to allow entities to electively defer the effective date of SFAS No. 157 for nonfinancial assets and liabilities, except for those items recognized or disclosed at fair value on an annual or more frequently recurring basis, until January 1, 2009. The Company will apply the fair value measurement provisions of SFAS No. 157 to its nonfinancial assets and liabilities measured at fair value effective January 1, 2009. The adoption of SFAS No. 157 had no impact on retained earnings and is not expected to have a material impact on the Company's statements of income and condition.

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### *Fair Value Option*

SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115*, which became effective for the Company on January 1, 2008, provides entities with an option to report selected financial assets and financial liabilities, on an instrument by instrument basis, at fair value. On January 1, 2008, the Company elected the fair value option for its subordinated notes, which are included in long-term debt on the Company's Consolidated Statements of Condition. In adopting the provisions of SFAS No. 159 on January 1, 2008, the Company adjusted the carrying value of the subordinated notes to fair value and recorded an after-tax cumulative-effect adjustment to reduce retained earnings by \$2.7 million. Prospectively, the accounting for the Company's subordinated notes at fair value is not expected to have a material impact on the Company's statements of income and condition.

### *Loan Commitments*

U.S. Securities and Exchange Commission (the SEC) Staff Accounting Bulletin (SAB) No. 109, *Written Loan Commitments Recorded at Fair Value Through Earnings*, which became effective for the Company on January 1, 2008, requires entities to include the expected net future cash flows related to the servicing of the loan in the measurement of written loan commitments that are accounted for at fair value through earnings. The expected net future cash flows from servicing the loan that are to be included in measuring the fair value of the written loan commitment is to be determined in the same manner that the fair value of a recognized servicing asset is measured under SFAS No. 156, *Accounting for Servicing of Financial Assets, an amendment of FASB Statement No. 140*. However, a separate and distinct servicing asset is not recognized for accounting purposes until the servicing rights have been contractually separated from the underlying loan by sale or securitization of the loan with servicing rights retained. The impact of SAB No. 109 was to accelerate the recognition of the estimated fair value of the servicing rights related to the loan from the loan sale date to the loan commitment date. The adoption of SAB No. 109 did not have a material impact on the Company's statements of income and condition.

### *Future Application of Accounting Pronouncements*

In March 2008, the FASB issued SFAS No. 161, *Disclosures About Derivative Instruments and Hedging Activities - an Amendment of FASB Statement No. 133*. SFAS No. 161 expands disclosure requirements regarding an entity's derivative instruments and hedging activities. Expanded qualitative disclosures that will be required under SFAS No. 161 include: (1) how and why an entity uses derivative instruments; (2) how derivative instruments and related hedged items are accounted for under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and related interpretations; and (3) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 also requires several added quantitative disclosures in financial statements. SFAS No. 161 will be effective for the Company on January 1, 2009 and its adoption is not expected to impact the Company's statements of income and condition.

Table of Contents**Note 2. Pension Plans and Postretirement Benefit Plan**

The components of net periodic benefit cost for the Company's pension plans and the postretirement benefit plan for the three and nine months ended September 30, 2008 and 2007 are presented in the following table:

**Pension Plans and Postretirement Benefit Plan (Unaudited)**

| (dollars in thousands)                  | Pension Benefits |               | Postretirement Benefits |                 |
|---|------------------|---------------|-------------------------|-----------------|
|   | 2008             | 2007          | 2008                    | 2007            |
| <b>Three Months Ended September 30,</b> |                  |               |                         |                 |
| Service Cost                            | \$               | \$            | \$ 89                   | \$ 178          |
| Interest Cost                           | 1,298            | 1,223         | 420                     | 412             |
| Expected Return on Plan Assets          | (1,522)          | (1,373)       |                         |                 |
| Amortization of Prior Service Credit    |                  |               | (53)                    | (50)            |
| Recognized Net Actuarial Losses (Gains) | 270              | 450           | (140)                   | (75)            |
| <b>Net Periodic Benefit Cost</b>        | <b>\$ 46</b>     | <b>\$ 300</b> | <b>\$ 316</b>           | <b>\$ 465</b>   |
| <b>Nine Months Ended September 30,</b>  |                  |               |                         |                 |
| Service Cost                            | \$               | \$            | \$ 267                  | \$ 488          |
| Interest Cost                           | 3,893            | 3,669         | 1,260                   | 1,202           |
| Expected Return on Plan Assets          | (4,565)          | (4,119)       |                         |                 |
| Amortization of Prior Service Credit    |                  |               | (159)                   | (150)           |
| Recognized Net Actuarial Losses (Gains) | 810              | 1,350         | (420)                   | (225)           |
| <b>Net Periodic Benefit Cost</b>        | <b>\$ 138</b>    | <b>\$ 900</b> | <b>\$ 948</b>           | <b>\$ 1,315</b> |

The net periodic benefit cost for the Company's pension plans and postretirement benefit plan are recorded as a component of salaries and benefits in the statements of income. The expected 2008 contribution to the Company's pension plans increased to \$7.7 million from \$0.7 million, as previously reported. There were no significant changes from the previously reported \$1.1 million that the Company expects to contribute to the postretirement benefit plan for the year ending December 31, 2008. For the three and nine months ended September 30, 2008, the Company contributed \$7.1 million and \$7.5 million, respectively, to its pension plans. For the three and nine months ended September 30, 2008, the Company contributed \$0.2 million and \$0.9 million, respectively, to its postretirement benefit plan.

**Note 3. Business Segments**

The Company's business segments are defined as Retail Banking, Commercial Banking, Investment Services, and Treasury. The Company's internal management accounting process measures the performance of the business segments based on the management structure of the Company. This process, which is not necessarily comparable with similar information for any other financial institution, uses various techniques to assign balance sheet and income statement amounts to the business segments, including allocations of income, expense, the provision for credit losses, and capital. This process is dynamic and requires certain allocations based on judgment and other subjective factors. Unlike financial accounting, there is no comprehensive authoritative guidance for management accounting that is equivalent to GAAP.



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Selected financial information for each business segment is presented below for the three and nine months ended September 30, 2008 and 2007.

**Business Segments Selected Financial Information (Unaudited)**

| (dollars in thousands)   | <b>Retail<br/>Banking</b> | <b>Commercial<br/>Banking</b> | <b>Investment<br/>Services</b> | <b>Treasury</b>     | <b>Consolidated<br/>Total</b> |
|--|---------------------------|-------------------------------|--------------------------------|---------------------|-------------------------------|
| <b>Three Months Ended</b>  |                           |                               |                                |                     |                               |
| <b>September 30, 2008 <sup>1</sup></b>                             |                           |                               |                                |                     |                               |
| Net Interest Income  | \$ 58,228                 | \$ 36,564                     | \$ 3,922                       | \$ 4,861            | \$ 103,575                    |
| Provision for Credit Losses  | 5,475                     | 13,826                        | 1,089                          | (32)                | 20,358                        |
| Net Interest Income After Provision<br>for Credit Losses           | 52,753                    | 22,738                        | 2,833                          | 4,893               | 83,217                        |
| Noninterest Income   | 27,380                    | 10,508                        | 17,458                         | 1,640               | 56,986                        |
| Noninterest Expense  | (43,709)                  | (24,488)                      | (16,800)                       | (1,793)             | (86,790)                      |
| Income Before Provision for Income<br>Taxes                        | 36,424                    | 8,758                         | 3,491                          | 4,740               | 53,413                        |
| Provision for Income Taxes   | (13,478)                  | (4,686)                       | (1,292)                        | 13,452              | (6,004)                       |
| <b>Allocated Net Income</b>  | <b>\$ 22,946</b>          | <b>\$ 4,072</b>               | <b>\$ 2,199</b>                | <b>\$ 18,192</b>    | <b>\$ 47,409</b>              |
| <b>Total Assets as of September 30,<br/>2008</b>                   | <b>\$ 3,669,924</b>       | <b>\$ 3,023,242</b>           | <b>\$ 285,497</b>              | <b>\$ 3,356,384</b> | <b>\$ 10,335,047</b>          |
| <b>Three Months Ended</b>  |                           |                               |                                |                     |                               |
| <b>September 30, 2007 <sup>2</sup></b>                             |                           |                               |                                |                     |                               |
| Net Interest Income (Loss)   | \$ 56,830                 | \$ 40,352                     | \$ 3,574                       | \$ (2,200)          | \$ 98,556                     |
| Provision for Credit Losses  | 1,773                     | 2,486                         | (1)                            | (188)               | 4,070                         |
| Net Interest Income (Loss) After<br>Provision<br>for Credit Losses | 55,057                    | 37,866                        | 3,575                          | (2,012)             | 94,486                        |
| Noninterest Income   | 26,346                    | 11,442                        | 18,068                         | 5,386               | 61,242                        |
| Noninterest Expense  | (41,653)                  | (22,430)                      | (16,074)                       | (1,293)             | (81,450)                      |
| Income Before Provision for Income<br>Taxes                        | 39,750                    | 26,878                        | 5,569                          | 2,081               | 74,278                        |
| Provision for Income Taxes   | (14,707)                  | (9,948)                       | (2,060)                        | 216                 | (26,499)                      |
| <b>Allocated Net Income</b>  | <b>\$ 25,043</b>          | <b>\$ 16,930</b>              | <b>\$ 3,509</b>                | <b>\$ 2,297</b>     | <b>\$ 47,779</b>              |
| <b>Total Assets as of September 30,<br/>2007 <sup>2</sup></b>      | <b>\$ 3,651,121</b>       | <b>\$ 3,118,106</b>           | <b>\$ 216,795</b>              | <b>\$ 3,563,573</b> | <b>\$ 10,549,595</b>          |
| <b>Nine Months Ended</b>   |                           |                               |                                |                     |                               |
| <b>September 30, 2008 <sup>1</sup></b>                             |                           |                               |                                |                     |                               |
| Net Interest Income  | \$ 176,207                | \$ 122,663                    | \$ 11,731                      | \$ 2,322            | \$ 312,923                    |
| Provision for Credit Losses  | 15,999                    | 25,704                        | 1,089                          | (835)               | 41,957                        |
| Net Interest Income After Provision<br>for Credit Losses           | 160,208                   | 96,959                        | 10,642                         | 3,157               | 270,966                       |
| Noninterest Income   | 83,196                    | 42,753                        | 54,738                         | 22,963              | 203,650                       |
| Noninterest Expense  | (130,813)                 | (72,753)                      | (50,026)                       | (10,492)            | (264,084)                     |
| Income Before Provision for Income<br>Taxes                        | 112,591                   | 66,959                        | 15,354                         | 15,628              | 210,532                       |
| Provision for Income Taxes   | (41,660)                  | (26,273)                      | (5,681)                        | 15,988              | (57,626)                      |
| <b>Allocated Net Income</b>  | <b>\$ 70,931</b>          | <b>\$ 40,686</b>              | <b>\$ 9,673</b>                | <b>\$ 31,616</b>    | <b>\$ 152,906</b>             |
| <b>Total Assets as of September 30,<br/>2008</b>                   | <b>\$ 3,669,924</b>       | <b>\$ 3,023,242</b>           | <b>\$ 285,497</b>              | <b>\$ 3,356,384</b> | <b>\$ 10,335,047</b>          |
| <b>Nine Months Ended</b>   |                           |                               |                                |                     |                               |
| <b>September 30, 2007 <sup>2</sup></b>                             |                           |                               |                                |                     |                               |

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|  |                     |                     |                   |                     |                      |
|--|---------------------|---------------------|-------------------|---------------------|----------------------|
| Net Interest Income (Loss)                     | \$ 166,855          | \$ 120,050          | \$ 10,565         | \$ (1,899)          | \$ 295,571           |
| Provision for Credit Losses                    | 4,576               | 5,700               | (1)               | (211)               | 10,064               |
| Net Interest Income (Loss) After Provision     |                     |                     |                   |                     |                      |
| for Credit Losses                              | 162,279             | 114,350             | 10,566            | (1,688)             | 285,507              |
| Noninterest Income                             | 78,714              | 31,689              | 56,669            | 13,158              | 180,230              |
| Noninterest Expense                            | (124,096)           | (67,667)            | (47,276)          | (4,366)             | (243,405)            |
| Income Before Provision for Income Taxes       | 116,897             | 78,372              | 19,959            | 7,104               | 222,332              |
| Provision for Income Taxes                     | (43,246)            | (28,881)            | (7,385)           | 23                  | (79,489)             |
| <b>Allocated Net Income</b>                    | <b>\$ 73,651</b>    | <b>\$ 49,491</b>    | <b>\$ 12,574</b>  | <b>\$ 7,127</b>     | <b>\$ 142,843</b>    |
| <b>Total Assets as of September 30, 2007 2</b> | <b>\$ 3,651,121</b> | <b>\$ 3,118,106</b> | <b>\$ 216,795</b> | <b>\$ 3,563,573</b> | <b>\$ 10,549,595</b> |

1 Business segment results have been revised for the three and nine months ended September 30, 2008, since reported in the Company's Form 8-K filing on October 27, 2008.

2 Certain prior period information has been reclassified to conform to the current presentation.

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## Note 4. Fair Value of Financial Assets and Liabilities

SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

- Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities 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: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by observable market data by correlation or other means.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

### Assets and Liabilities Measured at Fair Value on a Recurring Basis

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis as of September 30, 2008:

#### Assets and Liabilities Measured at Fair Value on a Recurring Basis (Unaudited)

| (dollars in thousands)                   | Quoted Prices in<br>Active Markets for<br>Identical Assets<br>(Level 1) | Significant Other<br>Observable Inputs<br>(Level 2) | Significant<br>Unobservable Inputs<br>(Level 3) | Total               |
|--|---|---|---|---------------------|
| Investment Securities Trading            | \$  | \$ 90,993   | \$  | \$ 90,993           |
| Investment Securities                    |   |   |   |                     |
| Available-for-Sale                       | 678   | 2,571,433   |   | 2,572,111           |
| Mortgage Servicing Rights                |   |   | 27,057  | 27,057              |
| Other Assets                             | 6,120   |   |   | 6,120               |
| Net Derivative Assets and<br>Liabilities | 606   | 96  | 41  | 743                 |
| <b>Total Assets at Fair Value</b>        | <b>\$ 7,404</b>   | <b>\$ 2,662,522</b>                                 | <b>\$ 27,098</b>                                | <b>\$ 2,697,024</b> |
| Long-Term Debt                           | \$  | \$  | \$ 120,598                                      | \$ 120,598          |
| <b>Total Liabilities at Fair Value</b>   | <b>\$</b>   | <b>\$</b>   | <b>\$ 120,598</b>                               | <b>\$ 120,598</b>   |



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For the three and nine months ended September 30, 2008, the changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

| Assets (Unaudited) (dollars in thousands)   | Investment<br>Securities<br>Available-for-<br>Sale 1 | Mortgage<br>Servicing<br>Rights 2 | Net<br>Derivative<br>Assets and<br>Liabilities 3 | Total      |
|---|--|-----------------------------------|--|------------|
| <b>Three Months Ended September 30, 2008</b>  |  |                                   |  |            |
| <b>Balance as of July 1, 2008</b>   | \$ 25,016  | \$ 30,272                         | \$ 326   | \$ 55,614  |
| Realized and Unrealized Net Gains (Losses):   |  |                                   |  |            |
| Included in Net Income  |  | (3,349)                           | 1,185  | (2,164)    |
| Included in Other Comprehensive Income  | (16)   |                                   |  | (16)       |
| Purchases, Sales, Issuances, and Settlements, Net   | (25,000)   | 134                               | (1,470)  | (26,336)   |
| <b>Balance as of September 30, 2008</b>   | \$   | \$ 27,057                         | \$ 41  | \$ 27,098  |
| <b>Total Unrealized Net Gains (Losses) Included in Net Income Related to Assets Still Held as of September 30, 2008</b> | \$   | \$ (2,894)                        | \$ 41  | \$ (2,853) |

| Liabilities (Unaudited) (dollars in thousands)  | Long-Term<br>Debt 4 | Total      |
|---|---------------------|------------|
| <b>Three Months Ended September 30, 2008</b>  |                     |            |
| <b>Balance as of July 1, 2008</b>   | \$ 121,326          | \$ 121,326 |
| Unrealized Net Gains Included in Net Income   | (728)               | (728)      |
| <b>Balance as of September 30, 2008</b>   | \$ 120,598          | \$ 120,598 |
| <b>Total Unrealized Net Gains Included in Net Income Related to Liabilities Still Held as of September 30, 2008</b> | \$ (728)            | \$ (728)   |

| Assets (Unaudited) (dollars in thousands)   | Investment<br>Securities<br>Available-for-<br>Sale 1 | Mortgage<br>Servicing<br>Rights 2 | Net<br>Derivative<br>Assets and<br>Liabilities 3 | Total      |
|---|--|-----------------------------------|--|------------|
| <b>Nine Months Ended September 30, 2008</b>   |  |                                   |  |            |
| <b>Balance as of January 1, 2008</b>  | \$ 218,980   | \$ 27,588                         | \$ 113   | \$ 246,681 |
| Realized and Unrealized Net Gains (Losses):   |  |                                   |  |            |
| Included in Net Income  |  | (4,248)                           | 4,079  | (169)      |
| Included in Other Comprehensive Income  | 1,012  |                                   |  | 1,012      |
| Purchases, Sales, Issuances, and Settlements, Net   | (219,992)  | 3,717                             | (4,151)  | (220,426)  |
| <b>Balance as of September 30, 2008</b>   | \$   | \$ 27,057                         | \$ 41  | \$ 27,098  |
| <b>Total Unrealized Net Gains (Losses) Included in Net Income Related to Assets Still Held as of September 30, 2008</b> | \$   | \$ (2,241)                        | \$ 41  | \$ (2,200) |

| Liabilities (Unaudited) (dollars in thousands)  | Long-Term<br>Debt 4 | Total      |
|---|---------------------|------------|
| <b>Nine Months Ended September 30, 2008</b>   |                     |            |
| <b>Balance as of January 1, 2008</b>  | \$ 129,032          | \$ 129,032 |
| Unrealized Net Gains Included in Net Income   | (2,434)             | (2,434)    |
| Purchases, Sales, Issuances, and Settlements, Net   | (6,000)             | (6,000)    |
| <b>Balance as of September 30, 2008</b>   | \$ 120,598          | \$ 120,598 |
| <b>Total Unrealized Net Gains Included in Net Income Related to Liabilities Still Held as of September 30, 2008</b> | \$ (2,239)          | \$ (2,239) |

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- 1 Unrealized gains and losses related to investment securities available-for-sale are reported as a component of other comprehensive income.
- 2 Realized and unrealized gains and losses related to mortgage servicing rights are reported as a component of mortgage banking income in the statement of income.
- 3 Realized and unrealized gains and losses related to written loan commitments are reported as a component of mortgage banking income in the statement of income.
- 4 Unrealized gains and losses related to long-term debt are reported as a component of other noninterest income in the statement of income.

There were no transfers in or out of the Company's Level 3 financial assets and liabilities for the three and nine months ended September 30, 2008.

Table of Contents*Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis*

The Company also measures certain financial assets at fair value on a nonrecurring basis in accordance with GAAP. For the three and nine months ended September 30, 2008, there were no adjustments to fair value for the Company's loans held for sale and mortgage servicing rights recorded at amortized cost in accordance with GAAP.

*Fair Value Option*

On January 1, 2008, the Company elected the fair value option for its subordinated notes, which are included in long-term debt on the Company's Consolidated Statements of Condition. The table below reconciles the balance of the Company's subordinated notes as of December 31, 2007 and January 1, 2008.

| <b>(Unaudited)</b>  | <b>(dollars in thousands)</b> | <b>Balance as of<br/>December 31, 2007<sup>1</sup></b> | <b>Net Loss<br/>Upon Adoption</b> | <b>Balance as of<br/>January 1, 2008</b> |
|---|-------------------------------|--|-----------------------------------|--|
| Long-Term Debt  |                               | \$ 124,822   | \$ 4,210                          | \$ 129,032                               |
| Pre-Tax Cumulative-Effect of Adopting the Fair Value Option   |                               |  | 4,210                             |  |
| Increase in Deferred Tax Asset                                |                               |  | (1,474)                           |  |
| After-Tax Cumulative-Effect of Adopting the Fair Value Option |                               |  | \$ 2,736                          |  |

<sup>1</sup> Includes unamortized discount and deferred costs, which were removed from the statement of condition with the cumulative-effect adjustment to adopt the provisions of SFAS No. 159 on January 1, 2008.

The fair value option was elected for the subordinated notes as it provided the Company with an opportunity to better manage its interest rate risk and to achieve balance sheet management flexibility. As of September 30, 2008, the subordinated notes no longer qualified as a component of Total Capital for regulatory capital purposes, due to the maturity being within 12 months from September 30, 2008.

Gains and losses on the subordinated notes subsequent to the initial fair value measurement are recognized in earnings as a component of other noninterest income. For the three and nine months ended September 30, 2008, the Company recorded a gain of \$0.7 million and \$2.4 million, respectively, as a result of the change in fair value of the Company's subordinated notes. Interest expense related to the Company's subordinated notes continues to be measured based on contractual interest rates and reported as such in the statement of income.

The following reflects the difference between the fair value carrying amount of the Company's subordinated notes and the aggregate unpaid principal amount the Company is contractually obligated to pay until maturity as of September 30, 2008.

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|                                       |                        | Fair Value            | Aggregate Unpaid       | Excess of Fair Value  |
|---------------------------------------|------------------------|-----------------------|------------------------|-----------------------|
|                                       |                        | Carrying Amount as of | Principal Amount as of | Carrying Amount       |
| (Unaudited)                           | (dollars in thousands) | September 30, 2008    | September 30, 2008     | Over Aggregate Unpaid |
|                                       |                        |                       |                        | Principal Balance     |
| Long-Term Debt Reported at Fair Value |                        | \$ 120,598            | \$ 118,971             | \$ 1,627              |

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**Note 5. Lease Transaction**

In March 2008, the lessee in an aircraft leveraged lease exercised its early buyout option resulting in an \$11.6 million pre-tax gain for the Company. This gain on the sale of the Company's equity interest in the lease was recorded as a component of other noninterest income in the statement of income. This sale also resulted in a benefit for income taxes of \$1.4 million from the adjustment of previously recognized tax liabilities. After-tax gains from this transaction were \$13.0 million.

**Note 6. Income Taxes**

*Lease In-Lease Out ( LILO ) and Sale In-Lease Out ( SILO ) Transactions*

During the years 1998 through 2002, the Company entered into one leveraged lease transaction known as a LILO transaction and five leveraged lease transactions known as SILO transactions. In August 2008, the Internal Revenue Service (the IRS) publicly released a general settlement initiative for identified participants, including the Company, in LILO and SILO transactions that would disallow 80% of previously claimed income tax deductions through December 31, 2007 but offered relief from penalties that might have otherwise been imposed. The Company accepted the settlement initiative from the IRS in October 2008. In accordance with the terms of the settlement initiative, the Company will consider December 31, 2008 to be the deemed termination date of the SILO transactions for income tax purposes. With the effective settlement of the SILO transactions at a disallowance percentage of less than its original estimate, the Company recalculated the total and periodic income from the SILO transactions from the inception of the lease through December 31, 2008. The Company remeasured its income tax liabilities in accordance with FASB Interpretation No. (FIN) 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109*, and its lease financing interest income in accordance with SFAS No. 13 and recorded a net gain of \$8.9 million in September 2008. This amount was comprised of a \$4.0 million decrease to lease financing interest income and a \$12.9 million credit to the provision for income taxes.

The Company previously reached an agreement with the IRS in June 2007 as to the terms of the settlement of the issues related to the Company's LILO transaction. As a result, the general settlement initiative released by the IRS in August 2008 had no impact on the LILO transaction which had previously been effectively settled.

As a result of the Company accepting the settlement initiative from the IRS related to the SILO transactions, the Company decreased its liability for unrecognized tax benefits (UTBs) by \$115.5 million during the three months ended September 30, 2008. As of September 30, 2008, all of the \$14.1 million in the Company's remaining liability for UTBs was related to UTBs that if reversed would have an impact on the Company's effective tax rate.

Table of Contents*Effective Tax Rate*

The following is a reconciliation of the statutory federal income tax rate to the effective tax rate for the three and nine months ended September 30, 2008 and 2007.

| (Unaudited)                                     | Three Months Ended<br>September 30, |               | Nine Months Ended<br>September 30, |               |
|---|-------------------------------------|---------------|------------------------------------|---------------|
|   | 2008                                | 2007          | 2008                               | 2007          |
| Statutory Federal Income Tax Rate               | 35.00%                              | 35.00%        | 35.00%                             | 35.00%        |
| Increase (Decrease) in Tax Rate Resulting From: |                                     |               |                                    |               |
| State Income Tax, Net of Federal Income Tax     | 5.47                                | 3.13          | 4.95                               | 3.54          |
| Foreign Tax Credits                             |                                     | (1.07)        |                                    | (1.08)        |
| Low Income Housing Investments                  | (0.14)                              | (0.14)        | (0.19)                             | (0.14)        |
| Bank-Owned Life Insurance                       | (1.59)                              | (0.92)        | (1.04)                             | (0.91)        |
| Leveraged Leases                                | (23.80)                             | (0.08)        | (9.69)                             | (0.36)        |
| Other   | (3.70)                              | (0.24)        | (1.66)                             | (0.30)        |
| <b>Effective Tax Rate</b>                       | <b>11.24%</b>                       | <b>35.68%</b> | <b>27.37%</b>                      | <b>35.75%</b> |

The lower effective tax rate for the three months ended September 30, 2008 compared to the three months ended September 30, 2007 was primarily due to the SILO deemed termination gain. The lower effective tax rate for the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007 was also due to the SILO deemed termination gain and the sale of the Company's equity interest in an aircraft leveraged lease in March 2008. The pre-tax gain from the aircraft sale would have resulted in an income tax expense of approximately \$4.6 million, based on statutory income tax rates. However, due to the timing of the sale of the Company's equity interest and the adjustment of previously recognized income tax liabilities, this transaction resulted in a \$1.4 million income tax benefit to the Company. As a result, the total income tax benefit from this transaction was approximately \$6.0 million. The income tax benefit from both of these transactions is reflected in the leveraged leases line item in the table above.

**Note 7. Contingencies***Parent Support of Money Market Mutual Fund*

The Bank provides investment advisory services to the Pacific Capital Funds' family of mutual funds. Due to the illiquidity and turmoil in the credit markets and money market mutual fund industry in the three months ended September 30, 2008, three investments made by the Pacific Capital Cash Assets Trust Fund (the "Fund"), an SEC registered money market mutual fund regulated under Rule 2a-7 of the Investment Company Act of 1940, measured at fair market value which was estimated at less than amortized cost during this period. For the three months ended September 30, 2008, the Parent pledged overnight support to the Fund on 11 days in amounts ranging from \$0.7 million to \$8.0 million in order to maintain the asset value of the Fund at a minimum of \$1.00. As of September 30, 2008, the Parent's pledge to the Fund was \$2.3 million. This support was not contractually required and was provided at the sole discretion of the Parent. As of September 30, 2008, management does not believe that the Parent will absorb the majority of the expected future risks associated with the Fund's assets, including interest rate, liquidity, credit, and other relevant risks that are expected to impact the value of the underlying assets of the Fund. As a result, as of September 30, 2008,

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management believes that on-balance sheet accounting treatment for the supported Fund is not required.

During October 2008, the Parent continued to pledge overnight support to the Fund in amounts within the range noted above. As of October 24, 2008, the Parent's pledge to the Fund was \$1.9 million.

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*Visa Litigation*

In October 2007, Visa, Inc. ( "Visa" ) announced that it had completed a series of restructuring transactions in preparation for its initial public offering ( "IPO" ) planned for the first quarter of 2008. As part of this restructuring, the Company received approximately 0.9 million shares of restricted Class USA stock in Visa in exchange for the Company's membership interests. The Company did not recognize a gain or loss upon the receipt of Class USA shares in October 2007. Visa completed its IPO in March 2008, resulting in the conversion of the Company's Class USA shares to approximately 0.8 million shares of Class B common stock in Visa. Visa exercised its option to mandatorily redeem approximately 0.3 million shares of the Company's Class B common stock in Visa in exchange for cash, which resulted in the Company recording a \$13.7 million gain in other noninterest income in the first quarter of 2008. The Company's remaining Class B shares (approximately 0.5 million) in Visa are restricted for a period of three years after the IPO or upon settlement of litigation claims, whichever is later. The Company has not recognized a gain or loss on the remaining Class B shares in Visa. Concurrent with its IPO, Visa funded an escrow account to cover litigation claims and settlements as discussed below.

In November 2007, Visa announced that it had reached an agreement with American Express, related to its claim that Visa and its member banks had illegally blocked American Express from the bank-issued card business in the United States. The Company was not a named defendant in the lawsuit and, therefore, was not directly liable for any amount of the settlement. However, according to an interpretation of Visa's by-laws, the Company and other Visa U.S.A., Inc. (a wholly-owned subsidiary of Visa) members are obligated to indemnify Visa for certain losses, including the settlement of the American Express matter. The Company's indemnification obligation is limited to its proportionate interest in Visa U.S.A., Inc. In December 2007, as a result of Visa's agreement with American Express, the Company established a liability of \$4.3 million for this indemnification obligation. However, as a result of Visa's IPO and funding of the escrow account, the Company reversed the \$4.3 million liability previously established and recorded a credit to other noninterest expense in March 2008.

Other litigation covered by the Company's indemnification of Visa and expected to be settled from the escrow account include: 1) a lawsuit filed by Discover Financial Services, Inc. ( "Discover" ) claiming that Visa prevented banks from issuing payment cards on the Discover network; 2) class action lawsuits filed on behalf of merchants who accept payment cards against Visa U.S.A., Inc. claiming that the setting of interchange is unlawful, among other claims; and 3) a consumer class action lawsuit against Visa U.S.A., Inc., Visa International, and MasterCard alleging unfair competition. In December 2007, the Company established a liability of \$1.3 million related to the indemnification of Visa in the Discover lawsuit. However, as a result of Visa's IPO and funding of the escrow account, the Company reversed the \$1.3 million liability previously established and recorded a credit to other noninterest expense in March 2008. Our indemnification of Visa, related to the costs of the class action lawsuits, if any, is expected to be funded from the Visa escrow account prior to any additional liability being incurred by the Company.

In October 2008, Visa announced a settlement of approximately \$1.9 billion with Discover, which is subject to approval by Visa's former U.S. member financial institutions. Management is in the process of analyzing the terms of the settlement and potential impact to the Company.

In addition to the Visa litigation, the Company is subject to various other pending and threatened legal proceedings arising out of the normal course of business or operations. Management believes that current legal reserves are adequate and the amount of an incremental liability, if any, arising from these matters is not expected to have a material adverse effect on the Company's financial condition or results of operations.



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

### Forward-Looking Statements

This report contains, and other written or oral statements made by the Company may contain, forward-looking statements concerning, among other things, the economic and business environment in our service area and elsewhere, credit quality, and other financial and business matters in future periods. Our forward-looking statements are based on numerous assumptions, any of which could prove to be inaccurate and actual results may differ materially from those projected because of a variety of risks and uncertainties, including, but not limited to: 1) general economic conditions are less favorable than expected; 2) competitive pressure among financial services and products; 3) the impact of legislation and the regulatory environment; 4) fiscal and monetary policies of the markets in which we operate; 5) actual or alleged conduct which could harm our reputation; 6) changes in accounting standards; 7) changes in tax laws or regulations or the interpretation of such laws and regulations; 8) changes in our credit quality or risk profile that may increase or decrease the required level of our reserve for credit losses; 9) changes in market interest rates that may affect our credit markets and ability to maintain our net interest margin; 10) unpredicted costs and other consequences of legal or regulatory matters involving the Company; 11) changes to the amount and timing of proposed common stock repurchases; and 12) geopolitical risk, military or terrorist activity, natural disaster, adverse weather, public health, and other conditions impacting us and our customers' operations. For a detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements, refer to the section entitled "Risk Factors" in Part I of the Company's Annual Report on Form 10-K for the year ended December 31, 2007, and subsequent periodic and current reports, filed with the U.S. Securities and Exchange Commission (the "SEC"). Words such as "believes," "anticipates," "expects," "intends," "targeted," and similar expressions are intended to identify forward-looking statements but are not exclusive means of identifying such statements. We do not undertake an obligation to update forward-looking statements to reflect later events or circumstances.

### Overview

*General*

Bank of Hawaii Corporation (the *Parent* ) is a bank holding company headquartered in Honolulu, Hawaii. The Parent's principal and only operating subsidiary is Bank of Hawaii (the *Bank* ).

The Bank, directly and through its subsidiaries, provides a broad range of financial services and products primarily to customers in Hawaii and the Pacific Islands (Guam, nearby islands, and American Samoa). References to *we*, *our*, *us*, or the *Company*, refer to the holding company and its subsidiaries that are consolidated for financial reporting purposes.

*2007+ Plan*

Our governing objective is to maximize shareholder value over time.

In January 2007, we introduced our 2007+ Plan ( *Plan* ) to our shareholders, customers, and employees. Our Plan, which we continue to follow in 2008, focuses on five strategic themes:

- Growth
- Integration
- People
- Brand
- Discipline



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# Plan Financial Objectives and Financial Results

Our Plan was prepared with the expectation that economic growth in Hawaii could slow in 2007 and beyond. Our Plan was based on assumptions of moderate growth in revenues and consistent, positive operating leverage. Our Plan also allowed us to adjust for economic softness as we became increasingly conservative in 2008. Our Plan is to grow with the markets that we serve, while maintaining our conservative risk profile. The following summarizes our Plan financial objectives compared with our financial results for the first nine months of 2008:

## Plan Financial Objectives and Financial Results

| Performance Ratios | Plan Financial Objectives | Nine Months Ended Sept. 30, 2008 |
|--------------------|---------------------------|----------------------------------|
| Average ROA        | Above 1.70%               | 1.95%                            |
| Average ROE        | Above 25.00%              | 26.26%                           |
| Efficiency Ratio   | Approaching 50.00%        | 51.12%                           |
| Operating Leverage | Positive                  | 8.65%                            |

We achieved our primary performance objectives for the first nine months of 2008, in spite of a slowing economy in Hawaii and the Mainland U.S.

The following transactions affected our financial results for the third quarter of 2008 compared to the same period in 2007:

- \$5.0 million increase in net interest income, despite a \$4.0 million decrease in lease financing interest income due to our acceptance of the settlement initiative from the Internal Revenue Service (the IRS) related to our Sale-In Lease-Out (SILO) transactions;
- \$16.3 million increase in the provision for credit losses (the Provision). The Provision was recorded to maintain the allowance for loan and lease losses (the Allowance) at levels adequate to cover our estimate of probable credit losses as of September 30, 2008. The increase in the Allowance was primarily due to heightened risk in three specific loan exposures and to general risk from the weakening economy in Hawaii and the Mainland U.S.; and
- \$20.5 million decrease in the provision for income taxes primarily as a result of a \$12.9 million benefit for income taxes due to our acceptance of the settlement initiative from the IRS related to our SILO transactions.

Our strong financial performance for the first nine months of 2008 was primarily due to a \$17.4 million increase in net interest income. Our performance was enhanced by two transactions recorded in the first quarter of 2008:

- \$13.7 million pre-tax gain resulting from the mandatory redemption of our Visa, Inc. (Visa) shares, as well as a \$5.6 million reversal of previously recorded contingency accruals related to Visa legal matters; and
- \$11.6 million pre-tax gain resulting from the sale of our equity interest in an aircraft lease. This sale also resulted in a net benefit for income taxes from the adjustment of previously recognized tax liabilities. After-tax gains from this transaction were \$13.0 million.

For the first nine months of 2008 compared to the same period in 2007, the increase in net interest income and the effect of the two transactions noted above were partially offset by the following:

- \$31.9 million increase in the Provision was recorded to maintain the Allowance at levels adequate to cover our estimate of probable credit losses as of September 30, 2008;
- \$9.2 million increase in incentive compensation expense for employees related to cash awards to encourage the purchase of our stock and other earnings-based incentive compensation;
- \$3.0 million increase in our reserves for contingencies, which reflects our on-going evaluation of potential losses related to pending litigation, claims, and assessments; and
- \$2.3 million increase in our contributions to the Bank of Hawaii Charitable Foundation and other charitable organizations.





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Table 1 presents our financial highlights for the three and nine months ended September 30, 2008 and 2007 and as of September 30, 2008, December 31, 2007, and September 30, 2007.

## Financial Highlights (Unaudited)

|  | Three Months Ended<br>September 30, |                      | Nine Months Ended<br>September 30, |              |
|--|-------------------------------------|----------------------|------------------------------------|--------------|
|  | 2008                                | 2007                 | 2008                               | 2007         |
| (dollars in thousands, except per share amounts) |                                     |                      |                                    |              |
| <b>For the Period:</b>                           |                                     |                      |                                    |              |
| Net Interest Income                              | \$ 103,575                          | \$ 98,556            | \$12,923                           | \$ 295,571   |
| Provision for Credit Losses                      | 20,358                              | 4,070                | 41,957                             | 10,064       |
| Total Noninterest Income                         | 56,986                              | 61,242               | 203,650                            | 180,230      |
| Total Noninterest Expense                        | 86,790                              | 81,450               | 264,084                            | 243,405      |
| Net Income                                       | 47,409                              | 47,779               | 152,906                            | 142,843      |
| Basic Earnings Per Share                         | 1.00                                | 0.98                 | 3.20                               | 2.90         |
| Diluted Earnings Per Share                       | 0.99                                | 0.96                 | 3.17                               | 2.86         |
| Dividends Declared Per Share                     | 0.44                                | 0.41                 | 1.32                               | 1.23         |
| Net Income to Average Total Assets               | 1.82%                               | 1.79%                | 1.95%                              | 1.82%        |
| Net Income to Average Shareholders Equity        | 24.17                               | 26.02                | 26.26                              | 26.43        |
| Efficiency Ratio 1                               | 54.05                               | 50.97                | 51.12                              | 51.16        |
| Operating Leverage 2                             | (12.02)                             | 1.65                 | 8.65                               | 2.97         |
| Net Interest Margin 3                            | 4.33                                | 4.03                 | 4.30                               | 4.07         |
| Dividend Payout Ratio 4                          | 44.00                               | 41.84                | 41.25                              | 42.41        |
| Effective Tax Rate                               | 11.24                               | 35.68                | 27.37                              | 35.75        |
| Average Loans and Leases                         | \$ 6,512,453                        | \$ 6,570,261         | \$6,443,871                        | \$ 6,554,979 |
| Average Assets                                   | 10,339,490                          | 10,576,565           | 10,495,367                         | 10,480,803   |
| Average Deposits                                 | 7,772,535                           | 8,015,594            | 7,893,972                          | 7,916,061    |
| Average Shareholders Equity                      | 780,334                             | 728,372              | 777,650                            | 722,522      |
| Average Shareholders Equity to Average Assets    | 7.55%                               | 6.89%                | 7.41%                              | 6.89%        |
| <b>Market Price Per Share of Common Stock:</b>   |                                     |                      |                                    |              |
| Closing  | \$ 53.45                            | \$ 52.85             | \$ 53.45                           | \$ 52.85     |
| High   | 70.00                               | 55.84                | 70.00                              | 55.84        |
| Low  | 37.46                               | 46.05                | 37.46                              | 46.05        |
|  | September 30,<br>2008               | December 31,<br>2007 | September 30,<br>2007              |              |
| <b>As of Period End:</b>                         |                                     |                      |                                    |              |
| Loans and Leases                                 | \$ 6,539,458                        | \$6,580,861          | \$ 6,599,915                       |              |
| Total Assets                                     | 10,335,047                          | 10,472,942           | 10,549,595                         |              |
| Total Deposits                                   | 7,658,484                           | 7,942,372            | 7,875,166                          |              |
| Long-Term Debt                                   | 204,616                             | 235,371              | 235,350                            |              |
| Total Shareholders Equity                        | 780,020                             | 750,255              | 731,697                            |              |
| Non-Performing Assets                            | \$ 5,927                            | \$ 5,286             | \$ 4,260                           |              |
| Allowance to Loans and Leases Outstanding        |                                     | 1.77%                | 1.38%                              | 1.38%        |
| Leverage Ratio 5                                 |                                     | 7.27                 | 7.02                               | 6.92         |
| Book Value Per Common Share                      | \$ 16.35                            | \$ 15.44             | \$ 14.91                           |              |

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|                                |       |       |       |
|--------------------------------|-------|-------|-------|
| Full-Time Equivalent Employees | 2,573 | 2,594 | 2,572 |
| Branches and Offices           | 84    | 83    | 83    |

1 Efficiency ratio is defined as noninterest expense divided by total revenue (net interest income and total noninterest income).

2 Operating leverage is defined as the percentage change in income before the provision for credit losses and the provision for income taxes. Measures are presented on a linked quarter basis.

3 Net interest margin is defined as net interest income, on a taxable equivalent basis, as a percentage of average earning assets.

4 Dividend payout ratio is defined as dividends declared per share divided by basic earnings per share.

5 Leverage ratio as of December 31, 2007 and September 30, 2007 was corrected from 7.04% and 6.95%, respectively.

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### Recent Government Initiatives

The Federal government and organizations have announced a number of programs to relieve distress in the financial markets, including the Emergency Economic Stabilization Act of 2008. We are evaluating the programs to determine our level of participation, if any.

### Recent Accounting Changes

We applied the provisions of the following new accounting pronouncements on January 1, 2008:

- Statement of Financial Accounting Standards ( SFAS ) No. 157, *Fair Value Measurements*;
- SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115*; and
- SEC Staff Accounting Bulletin ( SAB ) No. 109, *Written Loan Commitments Recorded at Fair Value Through Earnings*.

SFAS No. 157 had no impact on retained earnings and is not expected to have a material impact on our statements of income and condition. We have not made material changes to our valuation methodologies as previously disclosed in our financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2007. Our financial assets and liabilities do not require the use of a significant amount of unobservable (Level 3) inputs to estimate fair value.

SFAS No. 159 had the effect of reducing retained earnings by \$2.7 million as of January 1, 2008, as we elected the fair value option for our subordinated notes. See Notes 1 and 4 to our Consolidated Financial Statements (Unaudited) for more information on our application of SFAS No. 157 and 159.

SAB No. 109 had the effect of accelerating gain recognition of the estimated fair value of the servicing rights related to the loan from the loan sale date to the loan commitment date. The implementation of SAB No. 109 did not have a material impact on our statements of income and condition.



Table of Contents**Analysis of Statements of Income***Net Interest Income*

Average balances, related income and expenses, and resulting yields and rates, on a taxable equivalent basis, are presented in Table 2 for the three and nine months ended September 30, 2008 and 2007. An analysis of the change in net interest income, on a taxable equivalent basis, for the first nine months of 2008 compared to the same period in 2007, is presented in Table 3.

| (dollars in millions)               | Average Balances and Interest Rates - Taxable Equivalent Basis (Unaudited) |                    |                |  |                    |                |   |                    |                | Table 2                                   |                    |                |
|-------------------------------------|--|--------------------|----------------|--|--------------------|----------------|---|--------------------|----------------|---|--------------------|----------------|
|                                     | Three Months Ended<br>September 30, 2008                                   |                    |                | Three Months Ended<br>September 30, 2007 1 |                    |                | Nine Months Ended<br>September 30, 2008 |                    |                | Nine Months Ended<br>September 30, 2007 1 |                    |                |
|                                     | Average<br>Balance   | Income/<br>Expense | Yield/<br>Rate | Average<br>Balance                         | Income/<br>Expense | Yield/<br>Rate | Average<br>Balance                      | Income/<br>Expense | Yield/<br>Rate | Average<br>Balance                        | Income/<br>Expense | Yield/<br>Rate |
| <b>Earning Assets</b>               |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Interest-Bearing                    |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Deposits                            | \$ 6.4   | \$                 | 2.06%          | \$ 79.8                                    | \$ 1.1             | 5.35%          | \$ 22.2                                 | \$ 0.4             | 2.56%          | \$ 31.1                                   | \$ 1.2             | 5.29%          |
| Funds Sold                          | 28.4   | 0.1                | 1.96           | 86.2                                       | 1.1                | 5.01           | 82.6                                    | 1.6                | 2.47           | 69.3                                      | 2.7                | 5.12           |
| Investment Securities               |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Trading                             | 92.6   | 1.2                | 5.07           | 111.3                                      | 1.1                | 4.00           | 95.3                                    | 3.5                | 4.96           | 136.6                                     | 4.1                | 3.99           |
| Available-for-Sale                  | 2,601.2  | 35.4               | 5.44           | 2,556.7                                    | 33.7               | 5.28           | 2,627.5                                 | 105.5              | 5.35           | 2,499.3                                   | 96.7               | 5.16           |
| Held-to-Maturity                    | 255.4  | 2.9                | 4.50           | 318.0                                      | 3.6                | 4.55           | 270.1                                   | 9.1                | 4.51           | 339.3                                     | 11.5               | 4.52           |
| Loans Held for Sale                 | 6.6  | 0.1                | 6.34           | 7.3  | 0.1                | 6.78           | 8.8                                     | 0.4                | 5.79           | 9.4                                       | 0.5                | 6.41           |
| Loans and Leases 2                  |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Commercial and                      |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Industrial                          | 1,049.7  | 13.8               | 5.23           | 1,048.9                                    | 19.7               | 7.45           | 1,058.5                                 | 44.6               | 5.64           | 1,059.3                                   | 59.0               | 7.45           |
| Commercial Mortgage                 | 695.3  | 10.5               | 6.04           | 627.8                                      | 10.8               | 6.82           | 669.2                                   | 31.1               | 6.21           | 621.5                                     | 31.7               | 6.82           |
| Construction                        | 161.4  | 2.3                | 5.67           | 262.2                                      | 5.3                | 8.00           | 179.4                                   | 8.2                | 6.09           | 253.9                                     | 15.1               | 7.97           |
| Commercial Lease                    |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Financing                           | 472.9  | 0.2                | 0.15           | 479.4                                      | 3.6                | 2.98           | 473.8                                   | 8.3                | 2.33           | 467.7                                     | 11.0               | 3.15           |
| Residential Mortgage                | 2,500.0  | 37.8               | 6.04           | 2,502.2                                    | 38.5               | 6.15           | 2,509.5                                 | 114.5              | 6.09           | 2,499.4                                   | 114.9              | 6.13           |
| Home Equity                         | 975.3  | 14.2               | 5.79           | 946.2                                      | 18.3               | 7.67           | 971.6                                   | 44.3               | 6.09           | 943.3                                     | 53.9               | 7.64           |
| Automobile                          | 403.6  | 8.2                | 8.09           | 433.0                                      | 9.0                | 8.23           | 421.7                                   | 25.7               | 8.14           | 427.9                                     | 26.1               | 8.16           |
| Other 3                             | 254.3  | 5.6                | 8.80           | 270.6                                      | 7.5                | 11.05          | 260.2                                   | 18.0               | 9.22           | 282.0                                     | 22.9               | 10.85          |
| Total Loans and Leases              | 6,512.5  | 92.6               | 5.67           | 6,570.3                                    | 112.7              | 6.82           | 6,543.9                                 | 294.7              | 6.01           | 6,555.0                                   | 334.6              | 6.82           |
| Other                               | 79.6   | 0.5                | 2.46           | 79.4                                       | 0.4                | 1.83           | 79.6                                    | 1.4                | 2.35           | 79.4                                      | 1.1                | 1.78           |
| <b>Total Earning Assets</b>         |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| <b>4</b>                            | 9,582.7  | 132.8              | 5.53           | 9,809.0                                    | 153.8              | 6.25           | 9,730.0                                 | 416.6              | 5.71           | 9,719.4                                   | 452.4              | 6.21           |
| Cash and                            |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Noninterest-Bearing                 |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Deposits                            | 274.3  |                    |                | 285.3                                      |                    |                | 280.4                                   |                    |                | 290.3                                     |                    |                |
| Other Assets                        | 482.5  |                    |                | 482.3                                      |                    |                | 485.0                                   |                    |                | 471.1                                     |                    |                |
| <b>Total Assets</b>                 | <b>\$ 10,339.5</b>   |                    |                | <b>\$ 10,576.6</b>                         |                    |                | <b>\$ 10,495.4</b>                      |                    |                | <b>\$ 10,480.8</b>                        |                    |                |
| <b>Interest-Bearing Liabilities</b> |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Interest-Bearing                    |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Deposits                            |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Demand                              | \$ 1,827.9   | 1.5                | 0.32           | \$ 1,557.7                                 | 4.0                | 1.01           | \$ 1,686.9                              | 4.9                | 0.39           | \$ 1,580.2                                | 12.3               | 1.04           |
| Savings                             | 2,755.4  | 6.3                | 0.91           | 2,837.5                                    | 15.9               | 2.23           | 2,750.9                                 | 22.1               | 1.07           | 2,702.5                                   | 41.1               | 2.03           |
| Time                                | 1,594.8  | 9.9                | 2.48           | 1,742.0                                    | 17.7               | 4.03           | 1,662.6                                 | 38.4               | 3.09           | 1,727.3                                   | 51.3               | 3.97           |
| Total Interest-Bearing              |  |                    |                |  |                    |                |   |                    |                |   |                    |                |
| Deposits                            | 6,178.1  | 17.7               | 1.14           | 6,137.2                                    | 37.6               | 2.43           | 6,100.4                                 | 65.4               | 1.43           | 6,010.0                                   | 104.7              | 2.33           |

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|   |             |         |      |             |         |      |             |         |      |             |       |      |
|---|-------------|---------|------|-------------|---------|------|-------------|---------|------|-------------|-------|------|
| Short-Term Borrowings                             | 116.7       | 0.5     | 1.74 | 138.8       | 1.8     | 4.91 | 86.0        | 1.5     | 2.25 | 112.0       | 4.3   | 5.06 |
| Securities Sold Under Agreements to Repurchase    | 1,077.4     | 7.7     | 2.80 | 1,016.5     | 11.7    | 4.54 | 1,100.5     | 25.8    | 3.10 | 1,042.1     | 35.2  | 4.49 |
| Long-Term Debt                                    | 205.1       | 3.1     | 6.04 | 251.9       | 3.9     | 6.22 | 223.0       | 10.3    | 6.16 | 257.5       | 11.9  | 6.15 |
| <b>Total Interest-Bearing Liabilities</b>         | 7,577.3     | 29.0    | 1.52 | 7,544.4     | 55.0    | 2.89 | 7,509.9     | 103.0   | 1.83 | 7,421.6     | 156.1 | 2.81 |
| <b>Net Interest Income</b>                        | \$ 103.8    |         |      | \$ 98.8     |         |      | \$ 313.6    |         |      | \$ 296.3    |       |      |
| Interest Rate Spread                              | 4.01%       |         |      | 3.36%       |         |      | 3.88%       |         |      | 3.40%       |       |      |
| Net Interest Margin                               | 4.33%       |         |      | 4.03%       |         |      | 4.30%       |         |      | 4.07%       |       |      |
| Noninterest-Bearing                               |             |         |      |             |         |      |             |         |      |             |       |      |
| Demand Deposits                                   | 1,594.4     | 1,878.4 |      |             | 1,793.5 |      |             | 1,906.0 |      |             |       |      |
| Other Liabilities                                 | 387.5       | 425.4   |      |             | 414.3   |      |             | 430.7   |      |             |       |      |
| Shareholders' Equity                              | 780.3       | 728.4   |      |             | 777.7   |      |             | 722.5   |      |             |       |      |
| <b>Total Liabilities and Shareholders' Equity</b> | \$ 10,339.5 |         |      | \$ 10,576.6 |         |      | \$ 10,495.4 |         |      | \$ 10,480.8 |       |      |

1 Certain prior period information has been reclassified to conform to the current presentation.

2 Non-performing loans and leases are included in the respective average loan and lease balances. Income, if any, on such loans and leases is recognized on a cash basis.

3 Comprised of other consumer revolving credit, installment, and consumer lease financing.

4 Interest income includes taxable equivalent basis adjustments, based upon a federal statutory tax rate of 35%, of \$234,000 and \$237,000 for the three months ended September 30, 2008 and 2007, respectively, and \$711,000 and \$686,000 for the nine months ended September 30, 2008 and 2007, respectively.

Table of Contents**Analysis of Change in Net Interest Income - Taxable Equivalent Basis (Unaudited)****Table 3****Nine Months Ended September 30, 2008  
Compared to September 30, 2007**

| (dollars in millions)                          | Volume 1      | Rate 1         | Time 1        | Total          |
|--|---------------|----------------|---------------|----------------|
| <b>Change in Interest Income:</b>              |               |                |               |                |
| Interest-Bearing Deposits                      | \$ (0.3)      | \$ (0.5)       | \$            | \$ (0.8)       |
| Funds Sold                                     | 0.5           | (1.6)          |               | (1.1)          |
| Investment Securities                          |               |                |               |                |
| Trading  | (1.4)         | 0.8            |               | (0.6)          |
| Available-for-Sale                             | 5.1           | 3.7            |               | 8.8            |
| Held-to-Maturity                               | (2.4)         |                |               | (2.4)          |
| Loans Held for Sale                            |               | (0.1)          |               | (0.1)          |
| Loans and Leases                               |               |                |               |                |
| Commercial and Industrial                      | (0.1)         | (14.5)         | 0.2           | (14.4)         |
| Commercial Mortgage                            | 2.3           | (3.0)          | 0.1           | (0.6)          |
| Construction                                   | (3.9)         | (3.1)          | 0.1           | (6.9)          |
| Commercial Lease Financing                     | 0.1           | (2.8)          |               | (2.7)          |
| Residential Mortgage                           | 0.4           | (0.8)          |               | (0.4)          |
| Home Equity                                    | 1.6           | (11.4)         | 0.2           | (9.6)          |
| Automobile                                     | (0.4)         | (0.1)          | 0.1           | (0.4)          |
| Other 2  | (1.7)         | (3.3)          | 0.1           | (4.9)          |
| Total Loans and Leases                         | (1.7)         | (39.0)         | 0.8           | (39.9)         |
| Other  |               | 0.3            |               | 0.3            |
| <b>Total Change in Interest Income</b>         | <b>(0.2)</b>  | <b>(36.4)</b>  | <b>0.8</b>    | <b>(35.8)</b>  |
| <b>Change in Interest Expense:</b>             |               |                |               |                |
| Interest-Bearing Deposits                      |               |                |               |                |
| Demand   | 0.8           | (8.2)          |               | (7.4)          |
| Savings  | 0.7           | (19.9)         | 0.2           | (19.0)         |
| Time   | (1.9)         | (11.2)         | 0.2           | (12.9)         |
| Total Interest-Bearing Deposits                | (0.4)         | (39.3)         | 0.4           | (39.3)         |
| Short-Term Borrowings                          | (0.8)         | (2.0)          |               | (2.8)          |
| Securities Sold Under Agreements to Repurchase | 1.9           | (11.4)         | 0.1           | (9.4)          |
| Long-Term Debt                                 | (1.6)         |                |               | (1.6)          |
| <b>Total Change in Interest Expense</b>        | <b>(0.9)</b>  | <b>(52.7)</b>  | <b>0.5</b>    | <b>(53.1)</b>  |
| <b>Change in Net Interest Income</b>           | <b>\$ 0.7</b> | <b>\$ 16.3</b> | <b>\$ 0.3</b> | <b>\$ 17.3</b> |

<sup>1</sup> The changes for each category of interest income and expense are allocated between the portion of changes attributable to the variance in volume, rate, and time for that category.

<sup>2</sup> Comprised of other consumer revolving credit, installment, and consumer lease financing.



The increase in net interest income, on a taxable equivalent basis, and net interest margin was the result of lower funding costs and the effects of a steeper yield curve in 2008.

Rates paid on interest-bearing deposits decreased by 129 basis points in the third quarter of 2008 and by 90 basis points in the first nine months of 2008 compared to the same periods in 2007. Also contributing to our lower funding costs was a decrease in rates paid on securities sold under agreements to repurchase by 174 basis points in the third quarter of 2008 and by 139 basis points in the first nine months of 2008 compared to the same periods in 2007. The decrease in our funding costs was reflective of lower short-term interest rates in 2008

compared to 2007. Yields on our available-for-sale investment securities were 16 basis points higher in the third quarter of 2008 and 19 basis points higher in the first nine months of 2008 compared to the same periods in 2007. These increases reflected our ability to reinvest funds in higher yielding investment securities, due to favorable movements in interest rates. Partially offsetting the decrease in our funding costs and higher yields on our available-for-sale investment securities was a decrease in yields on our loans and leases, in all categories. Yields on our loans and leases decreased by 115 basis points in the third quarter of 2008 and by 81 basis points in the first nine months of 2008 compared to the



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same periods in 2007. Lower yields in our commercial and industrial, construction, and home equity loans in the third quarter and first nine months of 2008 compared to the same periods in 2007 were primarily driven by the decline in short-term interest rates over this period. Yields on our commercial lease financing portfolio decreased by 283 basis points in the third quarter of 2008 and by 82 basis points in the first nine months of 2008 compared to the same periods in 2007. This decrease was primarily due to a \$4.0 million reduction in lease financing interest income as a result of recording the effective settlement of our SILO transactions in September 2008. See Note 6 to the Consolidated Financial Statements (Unaudited) for more information on the effective settlement of our SILO transactions.

Average deposit balances decreased by \$243.1 million in the third quarter of 2008 and by \$22.1 million in the first nine months of 2008 compared to the same periods in 2007. Lower average customer deposit balances were partially offset by an increase in alternative funding sources. Average balances in securities sold under agreements to repurchase increased by \$60.9 million in the third quarter of 2008 and by \$58.4 million in the first nine months of 2008 compared to the same periods in 2007. Average loans and leases decreased by \$57.8 million in the third quarter of 2008 and by \$11.1 million in the first nine months of 2008 compared to the same periods in 2007. The decrease in average loan and lease balances were primarily due to a decrease in construction financing, reflective of construction projects nearing completion. While we continue to identify lending opportunities in the markets that we serve, we maintain a disciplined underwriting approach to these opportunities.

#### *Provision for Credit Losses*

The Provision reflects our judgment of the expense or benefit necessary to maintain the appropriate amount of the Allowance. We maintain the Allowance at levels adequate to absorb our estimate of probable credit losses estimated at the end of the reporting period. The Allowance is determined through detailed quarterly analyses of our loan and lease portfolio. The Allowance is based on our loss experience, changes in the economic environment, as well as an ongoing

assessment of our credit quality. We recorded a Provision of \$20.4 million for the third quarter of 2008 compared to a Provision of \$4.1 million for the same period in 2007. We recorded a Provision of \$42.0 million for the first nine months of 2008 compared to a Provision of \$10.1 million for the same period in 2007. The higher Provision recorded in the third quarter of 2008 compared to the same period in 2007, a result of our quarterly evaluation of the adequacy of the Allowance, was primarily due to heightened risk in three specific loan exposures and to general risk from the weakening economy in Hawaii and the Mainland U.S. The higher Provision recorded in the first nine months of 2008 compared to the same period in 2007 also reflects increased risk in our small business and unsecured consumer lending portfolios. Our commercial aircraft leasing portfolio, in particular, has been adversely affected by high oil prices. For further discussion on the Allowance, see the Corporate Risk Profile Reserve for Credit Losses section in Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ).

#### *Noninterest Income*

Noninterest income decreased by \$4.3 million or 7% in the third quarter of 2008 and increased by \$23.4 million or 13% in the first nine months of 2008 compared to the same periods in 2007. The results for the first nine months of 2008 were significantly impacted by the previously mentioned Visa transaction and from the sale of our equity interest in an aircraft lease.

Trust and asset management income decreased by \$1.0 million or 6% in the third quarter of 2008 compared to the same period in 2007, primarily due to a \$0.7 million decrease in fees from accounts under management, which were adversely affected by the decline in the equity markets over this period. Trust and asset management income decreased by \$2.4 million or 5% in the first nine months of 2008 compared to the same period in 2007, primarily due to a similar decrease in fees from accounts under management. Total trust assets under administration were \$11.3 billion as of September 30, 2008 and \$13.1



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billion as of September 30, 2007. Trust and asset management income is expected to continue to fluctuate based in part on the value of trust assets under administration and customer activity.

Table 4 presents the components of mortgage banking income for the third quarter and first nine months of 2008 and 2007.

**Mortgage Banking (Unaudited)****Table 4**

|  | <b>Three Months Ended<br/>September 30,</b> |                 | <b>Nine Months Ended<br/>September 30,</b> |                 |
|--|---|-----------------|--|-----------------|
| (dollars in thousands)   | <b>2008</b>                                 | <b>2007</b>     | <b>2008</b>                                | <b>2007</b>     |
| Mortgage Origination and Servicing Activities                        |   |                 |  |                 |
| Servicing Income   | \$ 1,602                                    | \$ 1,471        | \$ 4,681                                   | \$ 4,509        |
| Net Gains (Losses) on the Sale of Residential Mortgage Loans         | (170)                                       | 169             | 883  | 325             |
| Mortgage Loan Fees   | 504   | 635             | 1,847                                      | 1,858           |
| Total Mortgage Origination and Servicing Activities                  | 1,936                                       | 2,275           | 7,411                                      | 6,692           |
| Mortgage Servicing Rights and Derivative Financial Instruments       |   |                 |  |                 |
| Net Change in the Fair Value of Mortgage Servicing Rights            |   |                 |  |                 |
| Due to Originations and Payoffs 1                                    | (458)                                       | (228)           | (1,317)                                    | 271             |
| Net Change in the Fair Value of Mortgage Servicing Rights            |   |                 |  |                 |
| Due to Changes in Valuation Assumptions and the                      |   |                 |  |                 |
| Fair Value of Designated Securities 2                                | (2,582)                                     | 1,824           | (3,030)                                    | 2,650           |
| Net Losses Related to Mortgage Servicing Rights                      |   |                 |  |                 |
| Under the Amortization Method  | (146)                                       |                 | (146)                                      |                 |
| Net Gains (Losses) on Derivative Financial Instruments               | 1,871                                       | (23)            | 4,738                                      | 85              |
| Total Mortgage Servicing Rights and Derivative Financial Instruments | (1,315)                                     | 1,573           | 245  | 3,006           |
| <b>Total Mortgage Banking</b>  | <b>\$ 621</b>                               | <b>\$ 3,848</b> | <b>\$ 7,656</b>                            | <b>\$ 9,698</b> |

1 Principally represents changes due to the realization of expected cash flows over time.

2 Changes in valuation assumptions principally reflects changes in discount rates and loan repayment rate assumptions, mostly due to changes in interest rates. Designated Securities were comprised of mortgage-backed securities in our trading portfolio, which were used to manage the volatility of the fair value of our mortgage servicing rights. Realized investment trading gains and losses were not material.



Mortgage loan originations were \$157.4 million in the third quarter of 2008, a \$13.9 million or 8% decrease compared to the same period in 2007. Mortgage loan originations were \$685.8 million in the first nine months of 2008, a \$61.8 million or 10% increase compared to the same period in 2007. The decrease in mortgage loan originations in the third quarter of 2008 compared to the same period in 2007 was primarily due to the slowing residential real estate market in Hawaii. The increase in mortgage loan originations in the first nine months of 2008 compared to the same period in 2007 was primarily due to higher refinancing activity, particularly in the first quarter of 2008, due to lower interest rates on mortgage-based products. Servicing income has remained stable in 2008, as our portfolio of residential mortgage loans serviced for third parties was \$2.6 billion as of September 30, 2008 and \$2.5 billion as of September 30, 2007. The estimated fair values of our mortgage servicing rights and our trading securities (the Designated Securities ) fluctuates over time due to changes

in market interest rates, valuation assumptions, and the realization of expected cash flows. The increase in net gains on our derivative financial instruments in 2008 was primarily due to our adoption of SAB No. 109 on January 1, 2008, which had the effect of accelerating gain recognition of the estimated fair value of the servicing rights related to the loan from the loan sale date to the loan commitment date.

Service charges on deposit accounts increased by \$1.1 million or 9% in the third quarter of 2008 and by \$3.6 million or 11% in the first nine months of 2008 compared to the same periods in 2007. The increase in the third quarter of 2008 compared to the same period in 2007 was primarily due to a \$1.2 million increase in account analysis fees on analyzed business checking accounts as a result of lower earnings credit rates on customer accounts. Also contributing to the increase was a \$0.4 million increase in overdraft fees as a result of fee



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schedule changes implemented in the third quarter of 2007 and second quarter of 2008, as well as higher transactional volume. These increases were partially offset by a \$0.4 million decrease in monthly service fees due to a free checking promotion which began in the third quarter of 2008. The increase in the first nine months of 2008 compared to the same period in 2007 was also due to a \$3.1 million increase in account analysis fees and a \$1.4 million increase in overdraft fees, which were partially offset by a \$0.6 million decrease in monthly service fees.

Fees, exchange, and other service charges increased by \$0.5 million or 3% in the third quarter of 2008 and by \$1.2 million or 2% in the first nine months of 2008 compared to the same periods in 2007. The increase in the third quarter of 2008 compared to the same period in 2007 was primarily due to a \$0.4 million increase in fees from facilitating interest rate swaps on behalf of our customers. Also contributing to the increase was a \$0.3 million increase in debit card income resulting from higher transactional volume from new and existing debit cardholders. These increases were partially offset by a \$0.2 million decrease in ATM fee income. The increase in the first nine months of 2008 compared to the same period in 2007 was primarily due to a \$1.4 million increase in debit card income due to a similar increase in transactional volume from new and existing debit cardholders. Also contributing to the increase was a \$0.5 million increase in fees from facilitating interest rate swaps on behalf of our customers, partially offset by a \$0.8 million decrease in ATM fee income as a result of lower transactional volume.

Insurance income decreased by \$1.5 million or 21% in the third quarter of 2008 and slightly increased by \$0.1 million in the first nine months of 2008 compared to the same periods in 2007. The decrease in the third quarter of 2008 was primarily due to a \$2.1 million decrease in contingent commission income, partially offset by a \$0.8 million increase in income

from fixed income annuity products as customers preferred conservative investment alternatives in light of market conditions. The slight increase in the first nine months of 2008 compared to the same period in 2007 was primarily due to a \$1.6 million increase in income from fixed income annuity products, partially offset by a \$0.9 million decrease in contingent commission income and a \$0.4 million decrease in commission and brokerage income.

Other noninterest income increased by \$0.4 million or 8% in the third quarter of 2008 and by \$23.9 million in the first nine months of 2008 compared to the same periods in 2007. The increase in the third quarter of 2008 compared to the same period in 2007 was primarily due to a \$0.7 million increase in the estimated fair value of our subordinated notes. Also contributing to the increase was a \$0.5 million increase in death benefit proceeds from bank-owned life insurance ( BOLI ). These increases were partially offset by a \$0.3 million decrease in mutual fund and securities income as customers preferred conservative investment alternatives in light of market conditions. The increase in the first nine months of 2008 compared to the same period in 2007 was primarily due to the \$13.7 million gain from the mandatory redemption of our Visa shares and the \$11.6 million gain on the sale of our equity interest in an aircraft lease in March 2008. See Note 7 to the Consolidated Financial Statements (Unaudited) for more information on the mandatory redemption of our Visa shares. See Note 5 to the Consolidated Financial Statements (Unaudited) for more information on the sale of our equity interest in the aircraft lease.

#### *Noninterest Expense*

Noninterest expense increased by \$5.3 million or 7% in the third quarter of 2008 and by \$20.7 million or 8% in the first nine months of 2008 compared to the same periods in 2007.



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Table 5 presents the components of salaries and benefits expense for the third quarter and first nine months of 2008 and 2007.

**Salaries and Benefits (Unaudited)**

|                                     | <b>Table 5</b>            |                          |
|-------------------------------------|---------------------------|--------------------------|
|                                     | <b>Three Months Ended</b> | <b>Nine Months Ended</b> |
|                                     | <b>September 30,</b>      | <b>September 30,</b>     |
| <b>(dollars in thousands)</b>       | <b>2008</b>               | <b>2007</b>              |
| Salaries                            | \$ 30,190                 | \$ 28,882                |
| Incentive Compensation              | 5,969                     | 4,364                    |
| Cash for Stock Grants               | -                         | -                        |
| Share-Based Compensation            | 1,180                     | 1,601                    |
| Commission Expense                  | 1,653                     | 1,546                    |
| Retirement and Other Benefits       | 3,097                     | 3,865                    |
| Payroll Taxes                       | 2,162                     | 2,116                    |
| Medical, Dental, and Life Insurance | 2,452                     | 2,324                    |
| Separation Expense                  | 61                        | 246                      |
| <b>Total Salaries and Benefits</b>  | <b>\$ 46,764</b>          | <b>\$ 44,944</b>         |

Salaries and benefits expense increased in the third quarter of 2008 compared to the same period in 2007 primarily due to a \$1.6 million increase in incentive compensation expense and a \$1.4 million increase in salaries from annual merit increases and related payroll taxes. These increases were partially offset by a \$0.4 million decrease in restricted stock amortization expense, a \$0.4 million decrease in staff relocation, and a \$0.3 million decrease in retirement plan expenses. Salaries and benefits expense increased in the first nine months of 2008 compared to the same period in 2007 primarily due to a \$9.2 million increase in incentive compensation expense for employees related to cash awards to purchase our stock and other earnings-based incentive compensation. Of this increase, \$4.6 million related to a change in our practice of equity compensation for senior management. Senior officers, other than executive officers, generally received or will receive cash grants to encourage them to purchase our common stock in lieu of restricted stock grants. Of the \$4.6 million accrual, we paid \$2.3 million in cash to senior officers in the second quarter of 2008 with the remaining balance expected to be paid by December 31, 2008. Salaries and benefits expense also increased over this period due to a \$3.0 million increase in salaries from annual merit increases and related payroll taxes.

Net occupancy increased by \$1.5 million or 15% in the third quarter of 2008 and by \$3.8 million or 13% in the first nine months of 2008 compared to the same periods in 2007. The increase in the third quarter of 2008 compared to the same period in 2007 was primarily due to a \$0.7 million increase in net rental expense, related in part to our new Waikiki branch, and a \$0.6 million increase in utilities expense. The increase in the first nine months of 2008 was also due to a \$1.6 million increase in net rental expense, related in part to our new Waikiki branch, and a \$1.5 million increase in utilities expense.

Professional fees increased by \$0.9 million or 38% in the third quarter of 2008 and by \$1.0 million or 13% in the first nine months of 2008 compared to the same periods in 2007. The increase in the third quarter of 2008 compared to the same period in 2007 was primarily due to a \$0.3 million increase in legal and other professional services related to the SILO transactions. Also contributing to the increase in the third quarter of 2008 was a \$0.2 million reversal of legal fees recorded in 2007. The increase in the first nine months of 2008 compared to the same period in 2007 was also due to the \$0.3 million increase in legal and other professional services related to the SILO transactions, as well as a \$0.7 million reversal of legal fees recorded in 2007.





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Other noninterest expense increased by \$1.2 million or 6% in the third quarter of 2008 compared to the same period in 2007. The increase in other noninterest expense was primarily due to a \$0.3 million increase each in directors' fees due to the change in market value of the directors' deferred compensation plan assets, technology data services, and in our reserves for contingencies.

Other noninterest expense increased by \$3.6 million or 6% in the first nine months of 2008 compared to the same period in 2007. The increase in other noninterest expense was primarily due to:

- \$3.0 million increase in our reserves for contingencies;
- \$2.3 million increase in our contributions to the Bank of Hawaii Charitable Foundation and other charitable organizations;
- \$1.0 million related to the call premium on our Capital Securities;
- \$0.8 million increase in our airline mileage reward program expenses due to higher volume;
- \$0.6 million increase in directors' fees due to the change in market value of the directors' deferred compensation plan assets;
- \$0.6 million increase in delivery and postage services;
- \$0.5 million increase in merchant transaction and card processing fees due to higher volume; and
- \$0.3 million reversal of typhoon-related accruals in the second quarter of 2007 related to the Pacific Islands.

These increases in the first nine months of 2008 compared to the same period in 2007 were partially offset by the reversal of \$5.6 million in previously recorded Visa contingency accruals described in the Overview above.

See Note 7 to the Consolidated Financial Statements (Unaudited) for more discussion on the reversal of our Visa contingency accruals.

### *Provision for Income Taxes*

See Note 6 to the Consolidated Financial Statements (Unaudited) for information on the provision for income taxes.



Table of Contents**Analysis of Statements of Condition*****Investment Securities***

Table 6 presents the amortized cost and estimated fair value of our available-for-sale and held-to-maturity investment securities as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Investment Securities (Unaudited)**

|   | <b>Amortized<br/>Cost</b> | <b>Table 6<br/>Fair<br/>Value</b> |
|---|---------------------------|-----------------------------------|
| (dollars in thousands)  |                           |                                   |
| <b>September 30, 2008</b>   |                           |                                   |
| <b>Available-for-Sale:</b>  |                           |                                   |
| Debt Securities Issued by the U.S. Treasury and Government Agencies           | \$ 649                    | \$ 678                            |
| Debt Securities Issued by States and Political Subdivisions                   | 47,079                    | 46,691                            |
| Debt Securities Issued by U.S. Government-Sponsored Enterprises               | 235,386                   | 232,544                           |
| Mortgage-Backed Securities Issued by<br>U.S. Government-Sponsored Enterprises | 1,997,999                 | 1,996,671                         |
| Non-Agencies  | 311,537                   | 292,491                           |
| Total Mortgage-Backed Securities  | 2,309,536                 | 2,289,162                         |
| Other Debt Securities   | 3,033                     | 3,036                             |
| <b>Total</b>  | <b>\$ 2,595,683</b>       | <b>\$ 2,572,111</b>               |
| <b>Held-to-Maturity:</b>  |                           |                                   |
| Mortgage-Backed Securities Issued by U.S. Government-Sponsored Enterprises    | \$ 249,083                | \$ 245,720                        |
| <b>Total</b>  | <b>\$ 249,083</b>         | <b>\$ 245,720</b>                 |
| <b>December 31, 2007</b>  |                           |                                   |
| <b>Available-for-Sale:</b>  |                           |                                   |
| Debt Securities Issued by the U.S. Treasury and Government Agencies           | \$ 3,295                  | \$ 3,325                          |
| Debt Securities Issued by States and Political Subdivisions                   | 47,620                    | 47,910                            |
| Debt Securities Issued by U.S. Government-Sponsored Enterprises               | 294,223                   | 295,464                           |
| Mortgage-Backed Securities Issued by<br>U.S. Government-Sponsored Enterprises | 1,678,828                 | 1,684,471                         |
| Non-Agencies  | 312,973                   | 304,440                           |
| Total Mortgage-Backed Securities  | 1,991,801                 | 1,988,911                         |
| Other Debt Securities   | 228,421                   | 227,580                           |
| <b>Total</b>  | <b>\$ 2,565,360</b>       | <b>\$ 2,563,190</b>               |
| <b>Held-to-Maturity:</b>  |                           |                                   |
| Debt Securities Issued by States and Political Subdivisions                   | \$ 6                      | \$ 6                              |
| Mortgage-Backed Securities Issued by U.S. Government-Sponsored Enterprises    | 292,571                   | 287,638                           |
| <b>Total</b>  | <b>\$ 292,577</b>         | <b>\$ 287,644</b>                 |
| <b>September 30, 2007 <sup>1</sup></b>  |                           |                                   |
| <b>Available-for-Sale:</b>  |                           |                                   |
| Debt Securities Issued by the U.S. Treasury and Government Agencies           | \$ 4,043                  | \$ 4,054                          |
| Debt Securities Issued by States and Political Subdivisions                   | 47,663                    | 47,625                            |
| Debt Securities Issued by U.S. Government-Sponsored Enterprises               | 378,633                   | 379,336                           |
| Mortgage-Backed Securities Issued by<br>U.S. Government-Sponsored Enterprises | 1,637,611                 | 1,620,181                         |
| Non-Agencies  | 322,876                   | 314,878                           |

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|  |                     |                     |
|--|---------------------|---------------------|
| Total Mortgage-Backed Securities   | 1,960,487           | 1,935,059           |
| Other Debt Securities  | 228,348             | 225,908             |
| <b>Total</b>   | <b>\$ 2,619,174</b> | <b>\$ 2,591,982</b> |
| <b>Held-to-Maturity:</b>   |                     |                     |
| Debt Securities Issued by States and Political Subdivisions                | \$ 6                | \$ 6                |
| Mortgage-Backed Securities Issued by U.S. Government-Sponsored Enterprises | 307,647             | 299,185             |
| <b>Total</b>   | <b>\$ 307,653</b>   | <b>\$ 299,191</b>   |

1 Certain prior period information has been reclassified to conform to the current presentation.

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The carrying value of our investment securities, excluding trading securities, was \$2.8 billion as of September 30, 2008 and \$2.9 billion as of December 31, 2007 and September 30, 2007. Investment securities with a carrying value of \$2.1 billion as of September 30, 2008, \$1.7 billion as of December 31, 2007, and \$1.8 billion as of September 30, 2007, which approximates fair value, were pledged to secure deposits of governmental entities and securities sold under agreements to repurchase.

Investment securities pledged where the secured party has the right to sell or repledge the investment securities were \$768.7 million as of September 30, 2008, \$650.4 million as of December 31, 2007, and \$656.6 million as of September 30, 2007.

As of September 30, 2008, the par value of our callable debt and mortgage-backed securities issued by the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation were as follows:

**Investment Securities Issued by the Federal National Mortgage Association  
and the Federal Home Loan Mortgage Corporation (Unaudited)**

(dollars in thousands)

**Table 7  
Par Value**

**September 30, 2008**

|  |                     |
|--|---------------------|
| Debt Securities Issued by U.S. Government-Sponsored Enterprises            |                     |
| Federal National Mortgage Association                                      | \$ 210,057          |
| Federal Home Loan Mortgage Corporation                                     | 500                 |
| Subtotal   | 210,557             |
| Mortgage-Backed Securities Issued by U.S. Government-Sponsored Enterprises |                     |
| Federal National Mortgage Association                                      | 959,530             |
| Federal Home Loan Mortgage Corporation                                     | 854,641             |
| Subtotal   | 1,814,171           |
| <b>Total</b>   | <b>\$ 2,024,728</b> |



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As of September 30, 2008, we did not own any subordinated debt, or preferred or common stock of the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation.

As of September 30, 2008, all of our mortgage-backed securities issued by private issuers ( non-agencies ) were prime jumbo, AAA-rated, with an average current amortized loan-to-value ratio of 59%. As of September 30, 2008, 97% of the fair value of our mortgage-backed securities issued by non-agencies were originated prior to 2006.

Loans past due 90 days or more, underlying the mortgage-backed securities issued by non-agencies, represented approximately 66 basis points of the par value outstanding or approximately \$2.1 million as of September 30, 2008. As of September 30, 2008, there were no sub-prime or Alt-A securities in our mortgage-backed securities portfolio.



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Table 8 presents our temporarily impaired investment securities as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Temporarily Impaired Investment Securities (Unaudited)****Table 8**

|   | <b>Temporarily Impaired<br/>Less Than 12 Months</b> |             | <b>Temporarily Impaired<br/>12 Months or Longer</b> |             | <b>Total</b>                           |             |
|---|---|-------------|---|-------------|--|-------------|
|   | <b>Gross<br/>Unrealized<br/>Losses</b>              |             | <b>Gross<br/>Unrealized<br/>Losses</b>              |             | <b>Gross<br/>Unrealized<br/>Losses</b> |             |
| (dollars in thousands)  | <b>Fair Value</b>                                   |             | <b>Fair Value</b>                                   |             | <b>Fair Value</b>                      |             |
| <b>September 30, 2008</b>   |   |             |   |             |  |             |
| Debt Securities Issued by States<br>and Political Subdivisions                      | \$ 30,278   | \$ (471)    | \$ 552  | \$ (35)     | \$ 30,830                              | \$ (506)    |
| Debt Securities Issued by U.S.<br>Government-Sponsored<br>Enterprises               | 228,968   | (2,885)     | 1,431   | (16)        | 230,399                                | (2,901)     |
| Mortgage-Backed Securities<br>Issued by U.S.<br>Government-Sponsored<br>Enterprises | 1,039,599   | (14,411)    | 116,224   | (3,054)     | 1,155,823                              | (17,465)    |
| Non-Agencies  | 136,021   | (5,883)     | 140,490   | (13,346)    | 276,511                                | (19,229)    |
| Total Mortgage-Backed<br>Securities   | 1,175,620   | (20,294)    | 256,714   | (16,400)    | 1,432,334                              | (36,694)    |
| <b>Total Temporarily Impaired<br/>Investment Securities</b>                         |   |             |   |             |  |             |
| <b>September 30, 2008</b>   | \$ 1,434,866  | \$ (23,650) | \$ 258,697  | \$ (16,451) | \$ 1,693,563                           | \$ (40,101) |
| <b>December 31, 2007</b>  | \$ 150,249  | \$ (616)    | \$ 1,325,002  | \$ (21,445) | \$ 1,475,251                           | \$ (22,061) |
| <b>September 30, 2007</b>   | \$ 291,446  | \$ (1,629)  | \$ 1,766,042  | \$ (39,473) | \$ 2,057,488                           | \$ (41,102) |

Our temporarily impaired investment securities and related gross unrealized losses increased as of September 30, 2008 compared to December 31, 2007 primarily due to a rise in interest rates on mortgage-based products over this period of time. This rise in interest rates on mortgage-based products adversely affected the fair value of our mortgage-backed securities. The decrease in our temporarily impaired investment securities and related gross unrealized losses as of September 30, 2008 compared to September 30, 2007 was primarily due to the maturities and pay-downs on investment securities as well as decreasing interest rates on mortgage-based products over this period of time.

The gross unrealized losses reported for mortgage-backed securities are primarily related to investment securities issued by U.S. government-sponsored enterprises, such as the Federal National Mortgage Association and Federal Home Loan Mortgage Corporation, and to investment securities issued by non-agencies. We do not believe that the investment securities that were in an unrealized loss position as of September 30, 2008, which was comprised of 177 securities, represent an other-than-temporary impairment. Total gross unrealized losses were primarily attributable to changes in interest rates, relative to when the investment securities were purchased, and not due to the credit quality of the investment securities. We have both the intent and ability to hold the investment securities for a period of time necessary to recover the amortized cost.



Table of Contents*Loans and Leases*

Table 9 presents the composition of our loan and lease portfolio by major categories.

| <b>Loan and Lease Portfolio Balances (Unaudited)</b> | <b>September 30,<br/>2008</b> | <b>June 30,<br/>2008</b> | <b>March 31,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>Table 9<br/>September 30,<br/>2007<sup>1</sup></b> |
|--|-------------------------------|--------------------------|---------------------------|------------------------------|---|
| (dollars in thousands)                               |                               |                          |                           |                              |   |
| <b>Commercial</b>                                    |                               |                          |                           |                              |   |
| Commercial and Industrial                            | \$ 1,077,314                  | \$ 1,052,319             | \$ 1,079,772              | \$ 1,054,355                 | \$ 1,065,258  |
| Commercial Mortgage                                  | 708,961                       | 680,784                  | 650,638                   | 634,483                      | 627,329   |
| Construction   | 153,364                       | 168,678                  | 190,521                   | 208,670                      | 254,062   |
| Lease Financing                                      | 467,279                       | 471,443                  | 465,945                   | 481,882                      | 478,988   |
| Total Commercial                                     | 2,406,918                     | 2,373,224                | 2,386,876                 | 2,379,390                    | 2,425,637   |
| <b>Consumer</b>                                      |                               |                          |                           |                              |   |
| Residential Mortgage                                 | 2,496,983                     | 2,509,133                | 2,530,207                 | 2,508,261                    | 2,510,313   |
| Home Equity  | 986,379                       | 966,108                  | 967,146                   | 972,995                      | 953,713   |
| Automobile   | 395,015                       | 413,338                  | 430,920                   | 443,011                      | 440,525   |
| Other <sup>2</sup>                                   | 254,163                       | 256,325                  | 264,188                   | 277,204                      | 269,727   |
| Total Consumer                                       | 4,132,540                     | 4,144,904                | 4,192,461                 | 4,201,471                    | 4,174,278   |
| <b>Total Loans and Leases</b>                        | <b>\$ 6,539,458</b>           | <b>\$ 6,518,128</b>      | <b>\$ 6,579,337</b>       | <b>\$ 6,580,861</b>          | <b>\$ 6,599,915</b>                                   |

<sup>1</sup> Certain prior period information has been reclassified to conform to the current presentation.

<sup>2</sup> Comprised of other revolving credit, installment, and lease financing.

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Loans and leases represent our largest category of interest earning assets and the largest source of interest income.

The increase in total commercial loans and leases from December 31, 2007 was primarily due to a \$74.5 million increase in commercial mortgage loans and a \$23.0 million increase in commercial and industrial loans. The increase in our commercial secured mortgage loan portfolio was consistent with our strategy to grow this portfolio. The increase in our commercial and industrial loan portfolio was attributable to additional draws made by several corporate customers in the third quarter of 2008. Our construction loan portfolio decreased by \$55.3 million and our lease financing balances decreased by \$14.6 million from December 31, 2007. The decrease in our construction loan exposure is consistent with our strategy to reduce our exposure in this area as we experience a slowing economy in Hawaii. The decrease in lease financing balances was primarily due to the exercise of an early buy-out option by one of our aircraft lessees in March 2008. The decrease in consumer loans and leases from December 31, 2007 was in all categories except home equity loans, consistent with a slowing economy in Hawaii and our

continued disciplined underwriting approach. The increase in home equity loans was primarily due to customer utilization of existing home equity lines.

The decrease in total commercial loans and leases from September 30, 2007 was primarily due to a \$100.7 million decrease in construction loans and an \$11.7 million decrease in lease financing. The decrease in lease financing balances was primarily due to the exercise of an early buy-out option by one of our aircraft lessees in March 2008. These decreases in our commercial loan and lease portfolio were partially offset by an \$81.6 million increase in commercial mortgage loans from September 30, 2007. As noted above, our strategy has been to reduce our construction lending exposure and to grow our commercial secured mortgage portfolio. The decrease in consumer loans and leases from September 30, 2007 was in all categories except home equity loans. These trends in the consumer portfolio are consistent with a slowing economy in Hawaii and our continued disciplined underwriting approach. The increase in home equity loans was primarily due to customer utilization of existing home equity lines.





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Table 10 presents the composition of our loan and lease portfolio by geographic area and by major categories.

| <b>Geographic Distribution of Loan and Lease Portfolio (Unaudited)</b> |                               |                          |                           |                                | <b>Table 10</b>                 |
|--|-------------------------------|--------------------------|---------------------------|--------------------------------|---------------------------------|
| (dollars in thousands)   | <b>September 30,<br/>2008</b> | <b>June 30,<br/>2008</b> | <b>March 31,<br/>2008</b> | <b>December 31,<br/>2007 1</b> | <b>September 30,<br/>2007 1</b> |
| <b>Commercial</b>  |                               |                          |                           |                                |                                 |
| Hawaii   |                               |                          |                           |                                |                                 |
| Commercial and Industrial  | \$ 729,699                    | \$ 705,468               | \$ 718,457                | \$ 695,141                     | \$ 677,242                      |
| Commercial Mortgage  | 626,690                       | 597,322                  | 564,719                   | 548,423                        | 531,920                         |
| Construction   | 142,719                       | 157,642                  | 178,958                   | 197,762                        | 239,765                         |
| Lease Financing  | 107,704                       | 62,623                   | 55,498                    | 55,697                         | 51,839                          |
| Mainland U.S. 2  |                               |                          |                           |                                |                                 |
| Commercial and Industrial  | 198,708                       | 200,618                  | 205,122                   | 202,203                        | 233,931                         |
| Commercial Mortgage  | 4,695                         | 4,808                    | 4,953                     | 5,129                          | 5,569                           |
| Construction   | 8,655                         | 9,045                    | 10,278                    | 9,932                          | 14,088                          |
| Lease Financing  | 340,703                       | 389,573                  | 391,303                   | 395,419                        | 396,471                         |
| Guam   |                               |                          |                           |                                |                                 |
| Commercial and Industrial  | 78,700                        | 71,340                   | 74,736                    | 75,239                         | 64,063                          |
| Commercial Mortgage  | 73,240                        | 74,226                   | 76,220                    | 76,301                         | 85,098                          |
| Construction   | 1,990                         | 1,991                    | 1,285                     | 976                            | 209                             |
| Other Pacific Islands  |                               |                          |                           |                                |                                 |
| Commercial and Industrial  | 14,660                        | 15,942                   | 16,693                    | 17,771                         | 18,535                          |
| Commercial Mortgage  | 2,188                         | 2,365                    | 2,529                     | 2,629                          | 2,776                           |
| Foreign 3  |                               |                          |                           |                                |                                 |
| Commercial and Industrial  | 55,547                        | 58,951                   | 64,764                    | 64,001                         | 71,487                          |
| Commercial Mortgage  | 2,148                         | 2,063                    | 2,217                     | 2,001                          | 1,966                           |
| Lease Financing  | 18,872                        | 19,247                   | 19,144                    | 30,766                         | 30,678                          |
| Total Commercial   | 2,406,918                     | 2,373,224                | 2,386,876                 | 2,379,390                      | 2,425,637                       |
| <b>Consumer</b>  |                               |                          |                           |                                |                                 |
| Hawaii   |                               |                          |                           |                                |                                 |
| Residential Mortgage   | 2,274,028                     | 2,281,164                | 2,296,061                 | 2,269,670                      | 2,269,128                       |
| Home Equity  | 935,020                       | 912,467                  | 911,064                   | 915,820                        | 895,629                         |
| Automobile   | 271,568                       | 282,843                  | 294,410                   | 308,706                        | 313,712                         |
| Other 4  | 189,417                       | 189,087                  | 193,915                   | 201,323                        | 190,775                         |
| Mainland U.S. 2  |                               |                          |                           |                                |                                 |
| Home Equity  | 29,473                        | 31,881                   | 35,445                    | 37,878                         | 39,870                          |
| Automobile   | 48,631                        | 49,792                   | 48,667                    | 40,679                         | 30,632                          |
| Guam   |                               |                          |                           |                                |                                 |
| Residential Mortgage   | 214,748                       | 219,757                  | 225,503                   | 230,017                        | 232,238                         |
| Home Equity  | 18,625                        | 18,413                   | 17,148                    | 15,671                         | 14,531                          |
| Automobile   | 67,600                        | 72,428                   | 78,403                    | 83,491                         | 84,849                          |
| Other 4  | 31,961                        | 33,078                   | 34,679                    | 36,767                         | 37,765                          |
| Other Pacific Islands  |                               |                          |                           |                                |                                 |
| Residential Mortgage   | 8,207                         | 8,212                    | 8,643                     | 8,574                          | 8,947                           |
| Home Equity  | 3,261                         | 3,347                    | 3,489                     | 3,626                          | 3,683                           |
| Automobile   | 7,216                         | 8,275                    | 9,440                     | 10,135                         | 11,332                          |
| Other 4  | 32,780                        | 34,157                   | 35,588                    | 39,090                         | 41,166                          |
| Foreign 3  |                               |                          |                           |                                |                                 |
| Other 4  | 5                             | 3                        | 6                         | 24                             | 21                              |
| Total Consumer   | 4,132,540                     | 4,144,904                | 4,192,461                 | 4,201,471                      | 4,174,278                       |
| <b>Total Loans and Leases</b>  | <b>\$ 6,539,458</b>           | <b>\$ 6,518,128</b>      | <b>\$ 6,579,337</b>       | <b>\$ 6,580,861</b>            | <b>\$ 6,599,915</b>             |

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1 Certain prior period information has been reclassified to conform to the current presentation.

2 For secured loans and leases, classification as Mainland U.S. is made based on where the collateral is located. For unsecured loans and leases, classification as Mainland U.S. is made based on the location where the majority of the borrower's business operations are conducted.

3 Loans and leases classified as Foreign represents those which are recorded in the Company's international business units.

4 Comprised of other revolving credit, installment, and lease financing.

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Our commercial and consumer lending activities are concentrated primarily in Hawaii and the Pacific Islands. Our commercial loan and lease portfolio to borrowers based on the Mainland U.S. includes participation in shared national credits and leveraged lease financing. Our consumer loan and lease portfolio includes limited lending activities on the Mainland U.S.

### *Other Assets*

Table 11 presents the major components of other assets as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Other Assets (Unaudited)**

|  | <b>September 30,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>Table 11<br/>September 30,<br/>2007</b> |
|--|-------------------------------|------------------------------|--|
| (dollars in thousands)                                     |                               |                              |  |
| Bank-Owned Life Insurance                                  | \$ 194,420                    | \$ 188,888                   | \$ 186,880                                 |
| Federal Home Loan Bank and Federal Reserve Bank Stock      | 79,635                        | 79,494                       | 79,416                                     |
| Low Income Housing Investments and Other Equity Investment | 31,945                        | 36,376                       | 32,726                                     |
| Accounts Receivable  | 19,461                        | 26,748                       | 24,005                                     |
| Federal and State Tax Deposits                             | 82,500                        | 61,000                       | 61,000                                     |
| Other  | 52,826                        | 40,626                       | 38,023                                     |
| <b>Total Other Assets</b>                                  | <b>\$ 460,787</b>             | <b>\$ 433,132</b>            | <b>\$ 422,050</b>                          |

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We placed an additional tax deposit of \$21.5 million with the IRS and State of Hawaii Department of Taxation during the third quarter of 2008. The additional deposit was placed with the respective taxing authorities relating to our ongoing assessment of the outcome of the IRS review of our Lease-In Lease-Out ( LILO ) and SILO transactions. The placement of the deposits, totaling \$82.5 million as of September 30, 2008, with the respective taxing authorities limits the potential accrual of additional interest based on our current estimate of our tax liabilities.

The increase in other assets from December 31, 2007 was primarily due to the additional tax deposit placed with the taxing authorities as noted above. Also contributing to the increase in other assets was a \$6.6 million receivable, arising in the normal course of business, reflected in the other category in the table above as of September 30, 2008, which settled in October 2008. We also benefited from a \$5.5 million increase in BOLI assets from current year earnings. These increases in other assets were partially offset by a \$6.0 million decrease in accounts receivable due to the receipt of sales proceeds from a real estate transaction which occurred in the fourth quarter of 2007 as well as a \$4.4 million decrease in low income housing and other equity investments due to current year amortization.

The increase in other assets from September 30, 2007 was primarily due to the additional tax deposit placed with the taxing authorities. Also contributing to the increase in other assets was a \$6.6 million receivable, arising in the normal course of business, reflected in the other category in the table above as of September 30, 2008, which settled in October 2008, as well as a \$6.8 million increase in balances from customer-related interest rate swap accounts, which have off-setting amounts recorded in other liabilities. BOLI assets also increased by \$7.5 million from September 30, 2007, which reflected earnings over this period.

### *Deposits*

As of September 30, 2008, total deposits were \$7.7 billion, a decrease of \$283.9 million or 4% from December 31, 2007 and a decrease of \$216.7 million or 3% from September 30, 2007. The decrease in deposit balances from 2007 was primarily due to a decrease in consumer time deposit balances. Part of the decrease in time deposits was offset by the migration of balances into more liquid savings and interest-bearing demand deposits. The decrease in deposit balances from 2007 was also due to a decrease in commercial escrow accounts related to construction projects nearing completion and lower public deposits due to the timing of bond payments.



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Table 12 presents the composition of our savings deposits as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Savings Deposits (Unaudited)**

|                               | <b>September 30,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>Table 12<br/>September 30,<br/>2007</b> |
|-------------------------------|-------------------------------|------------------------------|--|
| (dollars in thousands)        |                               |                              |  |
| Money Market                  | \$ 965,149                    | \$ 1,061,808                 | \$ 1,141,863                               |
| Regular Savings               | 1,773,535                     | 1,568,663                    | 1,569,306                                  |
| <b>Total Savings Deposits</b> | <b>\$ 2,738,684</b>           | <b>\$ 2,630,471</b>          | <b>\$ 2,711,169</b>                        |



Table 13 presents our average balance of time deposits of \$100,000 or more for the three months ended September 30, 2008, December 31, 2007, and September 30, 2007, and for the nine months ended September 30, 2008 and 2007.

**Average Time Deposits of \$100,000 or More (Unaudited)**

**Table 13**

|                        | <b>Three Months Ended</b> |                      |                       | <b>Nine Months Ended</b> |                       |  |
|------------------------|---------------------------|----------------------|-----------------------|--------------------------|-----------------------|--|
| (dollars in thousands) | <b>Sept. 30, 2008</b>     | <b>Dec. 31, 2007</b> | <b>Sept. 30, 2007</b> | <b>Sept. 30, 2008</b>    | <b>Sept. 30, 2007</b> |  |
| Average Time Deposits  | \$ 934,845                | \$ 983,389           | \$ 975,301            | \$ 964,081               | \$ 974,428            |  |

*Borrowings and Long-Term Debt*

Borrowings, including funds purchased and other short-term borrowings, were \$200.3 million as of September 30, 2008, an increase of \$114.5 million from December 31, 2007. The increase was primarily due to higher levels of funds purchased resulting from short-term liquidity needs. Borrowings as of September 30, 2008 compared to the same period in 2007 remained relatively stable.

Long-term debt was \$204.6 million as of September 30, 2008, a decrease of \$30.8 million or 13% from December 31, 2007 and a decrease of \$30.7 million or 13% from September 30, 2007. The decrease in long-term debt from 2007 was primarily due to the redemption of our remaining

\$26.4 million in Capital Securities and \$6.0 million in subordinated notes in the second quarter of 2008. This was partially offset by the adoption of SFAS No. 159 on January 1, 2008, which resulted in a \$4.2 million carrying value adjustment to fair value on our subordinated notes. See Notes 1 and 4 to the Consolidated Financial Statements (Unaudited) for more information on our adoption of SFAS No. 159. Further discussion on borrowings is included in the Corporate Risk Profile Liquidity Management section of MD&A.

*Securities Sold Under Agreements to Repurchase*

Table 14 presents the composition of our securities sold under agreements to repurchase as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Securities Sold Under Agreements to Repurchase  
(Unaudited)**

|   | <b>September 30,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>Table 14<br/>September 30,<br/>2007</b> |
|---|-------------------------------|------------------------------|--|
| (dollars in thousands)                                      |                               |                              |  |
| Government Entities   | \$ 434,431                    | \$ 429,340                   | \$ 487,511                                 |
| Private Institutions  | 675,000                       | 600,000                      | 600,000                                    |
| <b>Total Securities Sold Under Agreements to Repurchase</b> | <b>\$ 1,109,431</b>           | <b>\$ 1,029,340</b>          | <b>\$ 1,087,511</b>                        |

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The increase in securities sold under agreements to repurchase from 2007 was primarily due to additional placements with private institutions that provided for sources of liquidity used

to repay long-term debt, a more expensive source of funds. As of September 30, 2008, the weighted average maturity was 62 days for our securities sold under agreements to repurchase



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with government entities and 8.54 years for securities sold under agreements to repurchase with private institutions, subject to the private institutions' right to terminate agreements at earlier specified dates which could decrease the weighted average maturity to as few as 250 days. As of September 30, 2008, \$250.0 million of our securities sold under agreements to repurchase placed with private institutions were indexed to the London Inter Bank Offering Rate ( LIBOR ) with the remaining \$425.0 million at fixed interest rates. If the agreements with private institutions are not terminated by the specified dates, the interest rates on the agreements become fixed, at rates ranging from 2.98% to 5.00%, for the remaining term of the respective agreements. As of September 30, 2008, the weighted average interest rate for outstanding agreements with private institutions was 3.47%.

#### *Shareholders' Equity*

As of September 30, 2008, shareholders' equity was \$780.0 million, an increase of \$29.8 million or 4% from December 31, 2007 and an increase of \$48.3 million or 7% from September 30, 2007. The increase in shareholders' equity from December 31, 2007 was primarily due to current period earnings of \$152.9 million, partially offset by \$61.7 million in common stock repurchases and \$63.4 million in cash dividends paid. Further discussion on our capital structure is included in the Corporate Risk Profile Capital Management section of MD&A.

#### **Analysis of Business Segments**

Our business segments are defined as Retail Banking, Commercial Banking, Investment Services, and Treasury. Our internal management accounting process measures the performance of the business segments based on the management structure of our company. This process, which is not necessarily comparable with similar information for any other financial institution, uses various techniques to assign balance sheet and income statement amounts to the business segments, including allocations of income, expense, the Provision, and capital. This process is dynamic and requires certain allocations based on judgment and other subjective factors. Unlike financial accounting, there is no comprehensive authoritative guidance for management accounting that is equivalent to U.S. generally accepted accounting principles.

We evaluate several performance measures of the business segments, the most important of which are net income less a charge for the cost of allocated capital ( NIACC ) and risk adjusted return on capital ( RAROC ). The cost of allocated capital is determined by multiplying our estimate of a shareholder's minimum required rate of return on the cost of capital invested (10% for 2008, 11% for 2007) by the segment's allocated equity. We assume a cost of capital that is equal to a risk-free rate plus a risk premium. RAROC is the ratio of economic net income to risk-adjusted equity. Equity is allocated to each business segment based on an assessment of its inherent risk. The net interest income of the business segments reflect the results of a funds transfer pricing process that matches assets and liabilities with similar interest rate sensitivity and maturity characteristics and reflects the allocation of net interest income related to our overall asset and liability management activities on a proportionate basis. The basis for the allocation of net interest income is a function of our assumptions that are subject to change based on changes in current interest rates and market conditions. Funds transfer pricing also serves to transfer interest rate risk to Treasury. However, the other business segments have some latitude to retain certain interest rate exposures related to customer pricing decisions within guidelines. Allocated net income for each business segment includes a Provision. For business segment reporting purposes, the Provision is reversed and is replaced by an economic provision. The economic provision is a statistically derived estimate of annual expected credit losses over an economic cycle.

We consider NIACC to be a measure of shareholder value creation. Our consolidated NIACC was \$37.4 million for the third quarter of 2008 compared to \$27.0 million for the same period in 2007. The increase in NIACC in the third quarter of 2008 was primarily due to the previously noted \$8.9 million net gain related to our acceptance of the settlement initiative from the IRS related to our SILO transactions. Our consolidated NIACC was \$110.9 million for the first nine months of 2008 compared to \$79.8 million for the





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same period in 2007. The increase in NIACC for the first nine months of 2008 was primarily due to an increase in net interest income as well as the previously noted gains related to Visa, the sale of our equity interest in an aircraft lease, and the net gain related to our SILO transactions. This was partially offset by accruals related to employee incentives, charitable contributions, the call premium on our Capital Securities, and contingencies. The increase in the Provision did not impact

NIACC since it is replaced by an economic provision. For the third quarter of 2008 and for the first nine months of 2008, the economic provision was relatively unchanged compared to the same periods in 2007.

Tables 15a and 15b summarize our NIACC and RAROC for the third quarter of 2008 and for the first nine months of 2008 compared to the same periods in 2007.

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**Business Segments Selected Financial Information (Unaudited)**

**Table 15a  
Consolidated  
Total**

| (dollars in thousands)   | <b>Retail<br/>Banking</b> | <b>Commercial<br/>Banking</b> | <b>Investment<br/>Services</b> | <b>Total</b> | <b>Treasury</b> |               |
|--|---------------------------|-------------------------------|--------------------------------|--------------|-----------------|---------------|
| <b>Three Months Ended September</b>                                |                           |                               |                                |              |                 |               |
| <b>30, 2008 1</b>  |                           |                               |                                |              |                 |               |
| Net Interest Income  | \$ 58,228                 | \$ 36,564                     | \$ 3,922                       | \$ 98,714    | \$ 4,861        | \$ 103,575    |
| Provision for Credit Losses  | 5,475                     | 13,826                        | 1,089                          | 20,390       | (32)            | 20,358        |
| Net Interest Income After<br>Provision for Credit Losses           | 52,753                    | 22,738                        | 2,833                          | 78,324       | 4,893           | 83,217        |
| Noninterest Income   | 27,380                    | 10,508                        | 17,458                         | 55,346       | 1,640           | 56,986        |
| Noninterest Expense  | (43,709)                  | (24,488)                      | (16,800)                       | (84,997)     | (1,793)         | (86,790)      |
| Income Before Provision for<br>Income Taxes                        | 36,424                    | 8,758                         | 3,491                          | 48,673       | 4,740           | 53,413        |
| Provision for Income Taxes   | (13,478)                  | (4,686)                       | (1,292)                        | (19,456)     | 13,452          | (6,004)       |
| Allocated Net Income   | 22,946                    | 4,072                         | 2,199                          | 29,217       | 18,192          | 47,409        |
| Allowance Funding Value  | (229)                     | (944)                         | (16)                           | (1,189)      | 1,189           |               |
| Provision for Credit Losses  | 5,475                     | 13,826                        | 1,089                          | 20,390       | (32)            | 20,358        |
| Economic Provision   | (1,912)                   | (3,222)                       | (78)                           | (5,212)      | (1)             | (5,213)       |
| Tax Effect of Adjustments  | (1,234)                   | (3,574)                       | (369)                          | (5,177)      | (426)           | (5,603)       |
| Income Before Capital Charge                                       | 25,046                    | 10,158                        | 2,825                          | 38,029       | 18,922          | 56,951        |
| Capital Charge   | (4,780)                   | (4,127)                       | (1,465)                        | (10,372)     | (9,135)         | (19,507)      |
| <b>Net Income (Loss) After Capital<br/>Charge (NIACC)</b>          | \$ 20,266                 | \$ 6,031                      | \$ 1,360                       | \$ 27,657    | \$ 9,787        | \$ 37,444     |
| <b>RAROC (ROE for the<br/>Company)</b>                             | 52%                       | 24%                           | 19%                            | 36%          | 96%             | 24%           |
| <b>Total Assets as of September 30,<br/>2008</b>                   | \$ 3,669,924              | \$ 3,023,242                  | \$ 285,497                     | \$ 6,978,663 | \$ 3,356,384    | \$ 10,335,047 |
| <b>Three Months Ended September</b>                                |                           |                               |                                |              |                 |               |
| <b>30, 2007 2</b>  |                           |                               |                                |              |                 |               |
| Net Interest Income (Loss)   | \$ 56,830                 | \$ 40,352                     | \$ 3,574                       | \$ 100,756   | \$ (2,200)      | \$ 98,556     |
| Provision for Credit Losses  | 1,773                     | 2,486                         | (1)                            | 4,258        | (188)           | 4,070         |
| Net Interest Income (Loss) After<br>Provision<br>for Credit Losses | 55,057                    | 37,866                        | 3,575                          | 96,498       | (2,012)         | 94,486        |
| Noninterest Income   | 26,346                    | 11,442                        | 18,068                         | 55,856       | 5,386           | 61,242        |
| Noninterest Expense  | (41,653)                  | (22,430)                      | (16,074)                       | (80,157)     | (1,293)         | (81,450)      |
| Income Before Provision for<br>Income Taxes                        | 39,750                    | 26,878                        | 5,569                          | 72,197       | 2,081           | 74,278        |
| Provision for Income Taxes   | (14,707)                  | (9,948)                       | (2,060)                        | (26,715)     | 216             | (26,499)      |
| Allocated Net Income   | 25,043                    | 16,930                        | 3,509                          | 45,482       | 2,297           | 47,779        |
| Allowance Funding Value  | (166)                     | (824)                         | (11)                           | (1,001)      | 1,001           |               |
| Provision for Credit Losses  | 1,773                     | 2,486                         | (1)                            | 4,258        | (188)           | 4,070         |
| Economic Provision   | (1,906)                   | (3,190)                       | (87)                           | (5,183)      |                 | (5,183)       |
| Tax Effect of Adjustments  | 111                       | 564                           | 37                             | 712          | (300)           | 412           |
| Income Before Capital Charge                                       | 24,855                    | 15,966                        | 3,447                          | 44,268       | 2,810           | 47,078        |
| Capital Charge   | (5,132)                   | (4,380)                       | (1,572)                        | (11,084)     | (8,948)         | (20,032)      |
| <b>Net Income (Loss) After Capital<br/>Charge (NIACC)</b>          | \$ 19,723                 | \$ 11,586                     | \$ 1,875                       | \$ 33,184    | \$ (6,138)      | \$ 27,046     |
| <b>RAROC (ROE for the<br/>Company)</b>                             | 53%                       | 40%                           | 24%                            | 44%          | 9%              | 26%           |
| <b>Total Assets as of September 30,<br/>2007 2</b>                 | \$ 3,651,121              | \$ 3,118,106                  | \$ 216,795                     | \$ 6,986,022 | \$ 3,563,573    | \$ 10,549,595 |

1 Business segment results have been revised for the three months ended September 30, 2008, since reported in our Form 8-K filing on October 27, 2008.

2 Certain prior period information has been reclassified to conform to the current presentation.



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| Business Segments Selected Financial Information (Unaudited) |                   |                       |                        |              |              | Table 15b             |
|--|-------------------|-----------------------|------------------------|--------------|--------------|-----------------------|
| (dollars in thousands)                                       | Retail<br>Banking | Commercial<br>Banking | Investment<br>Services | Total        | Treasury     | Consolidated<br>Total |
| <b>Nine Months Ended</b>                                     |                   |                       |                        |              |              |                       |
| <b>September 30, 2008 1</b>                                  |                   |                       |                        |              |              |                       |
| Net Interest Income  | \$ 176,207        | \$ 122,663            | \$ 11,731              | \$ 310,601   | \$ 2,322     | \$ 312,923            |
| Provision for Credit Losses                                  | 15,999            | 25,704                | 1,089                  | 42,792       | (835)        | 41,957                |
| Net Interest Income After<br>Provision                       |                   |                       |                        |              |              |                       |
| for Credit Losses  | 160,208           | 96,959                | 10,642                 | 267,809      | 3,157        | 270,966               |
| Noninterest Income   | 83,196            | 42,753                | 54,738                 | 180,687      | 22,963       | 203,650               |
| Noninterest Expense  | (130,813)         | (72,753)              | (50,026)               | (253,592)    | (10,492)     | (264,084)             |
| Income Before Provision for<br>Income Taxes                  | 112,591           | 66,959                | 15,354                 | 194,904      | 15,628       | 210,532               |
| Provision for Income Taxes                                   | (41,660)          | (26,273)              | (5,681)                | (73,614)     | 15,988       | (57,626)              |
| Allocated Net Income   | 70,931            | 40,686                | 9,673                  | 121,290      | 31,616       | 152,906               |
| Allowance Funding Value                                      | (626)             | (2,654)               | (42)                   | (3,322)      | 3,322        |                       |
| Provision for Credit Losses                                  | 15,999            | 25,704                | 1,089                  | 42,792       | (835)        | 41,957                |
| Economic Provision   | (6,000)           | (9,715)               | (243)                  | (15,958)     | (2)          | (15,960)              |
| Tax Effect of Adjustments                                    | (3,468)           | (4,934)               | (297)                  | (8,699)      | (920)        | (9,619)               |
| Income Before Capital Charge                                 | 76,836            | 49,087                | 10,180                 | 136,103      | 33,181       | 169,284               |
| Capital Charge   | (14,308)          | (12,260)              | (4,384)                | (30,952)     | (27,421)     | (58,373)              |
| <b>Net Income (Loss) After Capital<br/>Charge (NIACC)</b>    | \$ 62,528         | \$ 36,827             | \$ 5,796               | \$ 105,151   | \$ 5,760     | \$ 110,911            |
| <b>RAROC (ROE for the<br/>Company)</b>                       |                   |                       |                        |              |              |                       |
|  | 54%               | 40%                   | 23%                    | 44%          | 58%          | 26%                   |
| <b>Total Assets as of September 30,<br/>2008</b>             |                   |                       |                        |              |              |                       |
|  | \$ 3,669,924      | \$ 3,023,242          | \$ 285,497             | \$ 6,978,663 | \$ 3,356,384 | \$ 10,335,047         |
| <b>Nine Months Ended</b>                                     |                   |                       |                        |              |              |                       |
| <b>September 30, 2007 2</b>                                  |                   |                       |                        |              |              |                       |
| Net Interest Income (Loss)                                   | \$ 166,855        | \$ 120,050            | \$ 10,565              | \$ 297,470   | \$ (1,899)   | \$ 295,571            |
| Provision for Credit Losses                                  | 4,576             | 5,700                 | (1)                    | 10,275       | (211)        | 10,064                |
| Net Interest Income (Loss) After<br>Provision                |                   |                       |                        |              |              |                       |
| for Credit Losses  | 162,279           | 114,350               | 10,566                 | 287,195      | (1,688)      | 285,507               |
| Noninterest Income   | 78,714            | 31,689                | 56,669                 | 167,072      | 13,158       | 180,230               |
| Noninterest Expense  | (124,096)         | (67,667)              | (47,276)               | (239,039)    | (4,366)      | (243,405)             |
| Income Before Provision for<br>Income Taxes                  | 116,897           | 78,372                | 19,959                 | 215,228      | 7,104        | 222,332               |
| Provision for Income Taxes                                   | (43,246)          | (28,881)              | (7,385)                | (79,512)     | 23           | (79,489)              |
| Allocated Net Income   | 73,651            | 49,491                | 12,574                 | 135,716      | 7,127        | 142,843               |
| Allowance Funding Value                                      | (466)             | (2,405)               | (31)                   | (2,902)      | 2,902        |                       |
| Provision for Credit Losses                                  | 4,576             | 5,700                 | (1)                    | 10,275       | (211)        | 10,064                |
| Economic Provision   | (5,598)           | (9,629)               | (251)                  | (15,478)     | (1)          | (15,479)              |
| Tax Effect of Adjustments                                    | 551               | 2,344                 | 104                    | 2,999        | (995)        | 2,004                 |
| Income Before Capital Charge                                 | 72,714            | 45,501                | 12,395                 | 130,610      | 8,822        | 139,432               |
| Capital Charge   | (15,300)          | (13,215)              | (4,634)                | (33,149)     | (26,453)     | (59,602)              |
| <b>Net Income (Loss) After Capital<br/>Charge (NIACC)</b>    | \$ 57,414         | \$ 32,286             | \$ 7,761               | \$ 97,461    | \$ (17,631)  | \$ 79,830             |
| <b>RAROC (ROE for the<br/>Company)</b>                       |                   |                       |                        |              |              |                       |
|  | 52%               | 38%                   | 29%                    | 43%          | 9%           | 26%                   |
| <b>Total Assets as of September 30,<br/>2007 2</b>           |                   |                       |                        |              |              |                       |
|  | \$ 3,651,121      | \$ 3,118,106          | \$ 216,795             | \$ 6,986,022 | \$ 3,563,573 | \$ 10,549,595         |

1 Business segment results have been revised for the nine months ended September 30, 2008, since reported in our Form 8-K filing on October 27, 2008.

2 Certain prior period information has been reclassified to conform to the current presentation.

*Retail Banking*

Retail Banking offers a broad range of financial products and services to consumers and small businesses. Loan products include residential mortgage loans, home equity lines of credit, personal lines of credit, and installment loans. Deposit products include checking, savings, and time deposit accounts. Retail Banking also provides merchant services to its small business customers. Products and services from Retail Banking are delivered to customers through 72 Hawaii branch locations, 467 ATMs throughout Hawaii and the Pacific Islands, e-Bankoh (on-line banking service), a 24-hour customer service center, and a mobile banking service. This segment also offers retail property and casualty insurance products.

NIACC improved for the third quarter of 2008 compared to the same period in 2007, primarily due to higher net interest

income and noninterest income, partially offset by higher noninterest expense. The \$1.4 million increase in net interest income was primarily due to a reduction in funding costs and growth in average loan balances. These positive factors were partially offset by a decrease in average deposit balances. The \$1.0 million increase in noninterest income was primarily due to a \$1.0 million increase in mortgage banking income, excluding the net change in the fair value of mortgage servicing rights due to valuation assumptions and the fair value of Designated Securities which are both recorded in the Treasury segment. Noninterest expense increased by \$2.1 million primarily due to higher salaries and benefits, and occupancy expense, as well as higher allocated expenses related to earnings-based incentive compensation that was accrued during the third quarter of 2008. Retail Banking's economic provision and capital charge remained relatively unchanged in the third quarter of 2008 compared to the same period in 2007.







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Financial measures improved for the first nine months of 2008 compared to the same period in 2007, primarily due to an increase in net interest income and noninterest income, partially offset by higher noninterest expense. The \$9.4 million increase in net interest income was primarily due to lower funding costs on the segment's deposit portfolio and growth in average loan balances. These positive factors were partially offset by a decrease in average deposit balances. The \$4.5 million increase in noninterest income was primarily due to a \$3.0 million increase in mortgage banking income, excluding the net change in the fair value of mortgage servicing rights due to valuation assumptions and the fair value of Designated Securities which are both recorded in the Treasury segment. Also contributing to the increase in noninterest income was higher fee income from overdraft fees and debit card transactions. Noninterest expense increased by \$6.7 million primarily due to increased debit card, occupancy, and salaries and benefits expense, as well as higher allocated expenses related to earnings-based incentive compensation that was accrued for in the first and third quarters of 2008. Retail Banking's capital charge decreased slightly for the first nine months of 2008 compared to the same period in 2007, primarily due to a decrease in the capital charge rate.

#### *Commercial Banking*

Commercial Banking offers a broad range of financial products and services including corporate and commercial real estate loans, lease financing, auto dealer financing, automobile loans and leases, deposit and cash management products, and wholesale property and casualty insurance products. Lending, deposit, and cash management services are offered to middle-market and large companies in Hawaii. Commercial real estate mortgages are focused on customers that include investors, developers, and builders domiciled in Hawaii. Commercial Banking also includes international banking and operations at our 12 branches in the Pacific Islands.

Financial measures decreased for the third quarter of 2008 compared to the same period in 2007, primarily due to a decrease in net interest income and noninterest income and an increase in noninterest expense. The \$3.8 million decrease in net interest income was primarily due to the settlement of our SILO transactions. The \$0.9 million decrease in noninterest income was primarily due to lower contingent fee income on

our wholesale property and casualty insurance products. This decrease, however, was partially offset by higher account analysis fees as a result of lower earnings credit rates on customer accounts and income from facilitating interest rate swaps on behalf of our customers. Noninterest expense increased by \$2.1 million primarily due to higher salaries and benefits, and allocated expenses. The increase in the Provision allocated to the segment was primarily due to heightened risk in three specific loan exposures and to general risk from the weakening economy in Hawaii and the Mainland U.S.

Financial measures improved for the first nine months of 2008 compared to the same period in 2007, primarily due to an increase in noninterest income and net interest income. The \$11.1 million increase in noninterest income was primarily due to the \$11.6 million pre-tax gain on the sale of our equity interest in an aircraft lease in the first quarter of 2008. The \$2.6 million increase in net interest income was primarily due to a reduction in funding costs along with growth in our International Banking deposit portfolio. These positive factors were partially offset by a \$5.1 million increase in noninterest expense, primarily related to higher salaries and benefits, other operating, and allocated expenses. The increase in the Provision allocated to the segment was primarily due to heightened risk in three specific loan exposures and to general risk from the weakening economy in Hawaii and the Mainland U.S.

#### *Investment Services*

Investment Services includes private banking, trust services, asset management, and institutional investment advisory services. A significant portion of this segment's income is derived from fees, which are generally based on the market values of assets under management. The private banking and personal trust group assists individuals and families in building and preserving their wealth by providing investment, credit, and trust services to high-net-worth individuals. The asset management group manages portfolios and creates investment products. Institutional sales and service offers investment advice to corporations, government entities, and foundations. This segment also provides a full service brokerage offering equities, mutual funds, life insurance, and annuity products.





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Financial measures decreased for the third quarter of 2008 compared to the same period in 2007, primarily due to a decrease in noninterest income and an increase in noninterest expense, partially offset by an increase in net interest income. The \$0.6 million decrease in noninterest income was primarily due to lower mutual fund investment advisory fees, a result of lower assets under administration. The \$0.7 million increase in noninterest expense was primarily due to higher salaries and benefits, and allocated expenses related to earnings-based incentive compensation. This was partially offset by an increase in net interest income due to a reduction in funding costs on the segment's deposit balances.

Financial measures decreased for the first nine months of 2008 compared to the same period in 2007, primarily due to a decrease in noninterest income and an increase in noninterest expense, partially offset by an increase in net interest income. The \$1.9 million decrease in noninterest income was primarily due to lower mutual fund investment advisory fees, a result of lower assets under administration. The \$2.8 million increase in noninterest expense was primarily due to higher salaries and benefits, and allocated expenses related to the earnings-based incentive compensation accruals that were made in the first and third quarters of 2008. This was partially offset by an increase in net interest income due to a reduction in funding costs on the segment's deposit balances.

### *Treasury*

Treasury consists of corporate asset and liability management activities, including interest rate risk management and a foreign exchange business. This segment's assets and liabilities (and related interest income and expense) consist of interest-bearing deposits, investment securities, federal funds sold and purchased, government deposits, and short- and long-term borrowings. The primary sources of noninterest income are from BOLI and foreign exchange income related to customer driven currency requests from merchants and island visitors. The net residual effect of the transfer pricing of assets and liabilities is included in Treasury, along with eliminations of intercompany transactions.

Financial measures improved for the third quarter of 2008 compared to the same period in 2007, primarily due to the tax benefit related to our SILO transactions and higher net interest income, partially offset by lower noninterest income and higher noninterest expense. The \$7.1 million increase in net

interest income was primarily due to a reduction in loan funding charges allocated to the business segments, and decreases in the cost of securities sold under agreements to repurchase, funds purchased, and long-term debt. The \$3.7 million decrease in noninterest income was primarily due to a \$4.4 million net change in the fair value of our mortgage servicing rights due to changes in valuation assumptions and the fair value of our Designated Securities. This was partially offset by a \$0.5 million increase in BOLI income and a \$0.7 million increase in the fair value of our subordinated notes. The increase in the benefit for income taxes related to the segment was primarily due to the \$12.9 million credit related to our SILO transactions. The \$0.2 million increase in the capital charge for the third quarter of 2008 compared to the same period in 2007 was primarily due to an increase in excess equity held by the Company.

Financial measures improved for the first nine months of 2008 compared to the same period in 2007, primarily due to the tax benefit related to our SILO transactions and an increase in noninterest income and net interest income, partially offset by an increase in noninterest expense. The \$9.8 million increase in noninterest income was primarily due to the \$13.7 million pre-tax gain from the mandatory redemption of our Visa shares. The increase in net interest income was primarily due to a decrease in the cost of our securities sold under agreements to repurchase. These positive factors were partially offset by a \$6.1 million increase in noninterest expense primarily due to several accruals (cash awards to purchase our stock, legal contingencies, and a contribution to the Bank of Hawaii Charitable Foundation and other charitable organizations), partially offset by the reversal of the previously recorded contingency accruals related to Visa. The increase in the benefit for income taxes related to the segment was primarily due to the \$12.9 million credit related to our SILO transactions. The capital charge increased by \$1.0 million for the first nine months of 2008 compared to the same period in 2007, primarily due to an increase in excess equity held by the Company.

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Other organizational units (Technology, Operations, Marketing, Human Resources, Finance, Credit and Risk Management, and Corporate and Regulatory Administration) included in Treasury provided a wide-range of support to our other income earning segments. Expenses incurred by these support units are charged to the business segments through an internal cost allocation process.





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## Corporate Risk Profile

### *Credit Risk*

Our overall credit risk position remained relatively stable during the third quarter of 2008, with low, albeit increasing, levels of non-performing assets compared to December 31, 2007. Our credit risk profile reflects our continued disciplined underwriting approach. During the third quarter of 2008, signs of slowing in the Hawaii economy became more prominent. Reduced airline capacity, higher air travel fares, a slowing economy on the Mainland U.S., and the exit of cruise ships from the local market are resulting in lower visitor arrivals. Trends in the construction and real estate industries are also slowing. Unemployment levels are trending upward from record low levels. We expect inflation to moderate in future periods. The slowing economy in Hawaii may result in higher delinquencies and loss rates in our loan and lease portfolio, with the primary impact expected in our small business and unsecured consumer lending portfolios. We also have elevated risk in our air and other transportation, and commercial real estate exposures due to a weaker economy in Hawaii and the Mainland U.S.

Table 16 summarizes our air transportation credit exposure. As of September 30, 2008, included in our commercial lending portfolio are nine leveraged leases on aircraft that were originated in the 1990's and prior. Outstanding credit exposure related to these leveraged leases was \$70.9 million as of September 30, 2008. Our air transportation credit exposure decreased from December 2007 due to the sale of our equity interest in an aircraft lease in the first quarter of 2008. However, relative to our total loan and lease portfolio, domestic air transportation carriers continue to demonstrate a higher risk profile due to fuel costs, pension plan obligations, and marginal pricing power. We believe that volatile fuel costs, coupled with a slowing Mainland U.S. economy, will place additional pressure on the financial health of air transportation carriers for the foreseeable future. In the evaluation of the Reserve for Credit Losses (the Reserve), we continue to consider the ongoing financial concerns about the air transportation industry.

**Air Transportation Credit Exposure 1 (Unaudited)**
**Table 16**

| (dollars in thousands)                             | September 30,<br>2008 | June 30,<br>2008 | March 31,<br>2008 | December 31,<br>2007 | September 30,<br>2007 |
|--|-----------------------|------------------|-------------------|----------------------|-----------------------|
| Passenger Carriers Based In the United States      | \$ 60,260             | \$ 60,603        | \$ 61,190         | \$ 64,947            | \$ 64,867             |
| Passenger Carriers Based Outside the United States | 5,809                 | 7,161            | 7,258             | 19,078               | 19,162                |
| Cargo Carriers                                     | 13,689                | 13,568           | 13,472            | 13,390               | 13,326                |
| <b>Total Air Transportation Credit Exposure</b>    | <b>\$ 79,758</b>      | <b>\$ 81,332</b> | <b>\$ 81,920</b>  | <b>\$ 97,415</b>     | <b>\$ 97,355</b>      |

1 Exposure includes loans, leveraged leases, and operating leases.

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Table 17 presents information on non-performing assets ( NPAs ) and accruing loans and leases past due 90 days or more.

| <b>Non-Performing Assets and Accruing Loans and Leases Past Due 90 Days or More (Unaudited)</b>                 |                      |                     |                     |                     | <b>Table 17</b>      |
|---|----------------------|---------------------|---------------------|---------------------|----------------------|
|   | <b>September 30,</b> | <b>June 30,</b>     | <b>March 31,</b>    | <b>December 31,</b> | <b>September 30,</b> |
| (dollars in thousands)  | <b>2008</b>          | <b>2008</b>         | <b>2008</b>         | <b>2007</b>         | <b>2007 1</b>        |
| <b>Non-Performing Assets</b>  |                      |                     |                     |                     |                      |
| Non-Accrual Loans and Leases  |                      |                     |                     |                     |                      |
| Commercial  |                      |                     |                     |                     |                      |
| Commercial and Industrial   | \$ 574               | \$ 1,119            | \$ 794              | \$ 598              | \$ 359               |
| Commercial Mortgage   |                      |                     |                     | 112                 | 123                  |
| Lease Financing   | 149                  | 329                 | 504                 | 297                 |                      |
| Total Commercial  | 723                  | 1,448               | 1,298               | 1,007               | 482                  |
| Consumer  |                      |                     |                     |                     |                      |
| Residential Mortgage  | 3,749                | 3,784               | 3,235               | 2,681               | 3,237                |
| Home Equity   | 1,162                | 1,189               | 1,187               | 1,414               | 436                  |
| Other 2   |                      | 30                  | 31                  |                     |                      |
| Total Consumer  | 4,911                | 5,003               | 4,453               | 4,095               | 3,673                |
| Total Non-Accrual Loans and Leases  | 5,634                | 6,451               | 5,751               | 5,102               | 4,155                |
| Foreclosed Real Estate  | 293                  | 229                 | 294                 | 184                 | 105                  |
| <b>Total Non-Performing Assets</b>  | <b>\$ 5,927</b>      | <b>\$ 6,680</b>     | <b>\$ 6,045</b>     | <b>\$ 5,286</b>     | <b>\$ 4,260</b>      |
| <b>Accruing Loans and Leases Past Due 90 Days or More</b>   |                      |                     |                     |                     |                      |
| Commercial  |                      |                     |                     |                     |                      |
| Commercial and Industrial   | \$                   | \$                  | \$ 24               | \$                  | \$                   |
| Consumer  |                      |                     |                     |                     |                      |
| Residential Mortgage  | 3,455                | 2,601               | 3,892               | 4,884               | 639                  |
| Home Equity   | 296                  | 201                 | 328                 | 413                 | 115                  |
| Automobile  | 758                  | 625                 | 865                 | 1,174               | 734                  |
| Other 2   | 926                  | 756                 | 725                 | 1,112               | 944                  |
| Total Consumer  | 5,435                | 4,183               | 5,810               | 7,583               | 2,432                |
| <b>Total Accruing Loans and Leases Past Due 90 Days or More</b>   | <b>\$ 5,435</b>      | <b>\$ 4,183</b>     | <b>\$ 5,834</b>     | <b>\$ 7,583</b>     | <b>\$ 2,432</b>      |
| <b>Total Loans and Leases</b>   | <b>\$ 6,539,458</b>  | <b>\$ 6,518,128</b> | <b>\$ 6,579,337</b> | <b>\$ 6,580,861</b> | <b>\$ 6,599,915</b>  |
| Ratio of Non-Accrual Loans and Leases to Total Loans and Leases   |                      |                     |                     |                     |                      |
|   | 0.09%                | 0.10%               | 0.09%               | 0.08%               | 0.06%                |
| Ratio of Non-Performing Assets to Total Loans and Leases and Foreclosed Real Estate                             |                      |                     |                     |                     |                      |
|   | 0.09%                | 0.10%               | 0.09%               | 0.08%               | 0.06%                |
| Ratio of Commercial Non-Performing Assets to Total Commercial Loans and Leases                                  |                      |                     |                     |                     |                      |
|   | 0.03%                | 0.06%               | 0.05%               | 0.04%               | 0.02%                |
| Ratio of Consumer Non-Performing Assets to Total Consumer Loans and Leases and Foreclosed Real Estate           |                      |                     |                     |                     |                      |
|   | 0.13%                | 0.13%               | 0.11%               | 0.10%               | 0.09%                |
| Ratio of Non-Performing Assets and Accruing Loans and Leases Past Due 90 Days or More to Total Loans and Leases |                      |                     |                     |                     |                      |
|   | 0.17%                | 0.17%               | 0.18%               | 0.20%               | 0.10%                |

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| Quarter to Quarter Changes in<br>Non-Performing Assets |    |         |    |         |                            |
|--|----|---------|----|---------|----------------------------|
| Balance at Beginning of Quarter                        | \$ | 6,680   | \$ | 6,045   | \$ 5,286 \$ 4,260 \$ 6,314 |
| Additions  |    | 1,355   |    | 2,900   | 2,614 1,866 662            |
| Reductions   |    |         |    |         |                            |
| Payments   |    | (955)   |    | (630)   | (386) (256) (1,741)        |
| Return to Accrual Status                               |    | (756)   |    | (943)   | (944) (214) (787)          |
| Sales of Foreclosed Real Estate                        |    |         |    |         | (161) (48)                 |
| Charge-offs/Write-downs                                |    | (397)   |    | (692)   | (525) (209) (140)          |
| Total Reductions                                       |    | (2,108) |    | (2,265) | (1,855) (840) (2,716)      |
| Balance at End of Quarter                              | \$ | 5,927   | \$ | 6,680   | \$ 6,045 \$ 5,286 \$ 4,260 |

1 Certain prior period information has been reclassified to conform to the current presentation.

2 Comprised of other revolving credit, installment, and lease financing.

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The changes in NPAs by category from December 31, 2007 and September 30, 2007 reflect normal delinquency and resolution activity consistent with the slowing economy in Hawaii.

Included in NPAs are loans and leases that we consider impaired. Impaired loans and leases are defined as those which we believe it is probable we will not collect all amounts due according to the contractual terms of the loan or lease agreement, as well as those loans or leases whose terms have been modified in a troubled debt restructuring. There were no impaired loans as of September 30, 2008. Impaired loans were less than \$0.1 million as of December 31, 2007 and \$0.2 million as of September 30, 2007.

Credit quality in our commercial and mortgage-related consumer lending portfolios remained stable during the third quarter of 2008. Residential mortgage and home equity lending comprise the largest components of our consumer lending portfolio. As of September 30, 2008, the weighted average credit score for our residential mortgage loan portfolio

was 756, with 96% of this portfolio having a loan-to-value ratio of 80% or less. As of September 30, 2008, the weighted average credit score for our home equity loan portfolio was 747, with the majority of the portfolio having a loan-to-value ratio of 80% or less.

### *Loans and Leases Past Due 90 Days or More and Still Accruing Interest*

The changes in loans and leases past due 90 days or more and still accruing interest from December 31, 2007 and September 30, 2007 reflect normal delinquency and resolution activity consistent with the slowing economy in Hawaii. We do not expect to incur material losses on these loans and leases.

Due to the low volume of NPAs and accruing loans and leases past due 90 days or more, we anticipate some degree of variability in the balances in these categories from period to period and do not consider modest changes to be indicative of significant asset quality trends.





Table of Contents*Reserve for Credit Losses*

Table 18 presents the activity in our Reserve for the three and nine months ended September 30, 2008 and 2007.

**Reserve for Credit Losses (Unaudited)****Table 18**

|  | <b>Three Months Ended</b> |                     | <b>Nine Months Ended</b> |                     |
|--|---------------------------|---------------------|--------------------------|---------------------|
|  | <b>September 30,</b>      |                     | <b>September 30,</b>     |                     |
| (dollars in thousands)   | <b>2008</b>               | <b>2007 1</b>       | <b>2008</b>              | <b>2007 1</b>       |
| <b>Balance at Beginning of Period</b>                              | \$ 107,667                | \$ 96,167           | \$ 96,167                | \$ 96,167           |
| Loans and Leases Charged-Off                                       |                           |                     |                          |                     |
| Commercial   |                           |                     |                          |                     |
| Commercial and Industrial  | (1,783)                   | (715)               | (4,568)                  | (2,258)             |
| Lease Financing  | (27)                      | (123)               | (303)                    | (145)               |
| Consumer   |                           |                     |                          |                     |
| Residential Mortgage   | (398)                     |                     | (531)                    | (47)                |
| Home Equity  | (519)                     | (422)               | (1,798)                  | (764)               |
| Automobile   | (2,858)                   | (2,215)             | (7,960)                  | (7,642)             |
| Other 2  | (3,444)                   | (2,389)             | (8,202)                  | (6,871)             |
| <b>Total Loans and Leases Charged-Off</b>                          | <b>(9,029)</b>            | <b>(5,864)</b>      | <b>(23,362)</b>          | <b>(17,727)</b>     |
| Recoveries on Loans and Leases Previously Charged-Off              |                           |                     |                          |                     |
| Commercial   |                           |                     |                          |                     |
| Commercial and Industrial  | 220                       | 326                 | 1,407                    | 918                 |
| Commercial Mortgage  |                           | 35                  |                          | 156                 |
| Lease Financing  | 2                         | 2                   | 7                        | 2,089               |
| Consumer   |                           |                     |                          |                     |
| Residential Mortgage   | 67                        | 14                  | 162                      | 203                 |
| Home Equity  | 36                        | 69                  | 83                       | 189                 |
| Automobile   | 699                       | 596                 | 2,195                    | 1,980               |
| Other 2  | 647                       | 752                 | 2,051                    | 2,128               |
| <b>Total Recoveries on Loans and Leases Previously Charged-Off</b> | <b>1,671</b>              | <b>1,794</b>        | <b>5,905</b>             | <b>7,663</b>        |
| <b>Net Loans and Leases Charged-Off</b>                            | <b>(7,358)</b>            | <b>(4,070)</b>      | <b>(17,457)</b>          | <b>(10,064)</b>     |
| Provision for Credit Losses  | 20,358                    | 4,070               | 41,957                   | 10,064              |
| <b>Balance at End of Period 3</b>                                  | <b>\$ 120,667</b>         | <b>\$ 96,167</b>    | <b>\$ 120,667</b>        | <b>\$ 96,167</b>    |
| <b>Components</b>  |                           |                     |                          |                     |
| Allowance for Loan and Lease Losses                                | \$ 115,498                | \$ 90,998           | \$ 115,498               | \$ 90,998           |
| Reserve for Unfunded Commitments                                   | 5,169                     | 5,169               | 5,169                    | 5,169               |
| <b>Total Reserve for Credit Losses</b>                             | <b>\$ 120,667</b>         | <b>\$ 96,167</b>    | <b>\$ 120,667</b>        | <b>\$ 96,167</b>    |
| <b>Average Loans and Leases Outstanding</b>                        | <b>\$ 6,512,453</b>       | <b>\$ 6,570,261</b> | <b>\$ 6,543,871</b>      | <b>\$ 6,554,979</b> |
| Ratio of Net Loans and Leases Charged-Off to                       |                           |                     |                          |                     |
| Average Loans and Leases Outstanding (annualized)                  | 0.45%                     | 0.25%               | 0.36%                    | 0.21%               |
| Ratio of Allowance for Loan and Lease Losses to                    |                           |                     |                          |                     |
| Loans and Leases Outstanding                                       | 1.77%                     | 1.38%               | 1.77%                    | 1.38%               |

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- 1 Certain prior period information has been reclassified to conform to the current presentation.
- 2 Comprised of other revolving credit, installment, and lease financing.
- 3 Included in this analysis is activity related to the Company's reserve for unfunded commitments, which is separately recorded in other liabilities in the Consolidated Statements of Condition (Unaudited).

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We maintain a Reserve which consists of two components, the Allowance and a Reserve for Unfunded Commitments ( Unfunded Reserve ). The Reserve provides for the risk of credit losses inherent in the loan and lease portfolio and is based on loss estimates derived from a comprehensive quarterly evaluation. The evaluation reflects analyses of individual borrowers and historical loss experience, supplemented as necessary by credit judgment that considers observable trends, conditions, other relevant environmental and economic factors.



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The level of the Allowance is adjusted by recording an expense or recovery through the Provision. The level of the Unfunded Reserve is adjusted by recording an expense or recovery in other noninterest expense. The Provision exceeded net charge-offs of loans and leases for the third quarter of 2008 by \$13.0 million and by \$24.5 million for the first nine months of 2008. As of September 30, 2008, the Allowance was \$115.5 million or 1.77% of total loans and leases outstanding. This represents an increase of 39 basis points from December 31, 2007 and September 30, 2007. The increase in the Allowance during the first nine months of 2008 was due to heightened risk in three specific loan exposures and to general risk from the weakening economy in Hawaii and the Mainland U.S. The increase in the Allowance during the first nine months of 2008 also reflects increased risk in our small business and unsecured consumer lending portfolios.

Although we determine the amount of each component of the Allowance separately, the Allowance as a whole was considered appropriate by management as of September 30, 2008, based on our ongoing analysis of estimated probable credit losses, credit risk profiles, economic conditions, coverage ratios, and other relevant factors.

#### *The Reserve for Unfunded Commitments*

The Unfunded Reserve remained unchanged from December 31, 2007 and September 30, 2007. The process used to determine the Unfunded Reserve is consistent with the process for determining the Allowance, as adjusted for estimated funding probabilities or loan and lease equivalency factors.

#### **Market Risk**

Market risk is the potential of loss arising from adverse changes in interest rates, illiquidity, and credit risk. We are exposed to market risk in the normal course of conducting our business activities. Financial products that expose us to market risk include investment securities, loans and leases, deposits, debt, and derivative financial instruments. Our market risk management process involves measuring, monitoring, controlling, and adjusting levels of risk that can significantly impact our statements of income and condition. In this management process, market risks are balanced with expected returns in an effort to enhance earnings performance,

while limiting volatility. In the management of market risks, activities are categorized into trading and non-trading.

Our trading activities include trading securities that are used to manage the market risk exposure of our mortgage servicing rights, the majority of which are recorded at estimated fair value on the statement of condition. Our trading activities also include foreign currency and foreign exchange contracts that expose us to a small degree of foreign currency risk. Foreign currency and foreign exchange contracts are primarily executed on behalf of our customers and at times for our own account. We also enter into interest rate swap agreements with customers to assist them in managing their interest rate risk. However, we mitigate this risk by entering into offsetting interest rate swap agreements with third parties.

Our non-trading activities include normal business transactions that expose our balance sheet to varying degrees of market risk. Our primary market risk exposure is interest rate risk. A key element in the process of managing market risk involves oversight by senior management and the Board of Directors as to the level of such risk. The Board of Directors reviews and approves risk management policies, including risk limits and guidelines, and delegates oversight functions to the Asset/Liability Management Committee (ALCO). The ALCO, consisting of senior business and finance officers, monitors market risk exposure and, as market conditions dictate, modifies positions as deemed appropriate. The ALCO may also direct the use of derivative financial instruments to manage market risk.

*Interest Rate Risk*

The objective of the interest rate risk management process is to maximize net interest income while operating within acceptable limits established for interest rate risk and maintaining adequate levels of funding and liquidity.

Our statement of condition is sensitive to changes in the general level of interest rates. This interest rate risk arises primarily from normal business activities of gathering deposits and extending loans and leases. Many other factors also affect exposure to changes in interest rates, such as general economic and financial conditions, customer preferences, historical pricing relationships, and repricing characteristics of financial instruments.





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Our earnings are affected not only by general economic conditions, but also by the monetary and fiscal policies of the U.S. government and its agencies, particularly the Board of Governors of the Federal Reserve System (the FRB). The monetary policies of the FRB influence, to a significant extent, the overall growth of loans, investment securities, deposits as well as the level of interest rates earned on assets and paid for liabilities. The nature and impact of future changes in monetary policies are generally not predictable.

In managing interest rate risk, we, through the ALCO, measure short-term and long-term sensitivities to changes in interest rates. The ALCO utilizes several techniques to manage interest rate risk, which include shifting balance sheet mix or altering the interest rate characteristics of assets and liabilities, changing product pricing strategies, or modifying characteristics of our investment securities portfolio. We are also authorized to use derivative financial instruments. However, our use of derivative financial instruments has been limited over the past several years due to the natural on-balance sheet hedge arising out of offsetting interest rate exposures from loans and investment securities with deposits and other interest-bearing liabilities. In particular, the investment securities portfolio is utilized to manage the interest rate exposure and sensitivity to within the guidelines and limits established by the ALCO. For example, we continue to utilize our trading portfolio to offset the change in our mortgage servicing rights, the majority of which is recorded at estimated fair value. Natural and offsetting hedges reduce the need to employ off-balance sheet derivative financial instruments to hedge interest rate risk exposures. Expected movements in interest rates are also considered in managing interest rate risk. Thus, as interest rates change, we may use different techniques to manage interest rate risk.

A key element in our ongoing process to measure and monitor interest rate risk is the utilization of an asset/liability simulation model. This model is used to estimate and measure the balance sheet's sensitivity to changes in interest rates.

These estimates are based on assumptions regarding the behavior of loan and deposit pricing, repayment rates on mortgage-based assets, and principal amortization and maturities on other financial instruments. The model's analytics include the effects of standard prepayment options on mortgages and customer withdrawal options for deposits. While such assumptions are inherently uncertain, management believes that these assumptions are reasonable. As a result, the simulation model attempts to capture the dynamic nature of the balance sheet and provide a sophisticated estimate rather than a precise prediction of exposure to changes in interest rates.

We utilize net interest income simulations to analyze short-term income sensitivities to changes in interest rates. Table 19 presents, as of September 30, 2008 and 2007, an estimate of the change in net interest income during a quarterly time frame that would result from a gradual 100 and 200 basis point increase or decrease in interest rates, moving in a parallel fashion over the entire yield curve, over the next 12-month period, relative to the measured base case scenario for net interest income without any change in strategy. Based on the net interest income simulation as of September 30, 2008, our net interest income sensitivity was greater than our sensitivity as of September 30, 2007 in lower interest rate scenarios, while lower than our sensitivity as of September 30, 2007 in higher interest rate scenarios, due to a decline in interest rates. In lower interest rate scenarios, limited deposit repricing will adversely impact overall net interest income. In higher interest rate scenarios, liabilities are expected to reprice slightly faster than assets. Additionally, to analyze the impact of changes in interest rates in a more realistic manner, non-parallel interest rate scenarios are also simulated. These non-parallel interest rate scenarios indicate that net interest income may decrease from the base case scenario should the yield curve become flat or inverted for a period of time. Conversely, if the yield curve should steepen further, net interest income may increase.



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**Net Interest Income Sensitivity Profile (Unaudited)**

**Table 19**

| (dollars in thousands)                         | Change in Net Interest Income Per Quarter |         |                    |                 |
|--|---|---------|--------------------|-----------------|
|  | September 30, 2008                        |         | September 30, 2007 |                 |
| <b>Change in Interest Rates (basis points)</b> |   |         |                    |                 |
| +200   | \$  | (627)   | (0.6)%             | \$ (860) (0.9)% |
| +100   |   | (104)   | (0.1)              | (326) (0.3)     |
| -100   |   | (940)   | (0.9)              | (69) (0.1)      |
| -200   |   | (2,090) | (2.0)              | (366) (0.4)     |

We also use a Market Value of Portfolio Equity ( MVPE ) sensitivity analysis to estimate the change in the net present value of our assets, liabilities, and off-balance sheet arrangements from changes in interest rates. The MVPE was approximately \$1.6 billion as of September 30, 2008 and approximately \$1.8 billion as of September 30, 2007. Table 20 presents, as of September 30, 2008 and 2007, an estimate of the change in the MVPE sensitivity that would occur from an immediate 100 and 200 basis point increase or decrease in interest rates, moving in a parallel fashion over the entire yield curve. The MVPE sensitivity increased as of September 30, 2008, compared to September 30, 2007, primarily as a result of lower interest rates, a steeper yield curve, as well as

increased interest rate volatility. Further enhancing the MVPE sensitivity analysis are value-at-risk, key rate analysis, duration of equity, exposure to basis risk, and non-parallel yield curve shift analyses. There are inherent limitations to these measures; however, used along with the MVPE sensitivity analysis, we obtain better overall insight for managing our exposure to changes in interest rates. Based on the additional analyses, we estimate our greatest exposure is in scenarios where medium-term and long-term interest rates rise while short-term interest rates remain unchanged and when the spread between the U.S. Treasury and LIBOR rates decrease ( spread narrowing ).

**Market Value of Equity Sensitivity Profile (Unaudited)****Table 20**

| (dollars in thousands)                         | Change in Market Value of Equity |           |                    |                      |
|--|----------------------------------|-----------|--------------------|----------------------|
|  | September 30, 2008               |           | September 30, 2007 |                      |
| <b>Change in Interest Rates (basis points)</b> |                                  |           |                    |                      |
| +200   | \$                               | (196,695) | (12.5)%            | \$ (197,636) (11.2)% |
| +100   |                                  | (83,651)  | (5.3)              | (88,877) (5.0)       |
| -100   |                                  | (5,721)   | (0.4)              | 26,105 1.5           |
| -200   |                                  | (130,480) | (8.3)              | (43,640) (2.5)       |

## **Liquidity Management**

Liquidity is managed in an effort to ensure that we have continuous access to sufficient, reasonably priced funding to conduct our business and satisfy obligations in a normal manner.

Cash and noninterest-bearing deposits, interest-bearing deposits, and funds sold provide us with readily available sources of liquidity. Investment securities in our available-for-sale portfolio are also a near-term source of asset liquidity, although we do not have the intent to sell such investment securities that are currently in a gross unrealized loss position.

Core deposit balances (comprised of non-interest bearing demand, interest-bearing demand, and savings accounts) have historically provided a sizable source of relatively stable and low-cost funds. Time deposit balances also provide us with a relatively stable source of funds, albeit at a slightly higher cost. We are also able to utilize funds purchased, short-term borrowings, and securities sold under agreements to repurchase as a mechanism to fund growth in our loan and lease portfolio.

We are a member of the FHLB, which provides an additional source of short-term and long-term funding. Outstanding borrowings from the FHLB were \$50.0 million as of September 30, 2008, December 31, 2007 and September 30, 2007 with a weighted average interest rate of 4%.





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Additionally, a \$1.0 billion senior and subordinated bank note program is available. Under this program, we may issue additional notes provided that the aggregate amount outstanding does not exceed \$1.0 billion. The unpaid principal amount of our subordinated notes outstanding under this bank note program was \$119.0 million as of September 30, 2008 and \$124.9 million as of December 31, 2007 and September 30, 2007. These subordinated notes bear a fixed interest rate of 6.875% and will mature in March 2009.

### Capital Management

The Parent and the Bank are subject to regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can cause certain mandatory and discretionary actions by regulators that, if undertaken, could have a material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Parent and the Bank must meet specific capital guidelines that involve quantitative and qualitative measures. These measures were established by regulation to ensure capital adequacy. As of September 30, 2008, the Parent and the Bank were well capitalized under this regulatory framework. There have been no conditions or events since September 30, 2008 that management believes have changed either the Parent's or the Bank's capital classifications.

As of September 30, 2008, the fair value of our subordinated notes of \$120.6 million, recorded as a component of long-term debt on our statements of condition, no longer qualified as a component of Total Capital for regulatory capital purposes due to the maturity of our subordinated notes being within 12 months from September 30, 2008.

As of September 30, 2008, our leverage ratio was 7.27%. We actively manage our capital toward a leverage ratio that is adjusted periodically in consideration of market conditions. Our ability to manage toward a particular leverage ratio is aided by our strong capital structure, strong earnings and core deposit base, alternative sources of liquidity, and our ongoing share repurchase program.

From January 1, 2008 through September 18, 2008, we repurchased 1.2 million shares of common stock under our share repurchase program at an average cost of \$48.90 per share, totaling \$58.9 million. From the beginning of our share repurchase program in July 2001 through September 18, 2008, we repurchased a total of 45.6 million shares of common stock and returned \$1.6 billion to our shareholders at an average cost of \$35.44 per share. Since September 18, 2008, we have not repurchased shares of our common stock in order to further build our capital levels. We continue to monitor our capital position and will resume our share repurchases when deemed appropriate. On October 24, 2008, our Board of Directors increased the authorization under the share repurchase program by an additional \$50.0 million. This new authorization, combined with the previously announced authorization of \$1.65 billion, brings the total share repurchase authority of our common stock to \$1.70 billion.

In October 2008, our Board of Directors declared a quarterly cash dividend of \$0.45 per share on our outstanding shares, which represents an increase of \$0.01 from the dividend declared for the previous three quarters. The dividend will be payable on December 12, 2008 to our shareholders of record at the close of business on November 28, 2008.



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Table 21 presents our regulatory capital and ratios as of September 30, 2008, December 31, 2007, and September 30, 2007.

**Regulatory Capital and Ratios (Unaudited)**

|  |  | <b>September 30,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>Table 21<br/>September 30,<br/>2007</b> |
|--|--|-------------------------------|------------------------------|--|
| (dollars in thousands)                                       |  |                               |                              |  |
| <b>Regulatory Capital</b>                                    |  |                               |                              |  |
| Shareholders' Equity   |  | \$ 780,020                    | \$ 750,255                   | \$ 731,697                                 |
| Add:   | Capital Securities of Bancorp Hawaii Capital Trust I     |                               | 26,425                       | 26,425                                     |
| Less:  | Cumulative Change in Fair Value of Financial Liabilities |                               |                              |  |
|  | Accounted for Under the Fair Value Option                | (1,428)                       |                              |  |
|  | Goodwill   | 34,959                        | 34,959                       | 34,959                                     |
|  | Postretirement Benefit Liability Adjustments             | 8,274                         | 8,647                        | 6,731                                      |
|  | Net Unrealized Losses on Investment Securities           |                               |                              |  |
|  | Available-for-Sale                                       | (15,086)                      | (1,388)                      | (17,403)                                   |
|  | Other Assets   | 2,771                         | 2,759                        | 2,841                                      |
| Tier 1 Capital   |  | 750,530                       | 731,703                      | 730,994                                    |
| Allowable Reserve for Credit Losses                          |  | 84,663                        | 88,716                       | 90,058                                     |
| Qualifying Subordinated Debt                                 |  |                               | 24,982                       | 24,979                                     |
| Unrealized Gains on Investment Securities Available-for-Sale |  |                               | 59                           | 32   |
| <b>Total Regulatory Capital</b>                              |  | \$ 835,193                    | \$ 845,460                   | \$ 846,063                                 |
| <b>Risk-Weighted Assets</b>                                  |  | \$ 6,737,044                  | \$ 7,089,846                 | \$ 7,198,547                               |
| <b>Key Regulatory Capital Ratios</b>                         |  |                               |                              |  |
| Tier 1 Capital Ratio 1                                       |  | 11.14%                        | 10.32%                       | 10.15%                                     |
| Total Capital Ratio 2  |  | 12.40                         | 11.92                        | 11.75                                      |
| Leverage Ratio 3   |  | 7.27                          | 7.02                         | 6.92                                       |

1 Tier 1 capital ratio as of December 31, 2007 and September 30, 2007 was corrected from 10.36% and 10.19%, respectively.

2 Total capital ratio as of December 31, 2007 and September 30, 2007 was corrected from 11.96% and 11.79%, respectively.

3 Leverage ratio as of December 31, 2007 and September 30, 2007 was corrected from 7.04% and 6.95%, respectively.

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The corrections to our Regulatory Capital Ratios as of December 31, 2007 and September 30, 2007 did not change our well capitalized position, as defined in the regulatory framework for prompt corrective action, as previously reported.

### **Off-Balance Sheet Arrangements, Credit Commitments, and Contractual Obligations**

#### *Off-Balance Sheet Arrangements*

We do not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as variable-

which would have been established for the purpose of facilitating off-balance sheet arrangements.

#### *Contractual Obligations*

Our contractual obligations have not changed materially since previously reported in our Annual Report on Form 10-K for the year ended December 31, 2007.

#### *Credit Commitments*

Table 22 presents our credit commitments as of September 30, 2008:

interest entities,

**Credit Commitments (Unaudited)**

**Table 22**

| (dollars in thousands)                | <b>Less Than<br/>One Year</b> | <b>1-3 Years</b>  | <b>4-5 Years</b>  | <b>After 5<br/>Years</b> | <b>Total</b>        |
|---------------------------------------|-------------------------------|-------------------|-------------------|--------------------------|---------------------|
| Unfunded Commitments to Extend Credit | \$ 561,860                    | \$ 428,106        | \$ 212,314        | \$ 1,250,617             | \$ 2,452,897        |
| Standby Letters of Credit             | 84,632                        | 3,779             |                   |                          | 88,411              |
| Commercial Letters of Credit          | 26,427                        |                   |                   |                          | 26,427              |
| <b>Total Credit Commitments</b>       | <b>\$ 672,919</b>             | <b>\$ 431,885</b> | <b>\$ 212,314</b> | <b>\$ 1,250,617</b>      | <b>\$ 2,567,735</b> |

Table of Contents**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

See the Market Risk section of MD&A.

**Item 4. Controls and Procedures**

The Company's management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of September 30, 2008. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2008. There were no changes in the Company's internal controls over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the third quarter of 2008 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Part II - Other Information****Item 1A. Risk Factors**

There are no material changes from the risk factors set forth under Part 1, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2007.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The Parent's repurchases of equity securities for the third quarter of 2008 were as follows:

**Issuer Purchases of Equity Securities (Unaudited)**

| Period                 | Total Number of<br>Shares Purchased 1 | Average Price<br>Paid Per Share | Total Number of Shares<br>Purchased as Part of<br>Publicly Announced Plans<br>or Programs | Approximate Dollar Value<br>of Shares that May Yet Be<br>Purchased Under the<br>Plans or Programs 2 |
|------------------------|---------------------------------------|---------------------------------|---|---|
| July 1 - 31, 2008      | 208,693                               | \$ 45.80                        | 208,500   | \$ 42,039,916   |
| August 1 - 31, 2008    | 75,647                                | 52.93                           | 74,700  | 38,085,252  |
| September 1 - 30, 2008 | 50,876                                | 55.05                           | 49,000  | 35,399,309  |
| <b>Total</b>           | <b>335,216</b>                        | <b>\$ 48.82</b>                 | <b>332,200</b>  |   |



1 The months of July, August, and September 2008 included 193, 947, and 1,876 shares, respectively, purchased from employees in connection with stock swaps, income tax withholdings related to vesting of restricted stock, and shares purchased for a Rabbi Trust. These shares were not purchased as part of the publicly announced program. The shares were purchased at the closing price of the Parent's common stock on the dates of purchase.

2 The share repurchase program was first announced in July 2001. As of September 30, 2008, the Parent's Board of Directors authorized a total of \$1.65 billion under the share repurchase program. The program has no set expiration or termination date.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

A list of exhibits to this Form 10-Q is set forth on the Exhibit Index and is incorporated herein by reference.

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**Signatures**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: October 31, 2008

Bank of Hawaii Corporation

By: /s/ Allan R. Landon  
Allan R. Landon  
Chairman of the Board and  
Chief Executive Officer

By: /s/ Kent T. Lucien  
Kent T. Lucien  
Chief Financial Officer

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**Exhibit Index**

**Exhibit Number**

|      |   |
|------|---|
| 12   | Computation of Ratio of Earnings to Fixed Charges (Unaudited)   |
| 31.1 | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) Under the Securities Exchange Act of 1934   |
| 31.2 | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) Under the Securities Exchange Act of 1934   |
| 32   | Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

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