FIRST COMMONWEALTH FINANCIAL CORP /PA/
Form 10-K
February 26, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 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 001-11138

FIRST COMMONWEALTH FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

PENNSYLVANIA	25-1428528
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
22 NORTH SIXTH STREET INDIANA, PA	15701
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: (724) 349-7220

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
COMMON STOCK, $1 PAR VALUE	NEW YORK STOCK EXCHANGE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes ¨ No x

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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

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

Indicate by check mark whether the registrant is 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 x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

The aggregate market value of the voting and non-voting common stock, par value $1 per share, held by non-affiliates of the registrant (based upon the closing sale price on June 30, 2008) was approximately $646,516,649.

The number of shares outstanding of the registrant s common stock, $1.00 Par Value as of February 23, 2009, was 85,055,220.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement to be filed with the Securities and Exchange Commission in connection with the annual meeting of shareholders to be held April 20, 2009 are incorporated by reference into Part III.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

FORWARD-LOOKING STATEMENTS

Certain statements contained in this report that are not historical facts may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include, among others, statements regarding our strategy, evaluations of our asset quality, future interest rate trends and liquidity, prospects for growth in assets and prospects for future operating results. Forward-looking statements can generally be identified by the use of words such as believe, expect, anticipate, intend, plan, estimate or words of similar meaning, or future or conditional verbs such as will, would, should, could or Forward-looking statements are based on assumptions of management and are only expectations of future results. You should not place undue reliance on our forward-looking statements. Our actual results could differ materially from those projected in the forward-looking statements as a result of, among others, the risk factors described in Item 1A of this report. Forward-looking statements speak only as of the date on which they are made. We do not undertake any obligation to update any forward-looking statement to reflect circumstances or events that occur after the date the forward-looking statements are made.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

PART I

ITEM 1. Business

Overview

First Commonwealth Financial Corporation (First Commonwealth or we) is a registered bank holding company that is headquartered in Indiana, Pennsylvania. We provide a diversified array of consumer and commercial banking services through our bank subsidiary, First Commonwealth Bank. We also provide trust and wealth management services through First Commonwealth Financial Advisors, Inc. and insurance products through First Commonwealth Insurance Agency, Inc. At December 31, 2008, we had total assets of $6.4 billion, total loans of $4.4 billion, total deposits of $4.3 billion and shareholders equity of $652.8 million. Our principal executive office is located at 22 North Sixth Street, Indiana, Pennsylvania 15701, and our telephone number is (724) 349-7220.

First Commonwealth Bank (FCB or the Bank) is a Pennsylvania bank and trust company and is the seventh largest commercial bank headquartered in Pennsylvania. At December 31, 2008, the Bank operated 114 community banking offices throughout western Pennsylvania and three loan production offices in downtown Pittsburgh, State College and Canonsburg, Pennsylvania. The largest concentration of our branch offices are located within the greater Pittsburgh metropolitan area in Allegheny, Butler and Washington counties, while our remaining offices are located in smaller cities, such as Altoona, Greensburg, Johnstown, and Washington, Pennsylvania, and in towns and villages throughout predominantly rural counties. The Bank also operates a network of 124 automated teller machines, or ATMs, at various branch offices and offsite locations. All of our ATMs are part of the STAR and MasterCard/Cirrus networks, both of which operate nationwide. The Bank is also a member of the 29-bank Freedom ATM Alliance, which affords cardholders surcharge-free access to a network of over 600 ATMs in over 50 counties in Pennsylvania, Maryland, New York and Ohio.

Historical and Recent Developments

First Commonwealth Bank began in 1934 as First National Bank of Indiana with initial capitalization of $255 thousand. First National Bank of Indiana changed its name to National Bank of the Commonwealth in 1971 and became a subsidiary of First Commonwealth Financial Corporation in 1983.

Since the formation of the holding company in 1983, we have grown steadily through the acquisition of smaller banks and thrifts in our market area, including Deposit Bank in 1984, Dale National Bank and First National Bank of Leechburg in 1985, Citizens National Bank of Windber in 1986, Peoples Bank and Trust Company in 1990, Central Bank in 1992, Peoples Bank of Western Pennsylvania in 1993, Unitas National Bank and Reliable Savings Bank in 1994. In 1995, we merged all of our banking subsidiaries (other than Reliable Savings Bank) into Deposit Bank and renamed the resulting institution First Commonwealth Bank. We then merged Reliable Savings Bank into First Commonwealth Bank in 1997. We acquired Southwest Bank in 1998 and merged it into First Commonwealth Bank in 2002.

Our most recent acquisitions have expanded our presence in the Pittsburgh metropolitan area. In the fourth quarter of 2003, we acquired Pittsburgh Financial Corp., the holding company for Pittsburgh Savings Bank (dba BankPittsburgh), for a total cost of approximately $28.6 million. Pittsburgh Financial had total assets of approximately $376 million, with 7 branch offices and one loan production office in Allegheny and Butler Counties of Pennsylvania. In the second quarter of 2004, we acquired GA Financial, Inc., the holding company for Great American Federal, for a total cost of approximately $176.7 million. GA Financial had total assets of approximately $892 million, with 12 branch offices located in Allegheny County. In the third quarter of 2006, we acquired Laurel Capital Group, Inc., the holding company for Laurel Savings Bank, for a total cost of approximately $56.1 million. Laurel Capital Group had total assets of approximately $314 million, with 8 branch offices located in Allegheny and Butler Counties.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Historical and Recent Developments (Continued)

In recent years, we have primarily focused on organic growth, improving the reach of our franchise and the breadth of our product offering. As part of this strategy, we have opened twelve *de novo* branches since 2005, all of which are in the greater Pittsburgh area, and we are evaluating other sites for possible future branch locations. This emphasis on organic growth has been underscored by our most recent efforts to capitalize on the weakened state of our largest competitors, and it has provided us with new opportunities to expand our customer base and strategically augment our employee base.

The following are highlights of recent actions that we have taken to enhance our strategic position:

Management Restructuring. In March 2007, we promoted John J. Dolan to serve as the President and Chief Executive Officer of First Commonwealth Financial Corporation and Chief Executive Officer of First Commonwealth Bank. Prior to his promotion, Mr. Dolan served as our Chief Financial Officer since 1987 and previously served in various capacities since he joined First Commonwealth in 1980. In November 2007, we hired T. Michael Price to serve as President of First Commonwealth Bank. Prior to joining our organization, Mr. Price served as Chief Executive Officer for National City Bank in the Cincinnati and northern Kentucky market. In March 2007, we promoted Edward J. Lipkus, III to serve as the Chief Financial Officer of First Commonwealth Financial Corporation and of First Commonwealth Bank. Initially hired into our organization in August 2006, Mr. Lipkus previously served as the First Vice President, Controller and Principal Accounting Officer for Valley National Bancorp. In addition, we have filled numerous other management positions with new hires since the beginning of 2007. In doing so, we have added leadership and experience to our commercial lending, retail banking, small business and wealth management operations, and to certain critical support functions.

Implementing Best Practices. We have focused on improving accountability across our lines of business by establishing clear goals for our sales force and managing those goals with weekly sales calls and incentive programs that are closely aligned with our strategic and operating objectives. We have also introduced coordinated marketing blitzes in order to improve our market awareness and management branch visits in order to reinforce our community banking culture. We continue to build brand awareness in our markets through targeted advertising, sponsorships and a focus on community involvement. We have also strengthened our commercial lending group with the hiring of several new commercial lenders, the development of a corporate finance lending unit and a greater emphasis on relationship lending, all of which have contributed to improved loan production volume.

Leveraging Opportunities for Organic Growth. We believe that our size enables us to offer products and services that are competitive with those offered by large regional banks, while our community banking heritage allows us to deliver personalized service that appeals to consumers and small-and medium-sized businesses throughout our market areas. We believe that this advantage has become more pronounced due to the ongoing disruptions in the credit and capital markets and recent industry consolidation within our market area. As large competitors have focused on capital preservation and the resolution of problem credits in the wake of a deepening national economic and credit crisis, we have been able to grow our market share among both businesses and consumers.

Competition

The banking and financial services industry is extremely competitive in our market area. We face vigorous competition for customers, loans and deposits from many companies, including:

- commercial banks;
- savings and loan associations;

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Competition (Continued)

- finance companies;
- credit unions;
- trust companies;
- mortgage companies;
- money market mutual funds;
- insurance companies; and
- brokerage and investment firms.

Many of these competitors are significantly larger than us, have greater resources, lending limits and larger branch systems and offer a wider array of financial services than us. In addition, some of these competitors, such as credit unions, are subject to a lesser degree of regulation than that imposed on us.

Employees

At December 31, 2008, First Commonwealth and its subsidiaries employed 1,473 full-time employees and 220 part-time employees.

Supervision and Regulation

The following discussion sets forth certain of the material elements of the regulatory framework applicable to bank holding companies and their subsidiaries and provides certain specific information relevant to First Commonwealth and its subsidiaries. The regulatory framework is intended primarily for the protection of depositors, other customers and the federal deposit insurance fund and not for the protection of security holders. The rules governing the regulation of financial institutions and their holding companies are very detailed and technical. Accordingly, the following discussion is general in nature and is not intended to be complete or to describe all the laws and regulations that apply to First Commonwealth and its subsidiaries. A change in applicable statutes, regulations or regulatory policy may have a material adverse effect on our business, financial condition or results of operations.

Bank Holding Company Regulation

First Commonwealth Financial Corporation is registered as a bank holding company under the Bank Holding Company Act of 1956, as amended, which we refer to as the BHC Act, and is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (FRB).

Acquisitions. Under the BHC Act, First Commonwealth is required to secure the prior approval of the FRB before it can merge or consolidate with any other bank holding company or acquire all or substantially all of the assets of any bank that is not already majority owned by it or acquire direct or indirect ownership, or control of, any voting shares of any bank that is not already majority owned by it, if after such acquisition it would directly or indirectly own or control more than 5% of the voting shares of such bank. Satisfactory financial condition, particularly with regard to capital adequacy, and satisfactory Community Reinvestment Act (CRA) ratings are generally prerequisites to obtaining federal regulatory approval to make acquisitions and open branch offices.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Supervision and Regulation (Continued)

Bank Holding Company Regulation (Continued)

Non-Banking Activities. First Commonwealth is generally prohibited under the BHC Act from engaging in, or acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company engaged in non-banking activities unless the FRB, by order or regulation, has found such activities to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. In making this determination, the FRB considers whether the performance of these activities by a bank holding company can reasonably be expected to produce benefits to the public that outweigh the possible adverse effects.

Reporting. Under the BHC Act, First Commonwealth is required to file periodic reports and other information of its operations with, and is subject to examination by the FRB. In addition, under the Pennsylvania Banking Code of 1965, the Pennsylvania Department of Banking has the authority to examine the books, records and affairs of any Pennsylvania bank holding company or to require any documentation deemed necessary to ensure compliance with the Pennsylvania Banking Code.

Affiliate Transactions. There are various legal restrictions on the extent to which First Commonwealth and its non-bank subsidiaries can borrow or otherwise obtain credit from its banking subsidiaries. In general, these restrictions require that any such extensions of credit must be secured by designated amounts of specified collateral and are limited, as to any one of First Commonwealth or its non-bank subsidiaries, to ten percent of the lending bank s capital stock and surplus, and as to First Commonwealth and all such non-bank subsidiaries in the aggregate, to 20 percent of such lending bank s capital stock and surplus. Further, a bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property or furnishing of services.

SEC Regulations. First Commonwealth is also under the jurisdiction of the Securities and Exchange Commission and various state securities commissions for matters relating to the offer and sale of its securities and is subject to the Securities and Exchange Commission s rules and regulations relating to periodic reporting, proxy solicitation and insider trading.

Bank Regulations

FCB is a state bank chartered under the Pennsylvania Banking Code and is not a member of the Federal Reserve System. As such, FCB is subject to the supervision of, and is regularly examined by, both the Federal Deposit Insurance Corporation (FDIC) and the Pennsylvania Department of Banking and is required to furnish quarterly reports to both agencies. The approval of the Pennsylvania Department of Banking and FDIC is also required for FCB to establish additional branch offices or merge with or acquire another banking institution. Under current Pennsylvania law, banking institutions, such as FCB, may establish branches within any county in Pennsylvania, subject to prior regulatory approval.

Restrictions on Dividends. The Pennsylvania Banking Code states, in part, that dividends may be declared and paid only out of accumulated net earnings and may not be declared or paid unless surplus is at least equal to capital. Dividends may not reduce surplus without the prior consent of the Pennsylvania Department of Banking. FCB has not reduced its surplus through the payment of dividends. The FDIC also prohibits the declaration or payout of dividends at a time when FCB is in default in payment of any assessment due the FDIC. In addition, the FRB recently issued supervisory guidance regarding the payment of dividends by bank holding companies which states, among other things, that a company must consult with the FRB in advance of paying a dividend that exceeds earnings for the quarter for which the dividend is paid or that could result in a material adverse change to

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Supervision and Regulation (Continued)

Bank Regulations (Continued)

the company s capital structure. The guidance also states that a company should, as a general matter, eliminate, defer or severely limit its dividend if (1) the company s net income for the past four quarters, net of dividends paid during that period, is not sufficient to fully fund the dividend; (2) the company s prospective rate of earnings retention is not consistent with the company s capital needs and current and prospective financial condition; or (3) the company will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios.

Community Reinvestment. Under the CRA, a bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution s discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires the applicable regulatory agency to assess an institution s record of meeting the credit needs of its community. The CRA requires public disclosure of an institution s CRA rating and requires that the applicable regulatory agency provide a written evaluation of an institution s CRA performance utilizing a four-tiered descriptive rating system. An institution s CRA rating is considered in determining whether to grant charters, branches and other deposit facilities, relocations, mergers, consolidations and acquisitions. Performance less than satisfactory may be the basis for denying an application. For its most recent examination, the Bank received a satisfactory rating.

Consumer Laws. The operations of FCB are also subject to numerous Federal, state and local laws and regulations which set forth specific restrictions and procedural requirements with respect to interest rates on loans, the extension of credit, credit practices, the disclosure of credit terms and discrimination in credit transactions.

Deposit Insurance. Deposits of FCB are insured up to applicable limits by the FDIC and are subject to deposit insurance assessments to maintain the Deposit Insurance Fund. The insurance assessments are based upon a matrix that takes into account a bank s capital level and supervisory rating. In 2008, the FDIC instituted the Temporary Liquidity Guarantee Program, which, among other things, provides unlimited deposit insurance for funds deposited into non interest-bearing transaction accounts through December 31, 2009.

Capital Regulations

First Commonwealth and FCB are subject to risk-based capital standards by which all bank holding companies and banks are evaluated in terms of capital adequacy. These standards relate a banking company s capital to the risk profile of its assets. The risk-based capital standards require that bank holding companies and banks must have Tier 1 capital of at least 4% and total capital, including Tier 1 capital, equal to at least 8% of its total risk-adjusted assets. Tier 1 capital includes common stockholders equity and qualifying perpetual preferred stock together with related surpluses and retained earnings. The remaining portion of this capital standard, known as Tier 2 capital, may be comprised of limited life preferred stock, qualifying subordinated debt instruments, and the allowance for credit losses.

Additionally, banking organizations must maintain a minimum leverage ratio of 3% measured as the ratio of Tier 1 capital to adjusted average assets. This 3% leverage ratio is a minimum for the top-rated banking organizations without any supervisory, financial or operational weaknesses or deficiencies and other banking organizations are expected to maintain leverage capital ratios 100 to 200 basis points above the minimum depending on their financial condition.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Supervision and Regulation (Continued)

Capital Regulations (Continued)

Federal Banking Agencies have broad powers to take corrective action to resolve problems of insured depository institutions. The extent of these powers depends upon whether the institutions in question are well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, or critically undercapitalized. As of December 31, 2008, FCB was a well-capitalized bank as defined by the FDIC. See Note 29 of Notes to Consolidated Financial Statements, contained in Item 8, for a table that provides a comparison of First Commonwealth s and FCB s risk-based capital ratios and the leverage ratio to minimum regulatory requirements.

Gramm-Leach-Bliley Act

Enacted in 1999, the Gramm-Leach-Bliley Act, or GLBA, repealed the 1933 Glass-Steagall Act s separation of the commercial and investment banking industries. GLBA created a new category of holding company called a financial holding company, which is authorized to engage in an expanded range of nonbanking activities, as described below, while preserving existing authority for bank holding companies to engage in activities that are closely related to banking. Generally, a bank holding company may become a financial holding company upon filing an election with the FRB if each of its depository institution subsidiaries is well-capitalized, well managed and received a CRA rating of satisfactory or better at its most recent examination. First Commonwealth is eligible to become a financial holding company but has not yet elected to do so.

Financial holding companies may engage in any activity that (i) is financial in nature or incidental to such financial activity or (ii) is complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. GLBA specifies certain activities that are financial in nature. These activities include: acting as principal, agent or broker for insurance; underwriting, dealing in or making a market in securities; and providing financial and investment advice. The FRB and the Secretary of the Treasury have authority to decide whether other activities are also financial in nature or incidental to financial activity, taking into account changes in technology, changes in the banking marketplace, competition for banking services and so on.

GLBA also established a system of functional regulation, under which the federal banking agencies regulate the banking activities of financial holding companies; the Securities and Exchange Commission regulates their securities activities; and state insurance regulators regulate their insurance activities. GLBA also provided new protections against the transfer and use by financial institutions of consumers nonpublic, personal information.

USA Patriot Act

Anti-terrorism legislation enacted under the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, commonly known as the Patriot Act, expanded the scope of anti-money laundering laws and regulations and imposed additional obligations on U.S. financial institutions, including banks. These regulations include obligations to maintain appropriate policies, procedures and controls, which are reasonably designed to detect and report instances of money laundering and terrorist financing.

Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002, or Sarbanes-Oxley, implemented a broad range of corporate governance, accounting and reporting measures for companies that have securities registered under the Securities Exchange

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Supervision and Regulation (Continued)

Sarbanes-Oxley Act (Continued)

Act of 1934, including publicly-held bank holding companies such as First Commonwealth. Sarbanes-Oxley created new requirements in the areas of financial disclosure and corporate governance, including:

- increased responsibility for the Chief Executive Officer and the Chief Financial Officer with respect to the content of financial statements;
- new requirements for audit committees, including independence, expertise, and responsibilities;
- new standards for auditors and regulation of audits, including independence and the type of non-audit services that auditors may provide;
- accelerated filing requirements for SEC reports;
- disclosures concerning internal controls and procedures;
- increased disclosure and reporting obligations for the reporting company and their directors and executive officers;
- disclosure of a code of ethics; and
- a range of new and increased civil and criminal penalties for fraud and other violations of the securities laws.

National Monetary Policy

In addition to being affected by general economic conditions, the earnings and growth of FCB and, therefore, the earnings and growth of First Commonwealth, are affected by the policies of regulatory authorities, including the FRB, the FDIC and the Commonwealth of Pennsylvania. An important function of the FRB is to regulate the money supply and credit conditions. Among the instruments used to implement these objectives are open market operations in U.S. government securities, setting the discount rate and changes in reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall growth and distribution of credit, bank loans, investments and deposits, and their use may also affect interest rates charged on loans or paid on deposits.

The federal government greatly expanded the resources available to influence monetary policy during 2008 in response to significant disruptions in credit and capital markets and the greatly weakened financial condition of many large companies in the financial services industry. The Federal Reserve Board implemented new lending programs to improve liquidity at financial institutions and other market participants, which include auctions of short-term secured borrowings, the expansion of eligible collateral for certain lending programs and the extension of

borrowings to investment banks and other non-bank financial services companies. The Federal Deposit Insurance Corporation instituted the Temporary Liquidity Guarantee Program to strengthen liquidity in the banking system by guaranteeing newly issued senior unsecured debt of banks, thrifts, and certain holding companies, and by providing full coverage of non-interest bearing deposit transaction accounts, regardless of dollar amount, through December 31, 2009. Finally, the United States Treasury implemented the Capital Purchase Program under the Troubled-Asset Relief Program, or TARP, in which the Treasury injected capital into participating banks and bank holding companies through the purchase of senior preferred stock to encourage lending. First Commonwealth participates in various lending programs by the Federal Reserve Board, and also participates in the Temporary Liquidity Guarantee Program. First Commonwealth declined to participate in the TARP Capital Purchase Program.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1. Business (Continued)
Supervision and Regulation (Continued)

National Monetary Policy (Continued)

The monetary policies and regulations of the FRB have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. The effects of such policies upon our future business, earnings and growth cannot be predicted.

Availability of Financial Information

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission. You may read and copy any document we file at the Securities and Exchange Commission s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Our Securities and Exchange Commission filings are also available to the public on the Securities and Exchange Commission s website at www.sec.gov and on our website at www.fcbanking.com.

We also make available on our website, and in print to any shareholder who requests them, our Corporate Governance Guidelines, the charters for our Audit, Executive Compensation and Governance Committees, and the Code of Conduct and Ethics that applies to all of our directors, officers and employees.

Our Chief Executive Officer has certified to the New York Stock Exchange (NYSE) that, as of the date of the certification, he was not aware of any violation by First Commonwealth of NYSE s corporate governance listing standards. In addition, our Chief Executive Officer and Chief Financial Officer have made certain certifications concerning the information contained in this report pursuant to Section 302 of the Sarbanes-Oxley Act. The Section 302 certifications appear as exhibits 31.1 and 31.2 to this annual report on Form 10-K.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1A. Risk Factors

As a financial services company, we are subject to a number of risks, many of which are outside of our control. These risks include, but are not limited to:

Increases to the allowance for credit losses may cause our earnings to decrease.

Our customers may not repay their loans according to the original terms, and the collateral securing the payment of those loans may be insufficient to pay any remaining loan balance. This may result in significant loan losses, which could have a material adverse effect on our operating results. We make various assumptions and judgments about the future performance of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the amount of the allowance for credit losses, we rely on loan quality reviews, past experience, and an evaluation of economic conditions, among other factors. If our assumptions prove to be incorrect, our allowance for credit losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in additions to the allowance. In addition, bank regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or charge off all or a portion of non-performing loans. Any increase in our allowance for credit losses or loan charge-offs as required by these regulatory authorities could have a material adverse effect on our results of operations and/or financial condition.

Declines in value may adversely impact the carrying amount of our investment portfolio and result in other-than-temporary impairment charges.

As of December 31, 2008, we had single issuer trust preferred securities and trust preferred collateralized debt obligations with an aggregate book value of $121.7 million and an unrealized loss of approximately $48.0 million and equity securities with an aggregate book value of $65.1 million and an unrealized loss of approximately $519 thousand. As a result of recent adverse economic banking conditions, we incurred other-than-temporary impairment charges in our securities portfolio of approximately $13.0 million during 2008. We may be required to record additional impairment charges on other investment securities if they suffer a decline in value that is considered other-than-temporary. If the credit quality of the securities in our investment portfolio deteriorates, we may also experience a loss in interest income from the suspension of either interest or dividend payments. Numerous factors, including lack of liquidity for resales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate or adverse actions by regulators could have a negative effect on our investment portfolio in future periods. If an impairment charge is significant enough it could affect the ability of First Commonwealth Bank to upstream dividends to us, which could have a material adverse effect on our liquidity and our ability to pay dividends to shareholders and could also negatively impact our regulatory capital ratios and result in us not being classified as well-capitalized for regulatory purposes.

Weakening economic conditions may have a negative impact on our results of operations and financial condition.

During 2008, the global financial markets were in turmoil, and the equity and credit markets experienced extreme volatility, which caused already weak economic conditions to worsen. Weak economic conditions, including high and increasing levels of unemployment, reduced consumer spending and declining equity and real estate values could limit the demand for loans by creditworthy consumers and businesses, reduce the supply of low-cost deposits, impair the ability of our borrowers to repay their loans and reduce the value of collateral supporting those loans. Declines in equity valuations also reduce fees generated by our trust and other wealth management operations, which will negatively impact our non-interest income. Our financial condition and results of operations could be materially impacted if these conditions were to persist.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1A. Risk Factors (Continued)

Legislative and regulatory actions in reaction to the ongoing downturn in the financial services industry and disruptions in U.S. and global credit markets may adversely impact our results of operations.

Negative developments in the credit and capital markets and a significant decline in real estate values since 2007 have created significant volatility in the financial markets and have greatly weakened the financial condition of companies in the financial services industry. As a result, there is a potential for new federal or state laws and regulations regarding lending and funding practices, liquidity standards and capital adequacy, and financial institution regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations, including the more frequent issuance of formal enforcement orders and the institution of capital restoration plans. Negative developments in the financial services industry and the impact of new legislation in response to those developments could negatively impact our operations by restricting our business operations, including our ability to originate or sell loans and the levels of capital that we are required to maintain, which could adversely impact our financial performance.

Our commercial loans are subject to various lending risks depending on the nature of the borrower s business, its cash flow and our collateral.

Our commercial loans involve higher principal amounts than other loans, and repayment of these loans may be dependent on factors outside our control or the control of our borrowers. Repayment of commercial real estate loans is generally dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service and the successful operation and management of the properties. As a result, repayment of such loans may be affected by factors outside the borrower s control, such as adverse conditions in the real estate market or the economy or changes in government regulation. If the cash flow from the property is reduced, the borrower s ability to repay the loan and the value of the security for the loan may be impaired.

Repayment of our commercial business loans is often dependent on the cash flow of the borrower, which may be unpredictable, and collateral securing these loans may fluctuate in value. Most often, this collateral is accounts receivable, inventory, equipment or real estate. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. Other collateral securing loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business.

Our ability to pay dividends depends primarily on our receipt of dividends from First Commonwealth Bank, which in turn is limited by regulatory restrictions and its operating cash flow needs.

We are a bank holding company and our business is conducted by our subsidiaries, each of which is a separate and distinct legal entity. As a result, our ability to pay dividends depends on our receipt of dividends from our direct and indirect subsidiaries. Our bank subsidiary, First Commonwealth Bank, is our primary source of dividends. Dividend payments from First Commonwealth Bank are subject to legal and regulatory limitations, generally based on accumulated net earnings and surplus, imposed by bank regulatory agencies. The ability of First Commonwealth Bank to pay dividends is also subject to its profitability, financial condition, capital expenditures and other cash flow requirements. There is no assurance that First Commonwealth Bank or our other subsidiaries will be able to pay dividends in the future or that we will generate adequate cash flow to pay dividends in the future. Our failure to pay dividends on our common stock could have a material adverse effect on the market price of our common stock.

Our dividend payout ratio, which is calculated by dividing our dividends paid per share by our earnings per share, was 117.2% based on our dividends and reported earnings for 2008. A dividend payout ratio over 100% reduces our capital and is not sustainable over the long term. In the event that our earnings decline or fail to

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1A. Risk Factors (Continued)

improve in accordance with our business plan, our board of directors may make a decision to cease paying a dividend or reduce the quarterly dividend paid to our shareholders. In addition, recent regulatory guidance by the Federal Reserve Board may prohibit the payment of dividends at our current rate unless our earnings exceed our dividend payment and our capital needs and risk exposures support the continued payment of the dividend. See Supervision and Regulation Bank Regulations Restrictions on Dividends on page 7 for a description of this guidance. The elimination or reduction of our dividend could have a material adverse effect on the market price of our common stock.

Changes in interest rates could negatively impact our financial condition and results of operations.

Our results of operations depend substantially on net interest income, which is the difference between interest earned on interest-earning assets (such as investments and loans) and interest paid on interest-bearing liabilities (such as deposits and borrowings). Interest rates are highly sensitive to many factors, including governmental monetary policies and domestic and international economic and political conditions. Conditions such as inflation, recession, unemployment, money supply, and other factors beyond our control may also affect interest rates. If our interest-earning assets mature or reprice more quickly than interest-bearing liabilities in a declining interest rate environment, net interest income could be adversely impacted. Likewise, if interest-bearing liabilities mature or reprice more quickly than interest-earnings assets in a rising interest rate environment, net interest income could be adversely impacted.

Changes in interest rates also can affect the value of loans and other assets. An increase in interest rates that adversely affects the ability of borrowers to pay the principal or interest on loans may lead to an increase in non-performing assets and a reduction of income recognized, which could have a material adverse effect on our results of operations and cash flows.

Our expanding branch network may negatively affect our financial performance.

We continue to expand our branch network by both acquiring financial institutions and establishing de novo branches. At December 31, 2008, we operated 114 branches, including two new locations that were opened in 2007 and three new locations that were opened in 2008 as part of our de novo expansion. The profitability of our expansion strategy will depend on whether the income we generate in the new markets will offset the increased expenses of operating a larger entity with increased personnel, more branch locations and additional product offerings. We expect that it may take a period of time before certain of our new branches can become profitable, especially in areas in which we do not have an established physical presence. During this period, operating these new branches may negatively impact net income. Additionally, in connection with our expansion, we will need to increase our operational and financial procedures, systems and controls. If we have difficulty in doing so, it could harm our business, results of operations and financial condition.

Our wholesale funding sources may prove insufficient to replace deposits at maturity and support our future growth.

We must maintain sufficient funds to respond to the needs of depositors and borrowers. As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments. As we continue to grow, we are likely to become more dependent on these sources, which include Federal Home Loan Bank advances, proceeds from the sale of loans and liquidity resources at the holding company. At December 31, 2008, we had approximately $975.9 million of Federal Home Loan Bank advances outstanding. Our financial flexibility will be severely constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. Furthermore, if we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our operating margins and profitability would be adversely affected.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 1A. Risk Factors (Continued)

Competition from other financial institutions in originating loans, attracting deposits and providing various financial services may adversely affect our profitability.

We face substantial competition in originating loans and attracting deposits. This competition comes principally from other banks, savings institutions, mortgage banking companies, and credit unions, as well as institutions offering uninsured investment alternatives, including money market funds. Many of our competitors enjoy advantages, including greater financial resources and higher lending limits, better brand recognition, a wider geographic presence, more accessible branch office locations, the ability to offer a wider array of services or more favorable pricing alternatives, as well as lower origination and operating costs. These competitors may offer more favorable pricing through lower interest rates on loans or higher interest rates on deposits, which could force us to match competitive rates and thereby reduce our net interest income.

An interruption to our information systems could adversely impact our operations.

We rely upon our information systems for operating and monitoring all major aspects of our business, including deposit and loan operations, as well as internal management functions. These systems and our operations could be damaged or interrupted by natural disasters, power loss, network failure, improper operation by our employees, security breaches, computer viruses, intentional attacks by third parties or other unexpected events. Any disruption in the operation of our information systems could adversely impact our operations, which may affect our financial condition, results of operations and cash flows.

We may undertake acquisitions in the future which could place heavy demands on our employees, disrupt our business and cause us to not realize expected earnings.

Our growth has come primarily though the acquisition of other financial institutions, and we expect to continue to make acquisitions as opportunities arise, both within and outside our current market area. We cannot predict the number, size or timing of acquisitions that we will undertake in future periods. We may face difficulty in integrating an acquired company which could prevent us from realizing expected revenue growth or cost savings or other projected benefits from the acquisition. The integration could result in higher than expected deposit attrition, loss of key employees, disruption of our business or the business of the acquired company, or otherwise adversely affect our ability to maintain relationships with customers and employees or achieve the anticipated benefits of the acquisition.

Provisions of our articles of incorporation, bylaws and Pennsylvania law, as well as state and federal banking regulations, could delay or prevent a takeover of us by a third party.

Provisions in our articles of incorporation and bylaws, the corporate law of the Commonwealth of Pennsylvania, and state and federal regulations could delay, defer or prevent a third party from acquiring us, despite the possible benefit to our shareholders, or otherwise adversely affect the price of our common stock. These provisions include, among other things, advance notice requirements for proposing matters that shareholders may act on at shareholder meetings. In addition, under Pennsylvania law, we are prohibited from engaging in a business combination with any interested shareholder for a period of five years from the date the person became an interested shareholder unless certain conditions are met. These provisions may discourage potential takeover attempts, discourage bids for our common stock at a premium over market price or adversely affect the market price of, and the voting and other rights of the holders of, our common stock.

ITEM 1B. Unresolved Staff Comments

None.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 2. Properties

Our principal office is located in the old Indiana County courthouse complex, consisting of the former courthouse building and the former sheriff s residence and jail building for Indiana County. This certified Pennsylvania and national historic landmark was built in 1870 and restored by us in the early 1970s. We lease the complex from Indiana County pursuant to a lease agreement that was originally signed in 1973 and has a current term that expires in 2048.

The majority of our administrative personnel are also located in two owned buildings and one leased premise in Indiana, Pennsylvania, each of which is in close proximity to our principal office.

First Commonwealth Bank has 114 banking offices of which 26 are leased and 88 are owned. We also lease three loan production offices.

While these facilities are adequate to meet our current needs, available space is limited and additional facilities may be required to support future expansion. However, we have no current plans to lease, purchase or construct additional administrative facilities.

ITEM 3. Legal Proceedings

There are no material legal proceedings to which First Commonwealth or its subsidiaries are a party, or of which any of their property is the subject. All legal proceedings presently pending or threatened against First Commonwealth or its subsidiaries arose in the normal course of business and, in the opinion of management, will not have a material adverse effect on the consolidated operations or financial position of First Commonwealth and its subsidiaries.

ITEM 4. Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of our security holders in the fourth quarter of 2008.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

PART II

ITEM 5. Market for Registrant s Common Stock, Related Stockholder Matters and Issuer Purchase of Equity Securities

First Commonwealth is listed on the NYSE under the symbol FCF. As of February 11, 2009, there were approximately 9,038 holders of record of First Commonwealth s common stock. The table below sets forth the high and low sales prices per share and cash dividends declared per share for common stock of First Commonwealth for each quarter during the last two fiscal years.

Period	High Sale	Low Sale	Cash Dividends Per Share
2008			
First Quarter	$ 12.65	$ 9.00	$ 0.17
Second Quarter	$ 12.90	$ 9.12	$ 0.17
Third Quarter	$ 16.18	$ 8.00	$ 0.17
Fourth Quarter	$ 15.00	$ 8.70	$ 0.17

Period	High Sale	Low Sale	Cash Dividends Per Share
2007			
First Quarter	$ 13.66	$ 11.45	$ 0.17
Second Quarter	$ 12.57	$ 10.76	$ 0.17
Third Quarter	$ 12.39	$ 8.90	$ 0.17
Fourth Quarter	$ 12.18	$ 9.78	$ 0.17

Federal and State Regulations contain restrictions on the ability of First Commonwealth to pay dividends. For information regarding restrictions on dividends, see Part I, Item 1 Business Supervision and Regulation Restrictions on Dividends and Part II, Item 8, Financial Statements and Supplementary Data Note 29 (Regulatory Restrictions and Capital Adequacy). In addition, under the terms of the capital securities issued by First Commonwealth Capital Trust I, II, and III, First Commonwealth could not pay dividends on its common stock if First Commonwealth deferred payments on the junior subordinated debt securities which provide the cash flow for the payments on the capital securities.

First Commonwealth did not repurchase shares during the fourth quarter of 2008.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 5. Market for Registrant s Common Stock, Related Stockholder Matters and Issuer Purchase of Equity Securities (Continued)

The following five-year performance graph compares the cumulative total shareholder return (assuming reinvestment of dividends) on First Commonwealth s common stock to the KBW Regional Banking Index and the Russell 2000 Index. The stock performance graph assumes $100 was invested on December 31, 2003, and the cumulative return is measured as of each subsequent fiscal year end.

	Period Ending					
Index	**12/31/03**	**12/31/04**	**12/31/05**	**12/31/06**	**12/31/07**	**12/31/08**
First Commonwealth Financial Corporation	100.00	112.96	99.70	108.94	91.71	113.08
Russell 2000	100.00	118.33	123.72	146.44	144.15	95.44
KBW Regional Banking Index*	100.00	119.88	121.99	132.44	103.34	84.16

* The KBW Regional Banking Index is the property of Keefe, Bruyette & Woods, Inc. (KBW). KBW does not guarantee the accuracy or completeness of the Index, makes no express or implied warranties with respect to the Index and shall have no liability for any damages, claims, losses or expenses caused by errors in the Index calculation.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 6. Selected Financial Data

The following selected financial data is not covered by the auditor s report and should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, which follows, and with the Consolidated Financial Statements and related notes.

	Years Ended December 31,				
	2008	2007	2006	2005	2004
	(dollars in thousands, except share data)				
Interest income	$ 327,596	$ 331,095	$ 333,070	$ 312,068	$ 278,025
Interest expense	138,998	169,713	166,107	138,618	110,690
Net interest income	188,598	161,382	166,963	173,450	167,335
Provision for credit losses	23,095	10,042	11,544	8,628	8,070
Net interest income after provision for credit losses	165,503	151,340	155,419	164,822	159,265
Net securities (losses) gains	(11,494)	1,174	697	(7,673)	4,077
Gain on sale of branches	-0-	-0-	-0-	11,832	-0-
Gain on sale of merchant services business	-0-	-0-	-0-	1,991	-0-
Other income	54,325	47,696	43,550	44,075	43,572
Restructuring charges	-0-	-0-	-0-	5,437	-0-
Merger and related charges	-0-	-0-	-0-	-0-	2,125
(Gain) loss on extinguishment of debt	-0-	-0-	(410)	-0-	29,495
Other expenses	158,615	148,007	138,093	138,517	132,935
Income before taxes	49,719	52,203	61,983	71,093	42,359
Applicable income taxes	6,632	5,953	9,029	13,257	3,707
Net income	$ 43,087	$ 46,250	$ 52,954	$ 57,836	$ 38,652
Per Share Data					
Net income	$ 0.580	$ 0.640	$ 0.750	$ 0.830	$ 0.590
Dividends declared	$ 0.680	$ 0.680	$ 0.680	$ 0.665	$ 0.645
Average shares outstanding	74,477,795	72,816,208	70,766,348	69,276,141	65,887,611
Per Share Data Assuming Dilution					
Net income	$ 0.580	$ 0.630	$ 0.740	$ 0.830	$ 0.580
Dividends declared	$ 0.680	$ 0.680	$ 0.680	$ 0.665	$ 0.645
Average shares outstanding	74,583,236	72,973,259	71,133,562	69,835,285	66,487,516
At End of Period					
Total assets	$ 6,425,880	$ 5,883,618	$ 6,043,916	$ 6,026,320	$ 6,198,478
Investment securities	1,452,191	1,645,714	1,723,191	1,939,743	2,240,477
Loans and leases, net of unearned income	4,418,377	3,697,819	3,783,817	3,624,259	3,514,833
Allowance for credit losses	52,759	42,396	42,648	39,492	41,063
Deposits	4,280,343	4,347,219	4,326,440	3,996,552	3,844,475
Short-term borrowings	1,152,700	354,201	500,014	665,665	946,474
Subordinated debentures	105,750	105,750	108,250	108,250	108,250
Other long-term debt	170,530	442,196	485,170	691,494	731,324
Shareholders equity	652,779	568,788	571,361	521,045	531,978
Key Ratios					
Return on average assets	0.70%	0.80%	0.89%	0.94%	0.66%

Return on average equity	7.45%	8.08%	9.76%	10.89%	7.82%
Net loans to deposits ratio	101.99%	84.09%	86.47%	89.70%	90.36%
Dividend payout ratio	117.24%	106.25%	90.67%	80.12%	109.32%
Average equity to average assets ratio	9.35%	9.87%	9.08%	8.60%	8.47%

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis concerns the financial condition and the results of operations of First Commonwealth Financial Corporation (First Commonwealth or we) and its subsidiaries, First Commonwealth Bank (FCB), First Commonwealth Insurance Agency, Inc. (FCIA) and First Commonwealth Financial Advisors, Inc. (FCFA), as of and for the years ended December 31, 2008, 2007 and 2006. The purpose of this discussion is to focus on information concerning our financial condition and results of operations that is not readily apparent from the Consolidated Financial Statements. In order to obtain a clear understanding of this discussion, you should refer to the Consolidated Financial Statements, the notes thereto and other financial information presented in this Annual Report.

Company Overview

First Commonwealth provides a diversified array of consumer and commercial banking services through our bank subsidiary, FCB. We also provide trust and wealth management services through FCFA and insurance products through FCIA. At December 31, 2008, the Bank operated 114 community banking offices throughout western Pennsylvania and three loan production offices in downtown Pittsburgh, State College and Canonsburg, Pennsylvania.

Our consumer services include Internet and telephone banking, an automated teller machine network, personal checking accounts, interest-earning checking accounts, savings accounts, health savings accounts, insured money market accounts, debit cards, investment certificates, fixed and variable rate certificates of deposit, club accounts, secured and unsecured installment loans, construction and mortgage loans, safe deposit facilities, credit lines with overdraft checking protection, IRA accounts and student loans. Commercial banking services include commercial lending, small and high-volume business checking accounts, on-line account management services, ACH origination, payroll direct deposit, commercial cash management services and repurchase agreements. We also provide a variety of trust and asset management services and a full complement of auto, home and business insurance as well as term life insurance. We offer annuities, mutual funds, stock and bond brokerage services through an arrangement with a broker-dealer and insurance brokers. Most of our commercial customers are small and mid-sized businesses in central and western Pennsylvania.

As a financial institution with a focus on traditional banking activities, we earn the majority of our revenue through net interest income, which is the difference between interest earned on loans and investments and interest paid on deposits and borrowings. Growth in net interest income is dependent upon balance sheet growth and maintaining or increasing our net interest margin, which is net interest income (on a fully taxable-equivalent basis) as a percentage of our average interest-earning assets. We also generate revenue through fees earned on various services and products that we offer to our customers and through sales of assets, such as loans, investments, or properties. These revenue sources are offset by provisions for credit losses on loans, operating expenses and income taxes.

General economic conditions also affect our business by impacting our customers need for financing, thus affecting loan growth, and impacting the credit strength of existing and potential borrowers.

Critical Accounting Policies and Significant Estimates

First Commonwealth s accounting and reporting policies conform to accounting principles generally accepted in the United States of America (GAAP) and predominant practice in the banking industry. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Over time, these estimates and assumptions may prove to be inaccurate or vary from actual results and may significantly affect our reported

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Critical Accounting Policies and Significant Estimates (Continued)

results and financial position for the period presented or in future periods. We consider our accounting policies concerning the fair value of financial instruments, allowance for credit losses and goodwill and other intangible assets to be critical because they are highly dependent on subjective or complex judgments, assumptions and estimates made by management.

Fair Values of Financial Instruments

Statement of Financial Accounting Standards No. 157 (SFAS 157) Fair Value Measurements, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value.

In accordance with SFAS 157, First Commonwealth groups financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities. Level 1 securities include equity holdings comprised of bank stocks.

Level 2 Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained for identical or comparable assets or liabilities from alternative pricing sources with reasonable levels of price transparency. Level 2 securities include U.S. Government securities, municipals, Federal Home Loan Bank (FHLB) stock, interest rate derivatives that include interest rate swaps and risk participation agreements, and impaired loans.

Level 3 Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. If the inputs used to provide the evaluation are unobservable and/or there is very little, if any, market activity for the security or similar securities, the securities would be considered Level 3 securities. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities. The assets included in Level 3 are primarily trust preferred collateralized debt obligations. The trust preferred market has been severely impacted by the lack of liquidity in the credit markets and concern over the banking industry.

The fair value for pooled trust preferred collateralized debt obligations is measured by evaluating all relevant credit and structural aspects, determining appropriate performance assumptions and performing a discounted cash flow analysis. This evaluation includes detailed credit, performance and structural evaluations for each piece of collateral. Other factors in the valuation include consideration of the terms of the structure, the cash flow waterfall (for both interest and principal), the over collateralization and interest coverage provided by the structure and the probability of events of default and liquidation.

The discount rate used in the analysis combines an evaluation of current and observable market yields for comparable structured credit products with an evaluation of the risks associated with the underlying cash flows. The specific risks identified in a given collateralized debt obligation s cash flows are then evaluated and an adjustment is made to the credit spreads derived from market sources on the basis of this evaluation.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Critical Accounting Policies and Significant Estimates (Continued)

Fair Values of Financial Instruments (Continued)

Fair values for single issue trust preferred securities were obtained from pricing sources with reasonable pricing transparency, taking into account other unobservable inputs related to the risks for each issuer. These valuations are classified as Level 3 due to the inactivity in the markets.

Our valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes our valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. Furthermore, the reported fair value amounts have not been comprehensively revalued since the presentation dates, and therefore, estimates of fair value after the balance sheet date may differ significantly from the amounts presented herein.

In addition to valuation, on a quarterly basis we assess whether there are any declines in value below the carrying value of our assets that should be considered other than temporary. Methodologies and estimates used by management are discussed in detail in management s discussion and analysis of financial condition and results of operations and in Note 10 Impairment of Investment Securities and Note 21 Fair Values of Financial Instruments of Notes to Financial Statements.

Allowance for Credit Losses

We account for the credit risk associated with our lending activities through the allowance and provision for credit losses. The allowance represents management s best estimate of probable losses that are inherent in our existing loan portfolio as of the balance sheet date. The provision is a periodic charge to earnings in an amount necessary to maintain the allowance at a level that is appropriate based on management s assessment of probable estimated losses. Management determines and reviews with the Board of Directors the adequacy of the allowance on a quarterly basis in accordance with the methodology described below.

Individual loans are selected for review in accordance with FASB Statement No. 114, Accounting by Creditors for Impairment of a Loan, as amended by FASB Statement No. 118 (which we refer to as Statement 114). These are generally large balance commercial loans and commercial mortgages that are rated less than satisfactory based on our internal credit-rating process.

We assess whether the loans identified for review are impaired, which means that it is probable that all amounts will not be collected according to the contractual terms of the loan agreement, which generally represents loans that management has placed on nonaccrual status.

We calculate the estimated fair value of the loans that are selected for review based on observable market prices, discounted cash flows and the value of the underlying collateral.

We then select pools of homogenous smaller balance loans having similar risk characteristics for evaluation collectively under the provisions of FASB Statement No. 5, Accounting for Contingencies (which we refer to as Statement 5). These loans generally include residential mortgages, consumer loans, installment loans and smaller balance commercial loans.

Statement 5 loans are segmented into groups with similar characteristics and an allowance for credit losses is allocated to each segment based on recent loss history and other relevant information.

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Critical Accounting Policies and Significant Estimates (Continued)

Allowance for Credit Losses (Continued)

We then review the results to determine the appropriate balance of the allowance for credit losses. This review includes consideration of additional factors, such as the mix of loans in the portfolio, the balance of the allowance relative to total loans and non-performing assets, trends in the overall risk profile in the portfolio, trends in delinquencies and nonaccrual loans, local and national economic information and industry data, including trends in the industries we believe are higher risk.

There are many factors affecting the allowance for credit losses; some are quantitative while others require qualitative judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses based on historical loss experience and consideration of current economic trends and conditions, all of which may be susceptible to significant change. To the extent that actual outcomes differ from estimates, additional provisions for credit losses could be required that could adversely affect our earnings or financial position in future periods. The loan portfolio represents the largest asset category on our Consolidated Statements of Financial Condition.

Goodwill and Other Intangible Assets

We consider our accounting policies related to goodwill and other intangible assets to be critical because the assumptions or judgment used in determining the fair value of assets and liabilities acquired in past acquisitions are subjective and complex. As a result, changes in these assumptions or judgment could have a significant impact on our financial condition or results of operations.

The fair value of acquired assets and liabilities, including the resulting goodwill, was based either on quoted market prices or provided by other third-party sources, when available. When third-party information was not available, estimates were made in good faith by management primarily through the use of internal cash flow modeling techniques. The assumptions that were used in the cash flow modeling were subjective and are susceptible to significant changes.

Goodwill and other intangible assets with indefinite useful lives are tested for impairment at least annually and written down and charged to results of operations only in periods in which the recorded value is more than the estimated fair value. Intangible assets that have finite useful lives will continue to be amortized over their useful lives and are periodically evaluated for impairment.

As of December 31, 2008, goodwill and other intangible assets were not considered impaired; however, changing economic conditions could result in impairment, which could adversely affect earnings in future periods.

Recent Accounting Pronouncements

For a discussion of new accounting pronouncements adopted by First Commonwealth in 2008 and the expected impact of accounting pronouncements recently issued or proposed but not yet required to be adopted, refer to Note 2 of the accompanying Consolidated Financial Statements.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Results of Operations 2008 Compared to 2007

Summary of 2008 Results

The year 2008 was extremely challenging for the banking industry and First Commonwealth. However our operating results were solid despite the challenging conditions in the credit and capital markets. We experienced loan growth and we remain a well-capitalized institution with significant liquidity.

First Commonwealth experienced the following developments during 2008:

- We raised $115 million of common equity through a public stock offering.
- We elected not to participate in the Capital Purchase Program which is part of the federal government s Troubled Asset Relief Program.
- Total loans increased $720.6 million, or 19.5%.
- Net interest income increased $27.2 million, or 16.9%, and net interest margin increased 23 basis points.
- Impairment charges of $9.2 million, after tax, were recorded relating to bank equity securities, trust preferred collateralized debt obligations, and low income housing partnerships.
- We opened three new community banking offices.

The banking industry continued to see losses related to the sub-prime loans and investment write-downs. First Commonwealth is not a participant or underwriter in the sub-prime mortgage loan or collateralized debt marketplace and therefore does not have any direct exposure to risks associated with these activities. All mortgage backed securities in First Commonwealth s investment portfolio are AAA rated and backed by U.S. Government agencies and U.S. Government sponsored-enterprises.

Net income was $43.1 million or $0.58 per diluted share compared to $46.3 million or $0.63 per diluted share in 2007. The return on average equity and average assets was 7.45% and 0.70%, respectively, compared to 8.08% and 0.80% for the prior year period.

Earnings for 2008 were favorably impacted by a $27.2 million increase in net interest income; a $577 thousand increase in service charges on deposit accounts; a $1.0 million increase in card related interchange income; a $1.7 million increase in letter of credit fees; a $2.2 million increase in fees from interest rate derivatives; and a $564 thousand decrease in advertising. Earnings for 2008 were negatively impacted by a $13.1 million increase in the provision for credit losses; net securities losses of $11.5 million; a $7.4 million increase in salaries and employee benefits; a $1.3 million increase in net occupancy expense; and a $2.5 million increase in other expenses. The provision for income taxes increased $679 thousand due to decreases in tax free income and tax credits.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Results of Operations 2008 Compared to 2007 (Continued)

Summary of 2008 Results (Continued)

The following table illustrates the impact on diluted earnings per share of changes in certain components of net income for 2008 compared to 2007:

	2008 vs. 2007	2007 vs. 2006
Net income per diluted share, prior year	$ 0.63	$ 0.74
Increase (decrease) from changes in:		
Net interest income	0.32	(0.14)
Provision for credit losses	(0.17)	0.02
Security transactions (a)	(0.17)	0.01
Insurance commissions	0.02	0.00
Income from bank owned life insurance	(0.01)	0.00
Card related interchange income	0.01	0.00
Letter of credit fees	0.02	0.00
Fees from interest rate derivatives	0.03	0.00
Other operating income	0.00	0.04
Salaries and employee benefits	(0.08)	(0.02)
Occupancy and equipment costs	(0.01)	(0.02)
Advertising expense	0.01	(0.01)
Pennsylvania shares tax expense	0.01	0.00
Intangible amortization	0.01	(0.01)
Low income housing partnership impairment	(0.02)	0.00
Other professional fees and services	(0.01)	0.00
Extinguishment of debt	0.00	(0.01)
Other operating expenses	0.00	(0.02)
Provision for income taxes	(0.01)	0.05
Net income per diluted share	$ 0.58	$ 0.63

(a) Includes $13 million for other-than-temporary impairment charges. Reference Note 10 Impairment of Investment Securities.

Net Interest Income

Net interest income, which is our primary source of revenue, is the difference between interest income from earning assets (loans and securities) and interest expense paid on liabilities (deposits, short-term borrowings and long-term debt). The amount of net interest income is affected by both changes in the level of interest rates and the amount and composition of earning assets and interest-bearing liabilities. The net interest margin is expressed as the percentage of net interest income, on a fully tax equivalent basis, to average earning assets. To compare the tax exempt asset yields to taxable yields, amounts are adjusted to the pretax equivalent amounts based on the marginal corporate Federal income tax rate of 35%. The tax equivalent adjustment to net interest income for 2008 was $13.1 million compared to $14.7 million in 2007.

Net interest income for 2008 was $27.2 million, or 16.9% higher than 2007, primarily due to the $30.7 million decline in interest expense, resulting from an 86 basis point, or 0.86%, decrease in the cost of interest-bearing

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Net Interest Income (Continued)

liabilities. Interest income decreased $3.5 million as the yield on interest-earning assets declined 52 basis points, or 0.52%, which was partially offset by the $368.9 million increase in average interest-earning assets.

Net interest margin, on a tax-equivalent basis, for the year 2008 increased 23 basis points, or 0.23%, to 3.57% from 3.34% in 2007, as the affect of both increased loan volume and declines in the cost of interest-bearing liabilities exceeded the decreases in yields on interest-earning assets. First Commonwealth uses simulation models to help manage exposure to changes in interest rates. A discussion of the effects of changing interest rates is included in the Market Risk section of this discussion.

Interest and fees on loans decreased $2.4 million primarily due to a 78 basis point, or 0.78%, decline in the yield on loans from 7.09% to 6.31% which was partially offset by the $397.5 million, or 10.8%, growth in average loans.

Interest income on investment securities remained stable from 2007 as the $25.3 million decline in the average investment securities offset the slight increase in investment yields.

Interest on deposits decreased $31.3 million due to declines in both rates paid and balances. The cost of interest-bearing deposits decreased 76 basis points, or 0.76%, as a result of the lower interest rate environment and deposit mix changes. Average interest-bearing deposits decreased $72.5 million, or 1.9%, as time deposits declined $139.3 million and interest-bearing demand deposits and savings deposits increased $66.8 million. Management continued its strategy of supplementing deposit growth with wholesale borrowings due to the significant favorable spread between wholesale borrowing costs and rates paid on time deposits.

Interest expense on short-term borrowings increased $3.4 million, or 29.6%, primarily as a result of the $490.7 million growth in average balances, offset by a 217 basis point, or 2.17%, decline in rates paid for these borrowings. Interest expense on long-term debt declined $2.8 million as the $76.4 million decrease in average balances offset the 13 basis point, or 0.13%, increase in rate.

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Net Interest Income (Continued)

The following table provides information regarding the average balances and yields and rates on interest-earning assets and interest-bearing liabilities for each of the three years for the period ended December 31:

Average Balance Sheets and Net Interest Analysis

(dollars in thousands)

	2008			2007			2006		
	Average Balance	Income/ Expense	Yield or Rate (a)	Average Balance	Income/ Expense	Yield or Rate (a)	Average Balance	Income/ Expense	Yield or Rate (a)
Assets									
Interest-earning assets:									
Interest-bearing deposits with banks	$ 447	$ 10	2.34%	$ 639	$ 37	5.82%	$ 1,878	$ 99	5.27%
Tax-free investment securities	290,595	13,143	6.96	304,842	13,732	6.93	281,823	12,876	7.03
Taxable investment securities	1,267,446	62,895	4.96	1,278,469	63,218	4.94	1,487,267	71,215	4.79
Federal funds sold	94	2	2.49	3,204	157	4.89	2,854	142	4.99
Loans, net of unearned income (b)(c)(d)	4,084,506	251,546	6.31	3,687,037	253,951	7.09	3,707,233	248,738	6.92
Total interest-earning assets	5,643,088	327,596	6.04	5,274,191	331,095	6.56	5,481,055	333,070	6.34
Noninterest-earning assets:									
Cash	77,208			80,453			79,509		
Allowance for credit losses	(43,669)			(43,811)			(40,510)		
Other assets	505,790			489,502			452,915		
Total noninterest-earning assets	539,329			526,144			491,914		
Total Assets	$ 6,182,417			$ 5,800,335			$ 5,972,969		
Liabilities and Shareholders Equity									
Interest-bearing liabilities:									
Interest-bearing demand deposits (e)	$ 603,256	$ 5,302	0.88%	$ 595,055	$ 10,538	1.77%	$ 584,717	$ 10,251	1.75%
Savings deposits (e)	1,163,383	18,860	1.62	1,104,789	25,008	2.26	1,138,579	21,496	1.89
Time deposits	1,999,016	77,355	3.87	2,138,296	97,224	4.55	1,889,731	76,707	4.06
Short-term borrowings	769,770	14,828	1.93	279,045	11,442	4.10	568,327	25,448	4.48
Long-term debt	487,533	22,653	4.65	563,919	25,501	4.52	724,846	32,205	4.44
Total interest-bearing liabilities	5,022,958	138,998	2.77	4,681,104	169,713	3.63	4,906,200	166,107	3.39
Noninterest-bearing liabilities and capital:									
Noninterest-bearing demand deposits (e)	544,743			514,256			493,790		
Other liabilities	36,582			32,335			30,526		
Shareholders equity	578,134			572,640			542,453		

Total noninterest-bearing funding sources	1,159,459			1,119,231			1,066,769		
Total Liabilities and Shareholders Equity	$ 6,182,417			$ 5,800,335			$ 5,972,969		
Net Interest Income and Net Yield on Interest-Earning Assets		$ 188,598	3.57%		$ 161,382	3.34%		$ 166,963	3.31%

(a) Yields on interest-earning assets have been computed on a tax equivalent basis using the 35% Federal income tax statutory rate.
(b) Average balance includes loans held for sale in 2006.
(c) Income on nonaccrual loans is accounted for on the cash basis, and the loan balances are included in interest-earning assets.
(d) Loan income includes loan fees.
(e) Average balances do not include reallocations from noninterest-bearing demand deposits and interest-bearing demand deposits into savings deposits which were made for regulatory purposes.

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Net Interest Income (Continued)

The following table sets forth certain information regarding changes in net interest income attributable to changes in the volumes of interest-earning assets and interest-bearing liabilities and changes in the rates for the periods indicated:

Analysis of Year-to-Year Changes in Net Interest Income

(dollars in thousands)

	2008 Change from 2007			2007 Change from 2006		
	Total Change	Change Due to Volume	Change Due to Rate (a)	Total Change	Change Due to Volume	Change Due to Rate (a)
Interest-earning assets:						
Interest-bearing deposits with banks	$ (27)	$ (11)	$ (16)	$ (62)	$ (65)	$ 3
Tax-free investment securities	(589)	(987)	398	856	1,618	(762)
Taxable investment securities	(323)	(544)	221	(7,997)	(10,001)	2,004
Federal funds sold	(155)	(152)	(3)	15	17	(2)
Loans	(2,405)	28,181	(30,586)	5,213	(1,398)	6,611
Total interest income	(3,499)	26,487	(29,986)	(1,975)	(9,829)	7,854
Interest-bearing liabilities:						
NOW and super NOW accounts	(5,236)	145	(5,381)	287	181	106
MMDA and savings accounts	(6,148)	1,326	(7,474)	3,512	(638)	4,150
Time deposits	(19,869)	(6,333)	(13,536)	20,517	10,090	10,427
Short-term borrowings	3,386	20,122	(16,736)	(14,006)	(12,953)	(1,053)
Long-term debt	(2,848)	(3,454)	606	(6,704)	(7,150)	446
Total interest expense	(30,715)	11,806	(42,521)	3,606	(10,470)	14,076
Net interest income	$ 27,216	$ 14,681	$ 12,535	$ (5,581)	$ 641	$ (6,222)

(a) Changes in interest income or expense not arising solely as a result of volume or rate variances are allocated to rate variances due to interest sensitivity of consolidated assets and liabilities.

Provision for Credit Losses

The provision for credit losses is determined based on management s estimates of the appropriate level of allowance for credit losses needed to absorb probable losses inherent in the loan portfolio, after giving consideration to charge-offs and recoveries for the period.

The provision for credit losses increased $13.1 million in 2008 compared to 2007, and exceeded net charge offs by $10.4 million. The increase was primarily a result of an $8.8 million provision added in 2008 for four out-of-market commercial real estate construction loans. Loan growth

of $720.6 million also contributed to the increase in the provision. The allowance for credit losses was $52.8 million at year-end 2008, which represents a ratio of 1.29% of average loans compared to $42.4 million and 1.15% at December 31, 2007.

The increase in charge offs in real estate commercial from $1.8 million in 2007 to $3.5 million 2008 was primarily the result of two in-market loans that have been in the work out process for multiple years and are not indicative of the credit quality of the portfolio as a whole.

Net credit losses for 2008 increased $2.4 million. Net credit losses as a percentage of average loans outstanding increased to 0.31% at December 31, 2008 compared to 0.28% at December 31, 2007. For an analysis of credit quality, see the Non-Performing Loans and Allowance for Credit Losses sections of this discussion.

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Results of Operations 2008 Compared to 2007 (Continued)

Provision for Credit Losses (Continued)

A detailed analysis of our credit loss experience for the five years ended December 31, 2008, is shown below:

Summary of Credit Loss Experience

(dollars in thousands)

	2008	2007	2006	2005	2004
Loans outstanding at end of year	$ 4,418,377	$ 3,697,819	$ 3,783,817	$ 3,624,259	$ 3,514,833
Average loans outstanding	$ 4,084,506	$ 3,687,037	$ 3,707,233	$ 3,597,705	$ 3,251,645
Allowance for credit losses:					
Balance, beginning of year	$ 42,396	$ 42,648	$ 39,492	$ 41,063	$ 37,385
Addition as a result of acquisition	-0-	-0-	1,979	-0-	4,983
Loans charged off:					
Commercial, financial and agricultural	3,640	3,185	2,612	2,462	2,778
Loans to individuals	4,166	3,902	4,565	5,259	5,070
Real estate-construction	67	50	50	598	1
Real estate-commercial	3,479	1,832	522	965	1,060
Real estate-residential	2,529	2,662	2,660	2,103	1,456
Lease financing receivables	-0-	23	54	59	247
Total loans charged off	13,881	11,654	10,463	11,446	10,612
Recoveries of loans previously charged off:					
Commercial, financial and agricultural	426	495	848	601	772
Loans to individuals	522	672	590	550	351
Real estate-construction	-0-	-0-	-0-	-0-	-0-
Real estate-commercial	187	102	-0-	-0-	-0-
Real estate-residential	14	90	45	93	114
Lease financing receivables	-0-	1	-0-	3	-0-
Total recoveries	1,149	1,360	1,483	1,247	1,237
Net loans charged off	12,732	10,294	8,980	10,199	9,375
Credit losses on loans transferred to held for sale	-0-	-0-	1,387	-0-	-0-
Net credit losses	12,732	10,294	10,367	10,199	9,375
Provision for credit losses	23,095	10,042	11,544	8,628	8,070

Balance, end of year	$ 52,759	$ 42,396	$ 42,648	$ 39,492	$ 41,063
Ratios:					
Net credit losses as a percentage of average loans outstanding	0.31%	0.28%	0.28%	0.28%	0.29%
Allowance for credit losses as a percentage of average loans outstanding	1.29%	1.15%	1.15%	1.10%	1.26%

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Results of Operations 2008 Compared to 2007 (Continued)

Non-Interest Income

The components of non-interest income for the three years ended December 31 follow:

	2008	2007	2006
	(dollars in thousands)		
Non-Interest Income			
Trust income	$ 5,639	$ 5,881	$ 5,801
Service charges on deposit accounts	18,558	17,981	16,967
Insurance and retail brokerage commissions	5,297	3,560	2,804
Income from bank owned life insurance	5,523	6,101	5,742
Card related interchange income	7,609	6,564	5,583
Letter of credit fees	2,192	467	827
Fees from interest rate derivatives	2,190	14	-0-
Other operating income	7,317	7,128	5,826
Subtotal	54,325	47,696	43,550
Net securities (losses) gains	(11,494)	1,174	697
Total non-interest income	$ 42,831	$ 48,870	$ 44,247

Total non-interest income of $42.8 million for 2008 decreased $6.0 million, or 12.4%, compared to 2007, primarily related to net securities losses. Offsetting the losses were increases in service charges on deposit accounts, insurance and retail brokerage commissions, card related interchange income, letter of credit fees and fees from interest rate derivatives.

Service charges on deposit accounts are the most significant component of non-interest income and increased $577 thousand primarily due to revenue generated from overdraft fees. Increased fees from service charges on deposit accounts were also generated by the opening of three new branch offices.

Insurance and retail brokerage commissions, including retail advisor fees, increased $1.7 million, or 48.8%, as a result of higher sales driven by additional producers and an enhanced calling program.

We use bank owned life insurance (BOLI) to help offset the rising cost of employee benefits. Income from BOLI decreased $578 thousand, or 9.5%, in 2008 compared to 2007 due to reduced crediting rates of our insurance carriers. The crediting rates we receive consist of two components, yield and market value. The yield is lower as a result of the declining interest rate environment affecting funds allocated to U.S. Treasury securities and the market value is down due to the allocation of funds to asset backed securities which have declined in value.

Card related interchange income increased $1.0 million primarily due to higher usage of debit cards and larger dollar transactions. Card related interchange income includes income from debit, credit and ATM cards that are issued to consumers and businesses.

Increased loan volumes resulted in higher letter of credit fees as well as increased fees from interest rate derivatives of which $1.2 million related to interest rate swaps and $1.0 million related to risk participation agreements.

Net securities losses for 2008 were primarily due to other-than-temporary impairment charges of $9.0 million recorded on a trust preferred collateralized debt obligation security and $4.0 million on equity securities issued by seven Pennsylvania based financial institutions. The 2008 impairment write-downs were partially offset by

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Results of Operations 2008 Compared to 2007 (Continued)

Non-Interest Income (Continued)

gains of $871 thousand on the sale of equity securities and $441 thousand on the mandatory redemption of Class B Common Stock in VISA Inc. The 2007 net securities gains were primarily due to trust preferred investment securities being called at a premium.

Non-Interest Expense

The components of non-interest expense for the three years ended December 31 follow:

	2008	2007	2006
		(dollars in thousands)	
Non-Interest Expense			
Salaries and employee benefits	$ 83,507	$ 76,132	$ 72,988
Net occupancy expense	15,055	13,710	12,077
Furniture and equipment expense	11,976	12,000	11,703
Advertising expense	2,303	2,867	1,750
Data processing expense	4,283	3,808	3,456
Pennsylvania shares tax expense	5,309	5,769	5,420
Intangible amortization	3,208	3,428	2,607
Other professional fees and services	3,404	2,772	2,130
Other operating expenses	28,364	27,521	25,962
Subtotal	157,409	148,007	138,093
Gain on extinguishment of debt, net	-0-	-0-	(410)
Low income housing partnership impairment	1,206	-0-	-0-
Total non-interest expense	$ 158,615	$ 148,007	$ 137,683

Total non-interest expense was $158.6 million for 2008 reflecting an increase of $10.6 million, or 7.2%, over 2007 primarily due to higher salaries and employee benefits, net occupancy expense, and low income housing partnership impairment.

Salaries and employee benefits increased $7.4 million, or 9.7%, primarily as a result of higher incentive compensation expense of $2.7 million related to the strong loan and deposit growth in 2008 and $1.1 million due to greater insurance and retail brokerage sales, as well as annual merit increases and additional personnel expenses related to our new branch offices.

Net occupancy expense increased $1.3 million, or 9.8%, due to higher rental expense, utilities, and building repairs and maintenance.

Data processing expense increased $475 thousand, or 12.5%, primarily due to higher debit card related processing fees as a result of increased usage and an increased card base.

Advertising expense decreased $564 thousand, or 19.7%, primarily due to additional expenses in 2007 associated with branding efforts.

Pennsylvania shares tax expense decreased $460 thousand, or 8.0%, due to a change in the tax calculation which allows the deduction of goodwill from the equity calculation.

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Non-Interest Expense (Continued)

Other professional fees and services increased $632 thousand due to additional expenses incurred for evaluating pooled trust preferred collateralized debt obligations for fair value and impairment, professional development, and sales training.

Other operating expenses increased $843 thousand primarily due to costs associated with higher loan originations, and higher collection and repossession expense.

An impairment charge of $1.2 million was recorded in 2008 on low income housing partnerships because our estimated future benefits could not support our carrying value.

Income Tax

Income tax expense increased $679 thousand in 2008 primarily due to decreases in tax free income and tax credits, which resulted in an increase in our effective tax rate to 13.3% in 2008 compared to 11.4% in 2007.

Financial Condition

First Commonwealth s total assets increased $542.3 million, or 9.2%, in 2008, primarily due to an increase in loans of $720.6 million, or 19.5%, offset by a decrease in investments of $193.5 million, or 11.8%. First Commonwealth s total liabilities increased by $458.3 million, or 8.6%, in 2008. Total short-term borrowings increased $798.5 million, or 225.4%, which was partially offset by a decrease in long-term debt of $271.7 million, or 49.6%, and a decrease in deposits of $66.9 million, or 1.5%.

Loan Portfolio

Following is a summary of our loan portfolio as of December 31:

Loans by Classification

(dollars in thousands)

	2008		2007		2006		2005		2004	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Commercial, financial, agricultural and other	$ 1,272,094	29%	$ 926,904	25%	$ 861,427	23%	$ 729,962	20%	$ 715,280	20%
Real estate-construction	418,639	9	207,708	6	92,192	2	78,279	2	71,351	2
Real estate-residential	1,215,193	28	1,237,986	33	1,346,503	36	1,213,223	33	1,164,707	33
Real estate-commercial	1,016,651	23	861,077	23	935,635	25	987,798	27	988,611	28
Loans to individuals	495,800	11	464,082	13	547,196	14	610,529	17	562,069	16
Net leases	-0-	-0-	62	-0-	864	-0-	4,468	1	12,815	1
Total loans and leases net of unearned income	$ 4,418,377		$ 3,697,819		$ 3,783,817		$ 3,624,259		$ 3,514,833	

Total loans increased $720.6 million, or 19.5%, in 2008. The increase in loans was primarily in the commercial portfolio, with increases of $345.2 million in the commercial, financial, agricultural and other category, $210.9 million in real estate construction, which is primarily commercial construction, and $155.6 million in real estate commercial. Although there was significant growth in the loan portfolio, it was obtained while maintaining our credit quality standards.

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Financial Condition (Continued)

Loan Portfolio (Continued)

The increase in loans includes $377.6 million in participation loans, of which $218.6 million, or 30.3% of total growth, are for projects outside of Pennsylvania. The participations for projects outside of Pennsylvania increased from $154.7 million at December 31, 2007 to $373.3 million at December 31, 2008, or 99.4%. The growth in participation loans for projects outside of Pennsylvania is comprised of $136.7 million in the commercial, financial, agricultural and other loans and $81.9 million in the real estate construction loans.

Total real estate construction loans have increased $210.9 million, or 101.6%, in 2008. The majority of the construction properties are located within Pennsylvania, with less than 35% of the construction loans outside of Pennsylvania. The average outstanding balance of the construction projects in Pennsylvania is $1.8 million, and the average size outside of Pennsylvania is $5.8 million. At origination, the estimated disbursement for the construction process is reviewed, including taking into consideration weather delays, to ensure the adequacy of the interest reserve for the construction period. All disbursements are reviewed by management as well as an independent engineer prior to the customer receiving the funds. We also review the projects regularly for the status of the construction, the amount of disbursements and to monitor the interest reserve. The typical period for a construction project is 18 24 months. A portion of the real estate construction loan portfolio is construction permanent loans with maturities that extend beyond the construction period.

The majority of our loan portfolio is with borrowers located in Pennsylvania. As of December 31, 2008 and 2007, there were no concentrations of loans relating to any industry in excess of 10% of total loans.

Final loan maturities and rate sensitivities of the loan portfolio excluding consumer installment and mortgage loans and before unearned income at December 31, 2008 were as follows (dollars in thousands):

	Within One Year	One to 5 Years	After 5 Years	Total
Commercial and industrial	$ 831,818	$ 131,389	$ 112,363	$ 1,075,570
Financial institutions	40	-0-	-0-	40
Real estate-construction	119,151	175,088	124,400	418,639
Real estate-commercial	141,944	288,448	586,259	1,016,651
Other	30,475	17,276	148,733	196,484
Totals	$ 1,123,428	$ 612,201	$ 971,755	$ 2,707,384
Loans at fixed interest rates		$ 270,939	$ 251,174	
Loans at variable interest rates		341,262	720,581	
Totals		$ 612,201	$ 971,755	

Non-Performing Loans

Non-performing loans include nonaccrual loans and restructured loans. Nonaccrual loans represent loans on which interest accruals have been discontinued. Restructured loans are those loans whose terms have been renegotiated to provide a reduction or deferral of principal or interest as a result of the deteriorating financial position of the borrower.

We discontinue interest accruals on a loan when, based on current information and events, it is probable that we will be unable to fully collect principal or interest due according to the contractual terms of the loan. A loan is also placed in nonaccrual status when, based on regulatory definitions, the loan is maintained on a cash basis due to

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Financial Condition (Continued)

Non-Performing Loans (Continued)

the weakened financial condition of the borrower. Past due loans are those loans which are contractually past due 90 days or more as to interest or principal payments but are well secured and in the process of collection.

Non-performing loans are closely monitored on an ongoing basis as part of our loan review and work-out process. The potential risk of loss on these loans is evaluated by comparing the loan balance to the fair value of any underlying collateral or the present value of projected future cash flows. Losses are recognized where appropriate.

Following is a summary of non-performing loans at December 31:

	2008	2007
	(dollars in thousands)	
Nonaccrual loans	$ 55,922	$ 54,119
Troubled debt restructured loans	132	147
Total non-performing loans	$ 56,054	$ 54,266
Loans past due in excess of 90 days and still accruing	$ 16,189	$ 12,853

Non-performing loans increased $1.8 million, or 3.3%, to $56.1 million at December 31, 2008 compared to $54.3 million at December 31, 2007. Included in nonaccrual loans is a $31.2 million commercial credit relationship that has been monitored since the second quarter of 2006 and was placed on nonaccrual during the second quarter of 2007. This credit is collateralized by real estate and equipment and a reserve has been allocated, primarily during 2006, to cover the expected losses. The payment of principal and interest on this credit was deferred pursuant to two loan forbearance agreements, with the most recent agreement expiring December 31, 2008. Since the expiration of the forbearance agreement we have not received any interest or principal payments. Management continues to monitor the borrower closely and is presently evaluating options with respect to the collection or resolution of this credit.

The following is a comparison of non-performing and impaired assets and the effects on interest due to nonaccrual loans at December 31:

Non-performing and Impaired Assets and Effects

on Interest Income Due to Nonaccrual

(dollars in thousands)

	2008	2007	2006	2005	2004
Nonaccrual loans	$ 55,922	$ 54,119	$ 12,043	$ 11,391	$ 10,732
Troubled debt restructured loans	132	147	160	173	183
Total non-performing loans	$ 56,054	$ 54,266	$ 12,203	$ 11,564	$ 10,915

Non-performing loans as a percentage of total loans	1.27%	1.47%	0.32%	0.32%	0.31%
Allowance as a percentage of non-performing loans	94.12%	78.13%	349.49%	341.51%	376.21%
Other real estate owned	$ 3,262	$ 2,172	$ 1,507	$ 1,655	$ 1,814
Gross income that would have been recorded at original rates	$ 6,265	$ 4,124	$ 3,246	$ 2,344	$ 1,757
Interest that was reflected in income	550	381	706	506	307
Net reduction to interest income due to nonaccrual	$ 5,715	$ 3,743	$ 2,540	$ 1,838	$ 1,450

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ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Financial Condition (Continued)

Non-Performing Loans (Continued)

The non-performing loans as a percentage of total loans decreased from 1.47% at December 31, 2007 to 1.27% at December 31, 2008 primarily due to the loan growth of $720.6 million in 2008.

Other real estate owned increased $1.1 million, or 50.2%, to $3.3 million at December 31, 2008 compared to $2.2 million at December 31, 2007. The increase was primarily due to one large commercial credit placed in other real estate owned in the third quarter of 2008 that was sold in February 2009 for $173 thousand over its carrying value.

Allowance for Credit Losses

The allowance for credit losses represents management s estimate of probable losses inherent in the loan portfolio at a specific point in time. This estimate includes losses associated with specifically identified loans, as well as estimated probable credit losses inherent in the remainder of the loan portfolio. Additions are made to the allowance through both periodic provisions charged to income and recoveries of losses previously incurred. Reductions to the allowance occur as loans are charged off. Management evaluates the adequacy of the allowance at least quarterly, and in doing so relies on various factors including, but not limited to, assessment of historical loss experience, delinquency and nonaccrual trends, portfolio growth, underlying collateral coverage and current economic conditions. This evaluation is subjective and requires material estimates that may change over time. For a description of the methodology used to calculate the allowance for credit losses, please refer to Critical Accounting Policies and Significant Estimates Allowance for Credit Losses.

Following is a summary of the allocation of the allowance for credit losses at December 31:

Allocation of the Allowance for Credit Losses

(dollars in thousands)

	2008	2007	2006	2005	2004
Commercial, industrial, financial, agricultural and other	$ 18,072	$ 16,860	$ 17,030	$ 12,443	$ 12,993
Real estate-construction	10,165	1,217	1,019	1,692	1,045
Real estate-commercial	8,648	11,961	13,529	13,371	12,505
Real estate-residential	7,560	5,146	4,064	3,700	8,061
Loans to individuals	4,338	2,882	3,063	3,984	3,469
Lease financing receivables	-0-	2	14	61	128
Unallocated	3,976	4,328	3,929	4,241	2,862
Total	$ 52,759	$ 42,396	$ 42,648	$ 39,492	$ 41,063
Allowance as a percentage of average total loans	1.29%	1.15%	1.15%	1.10%	1.26%

The allowance for credit losses increased $10.4 million from $42.4 million at December 31, 2007 to $52.8 million at December 31, 2008. The allowance as a percentage of average total loans increased from 1.15% at December 31, 2007 to 1.29% at December 31, 2008. The 2008 increase in the allowance for credit losses was primarily attributable to four out-of-market commercial real estate construction loans that have an aggregate outstanding balance of $13.3 million, and the growth in the loan portfolio of $720.6 million.

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Allowance for Credit Losses (Continued)

Management reviews the local and national economic information and industry data, including the trends in the industries we believe are higher risk, and an allocation is made to the allowance for credit losses based on this review, which is reflected in the unallocated line of the above table. Prior to 2008, there was also an unallocated portion of the allowance to account for any factors or conditions that may cause a potential credit loss that were not specifically identifiable or considered in the allowance for credit loss methodology. In 2008, management determined that the allocation made based upon the review of economic and industry data was sufficient to also account for any other factors that are not specifically identifiable. For years prior to 2008, the unallocated line of the above table includes both the allocation made by management based upon review of economic and industry data and the additional allocation that was made for items that were not specifically identifiable. The unallocated balance decreased $352 thousand from $4.3 million at December 31, 2007 to $4.0 million at December 31, 2008.

Investment Portfolio

Marketable securities that we hold in our investment portfolio, which are classified as securities available for sale, may be a source of liquidity; however, we do not anticipate liquidating the investments prior to maturity. As indicated in Note 21, $68.4 million of available for sale securities are classified as Level 3 assets because of inactivity in the market and therefore would not be considered a source of liquidity. As of December 31, 2008, securities available for sale had an amortized cost and fair value of $1.4 billion. Gross unrealized gains were $28.7 million and gross unrealized losses were $61.9 million.

The following is a schedule of the contractual maturity distribution of securities held to maturity and securities available for sale at December 31, 2008:

Maturity Distribution of Securities Held to Maturity

At Amortized Cost

(dollars in thousands)

	U.S. Government Agencies and U.S. Government Sponsored-Enterprises	States and Political Subdivisions	Other Securities	Total Amortized Cost	Weighted Average Yield*
Within 1 year	$ 11	$ 2,465	$ -0-	$ 2,476	7.77%
After 1 but within 5 years	112	13,207	-0-	13,319	7.38%
After 5 but within 10 years	86	8,870	-0-	8,956	7.20%
After 10 years	-0-	26,089	-0-	26,089	6.43%
Total	$ 209	$ 50,631	$ -0-	$ 50,840	6.88%

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Investment Portfolio (Continued)

Maturity Distribution of Securities Available for Sale

At Amortized Cost

(dollars in thousands)

	U.S. Government Agencies and U.S. Government Sponsored-Enterprises	States and Political Subdivisions	Other Securities	Total Amortized Cost (a)	Weighted Average Yield*
Within 1 year	$ 3,984	$ 810	$ 5,268	$ 10,062	2.98%
After 1 but within 5 years	161,427	9,817	-0-	171,244	4.61%
After 5 but within 10 years	335,384	45,184	1,181	381,749	4.69%
After 10 years	531,670	160,154	119,925	811,749	5.65%
Total	$ 1,032,465	$ 215,965	$ 126,374	$ 1,374,804	5.24%

(a) Stock equities are excluded from this schedule because they have an indefinite maturity.
* Yields are calculated on a tax-equivalent basis.

The decrease in average securities of $25.2 million in 2008 helped to fund loan growth. The largest components of the 2008 decrease included $39.8 million of corporate securities, $82.1 million of other agencies, $13.5 million of states and political subdivisions, and $783 thousand in treasury securities. Offsetting these decreases was an average increase of $103.7 million of mortgage backed securities and $7.7 million in marketable equity securities.

Included in equity securities is stock in the Federal Home Loan Bank (FHLB) of Pittsburgh. As a member, we are required to purchase and hold stock in the FHLB of Pittsburgh to satisfy membership and borrowing requirements. As of December 31, 2008 and 2007, our FHLB stock totaled $51.4 million and $27.5 million, respectively. This investment is recorded at historical cost. For the years ended December 31, 2008, 2007 and 2006, we received dividends from our FHLB stock totaling $1.3 million, $1.7 million, and $2.0 million, respectively. In December 2008, the FHLB of Pittsburgh suspended dividend payments on their stock and the repurchase of excess stock from members.

See Note 8 Securities Available for Sale, Note 9 Securities Held to Maturity, Note 10 Impairment of Investment Securities, and Note 21 Fair Values of Financial Instruments for additional information related to the investment portfolio.

Our investment portfolio includes $97.1 million in pooled trust preferred collateralized debt obligations. The valuation of these securities involves evaluating all relevant credit and structural aspects, determining appropriate performance assumptions and performing a discounted cash flow analysis. This evaluation includes detailed credit, performance and structural evaluations for each piece of collateral. Other factors in the valuation include terms of the structure, the cash flow waterfall (for both interest and principal), the over collateralization and interest

coverage tests and events of default/liquidation.

The discount rate used in the analysis combines an evaluation of current and observable market yields for comparable structured credit products with an evaluation of the risks associated with the underlying cash flows.

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Investment Portfolio (Continued)

The specific risks identified in a given collateralized debt obligations cash flows are then evaluated and an adjustment is made to the credit spreads derived from market sources on the basis of this evaluation.

In order to test the model s collateral performance assumptions, specifically default probabilities, our internal credit analysis area completes independent financial review for a sample of securities. A function independent of the area initiating the risk position is an integral part of the review and approval of the valuation adjustments.

The security prices obtained were not adjusted, and were non-binding quotes. Fair values used for investment securities are validated through periodic reviews of changes in total portfolio value, as well as key portfolio groups, compared to movements in interest rates, credit risks as well as underlying financial markets.

Additional information as of December 31, 2008 related to our pooled trust preferred collateralized debt obligations is provided in the table below:

Pooled Trust Preferred Security Detail

(dollars in thousands)

Deal	Class	Book Value	Fair Value	Unrealized Gain (Loss)	Moody s/ Fitch Ratings	Number of Banks	Deferrals and Defaults as a % of Current Collateral
PreTSL I	Senior	$ 3,841	$ 4,212	$ 371	Aa1/AAA	33	12.70%
PreTSL IV	Mezzanine	1,830	905	(925)	Ba3/A+(n)	6	18.05%
PreTSL V	Mezzanine	620	289	(331)	B3/A(n)	4	0.00%
PreTSL VI	Mezzanine	388	207	(181)	B3/A(n)	5	0.00%
PreTSL VII	Mezzanine	3,987	3,987	-0-	Caa2/A+(n)	20	30.71%
PreTSL VIII	Mezzanine	5,980	2,272	(3,708)	B3/A(n)	36	10.59%
PreTSL IX	Mezzanine	3,000	1,194	(1,806)	Ba3/A(n)	49	6.14%
PreTSL X	Mezzanine	4,000	1,572	(2,428)	B3/A(n)	58	11.13%
PreTSL XII	Mezzanine	10,000	3,878	(6,122)	B3/A(n)	81	8.20%
PreTSL XIII	Mezzanine	17,540	6,881	(10,659)	B3/A(n)	66	8.22%
PreTSL XIV	Mezzanine	16,047	6,112	(9,935)	Ba3/A(n)	64	4.19%
MMCap I	Senior	8,838	7,010	(1,828)	Aa1/AAA	29	7.32%
MMCap I	Mezzanine	1,065	541	(524)	B1/BBB	29	7.32%
MMCap IX	Mezzanine	20,000	8,020	(11,980)	B3/A-(n)	34	10.19%
Total		$ 97,136	$ 47,080	$ (50,056)			

As a result of our cash flow analysis for PreTSL VII, we determined that all contractual cash flows may not be received, and a $9.0 million other-than-temporary impairment charge was recorded for this security in 2008. Any future deferrals or defaults for this security will likely result in an additional other-than-temporary impairment charge.

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Deposits

Total deposits decreased $66.9 million, or 1.5%, in 2008, as a $110.5 million decrease in interest-bearing deposits was partially offset by a $43.6 million increase in non-interest bearing deposits. The decrease in interest-bearing deposits was due to a $337.2 million decrease in higher-costing time deposits that was partly offset by a $226.7 million increase in savings deposits. Non-core deposits, which are time deposits in denominations of $100,000 or more, decreased $243.7 million in 2008 and represented 13.6% of total deposits at December 31, 2008. Non-core deposits as of December 31, 2007 totaled $827.0 million and represented 19.0% of total deposits.

Time deposits of $100,000 or more had remaining maturities as follows as of the end of each year in the three-year period ended December 31, 2008:

Maturity Distribution of Large Certificates of Deposit

(dollars in thousands)

	2008		2007		2006	
	Amount	Percent	Amount	Percent	Amount	Percent
Remaining Maturity:						
3 months or less	$ 174,150	30%	$ 329,977	40%	$ 321,137	40%
Over 3 months through 6 months	123,589	21	189,572	23	148,843	19
Over 6 months through 12 months &n						