UNIVEST CORP OF PENNSYLVANIA
Form 10-Q
May 10, 2007

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**United States**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, DC 20549**

**Form 10-Q**

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2007.

or

o Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _________ to _________.

Commission File Number: 0-7617

UNIVEST CORPORATION OF PENNSYLVANIA
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Pennsylvania | 23-1886144 |
| (State or other jurisdiction of incorporation of organization) | (IRS Employer Identification No.) |

14 North Main Street, Souderton, Pennsylvania 18964
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code: (215) 721-2400

Not applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed 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. RYes £No

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

Large accelerated filer £ Accelerated filer R Non-accelerated filer £

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

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

| | |
|---|---|
| Common Stock, $5 par value | 12,978,481 |
| (Title of Class) | (Number of shares outstanding at 3/31/07) |

UNIVEST CORPORATION OF PENNSYLVANIA AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

**UNIVEST CORPORATION OF PENNSYLVANIA**
**CONDENSED CONSOLIDATED BALANCE SHEETS**

| | (UNAUDITED) March 31, 2007 | (SEE NOTE) December 31, 2006 |
|---|---|---|
| **ASSETS** | (In thousands, except share data) | |
| Cash and due from banks | **$ 46,291** | $ 46,956 |
| Interest-earning deposits with other banks | **478** | 582 |
| Federal funds sold | **15,420** | 22,817 |
| Investment securities held-to-maturity (market value $2,463 and $2,685 at March 31, 2007 and December 31, 2006, respectively) | **2,394** | 2,619 |
| Investment securities available-for-sale | **377,093** | 379,781 |
| Loans and leases | **1,372,523** | 1,353,681 |
| Less: Reserve for loan and lease losses | **(13,414)** | (13,283) |
| Net loans and leases | **1,359,109** | 1,340,398 |
| Premises and equipment, net | **21,833** | 21,878 |
| Goodwill, net of accumulated amortization of $2,942 at March 31, 2007 and December 31, 2006 | **44,425** | 44,273 |
| Other intangibles, net of accumulated amortization and fair value adjustments of $5,134 and $5,113 at March 31, 2007 and December 31, 2006, respectively | **3,194** | 3,335 |
| Cash surrender value of insurance policies | **37,008** | 36,686 |
| Accrued interest and other assets | **28,685** | 30,176 |
| Total assets | **$ 1,935,930** | $ 1,929,501 |
| | | |
| **LIABILITIES** | | |
| Demand deposits, noninterest-bearing | **$ 244,410** | $ 263,417 |
| Demand deposits, interest-bearing | **519,102** | 508,140 |
| Savings deposits | **204,815** | 195,126 |
| Time deposits | **553,013** | 521,862 |
| Total deposits | **1,521,340** | 1,488,545 |
| Securities sold under agreements to repurchase | **83,826** | 99,761 |
| Other short-term borrowings | **-** | 17,900 |
| Accrued expenses and other liabilities | **35,962** | 30,505 |
| Long-term debt | **75,919** | 77,036 |
| Subordinated notes | **9,375** | 9,750 |
| Company-obligated mandatorily redeemable preferred securities of subsidiary trusts holding junior subordinated debentures of Univest ("Trust Preferred Securities") | **20,619** | 20,619 |
| Total liabilities | **1,747,041** | 1,744,116 |
| **SHAREHOLDERS' EQUITY** | | |
| Common stock, $5 par value: 24,000,000 shares authorized at March 31, 2007 and December 31, 2006; 14,873,904 shares issued at March 31, 2007 and December 31, 2006; 12,978,481 and 13,005,329 shares outstanding at March 31, 2007 and December 31, 2006, respectively | **74,370** | 74,370 |
| Additional paid-in capital | **22,493** | 22,459 |

| | | | | |
|---|---|---|---|---|
| Retained earnings | | **131,884** | | 128,242 |
| Accumulated other comprehensive loss, net of tax benefit | | **(3,974)** | | (4,463) |
| Treasury stock, at cost; 1,895,423 and 1,868,575 shares at March 31, 2007 and December 31, 2006, respectively | | **(35,884)** | | (35,223) |
| Total shareholders' equity | | **188,889** | | 185,385 |
| Total liabilities and shareholders' equity | **$** | **1,935,930** | $ | 1,929,501 |

Note: The condensed consolidated balance sheet at December 31, 2006 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statement. See accompanying notes to the unaudited condensed consolidated financial statements.

**UNIVEST CORPORATION OF PENNSYLVANIA**
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**
**(Unaudited)**

| | For the Three Months Ended March 31, 2007 | 2006 |
|---|---|---|
| **Interest income** | ($ in thousands, except per share data) | |
| Interest and fees on loans and leases: | | |
| Taxable | $ **22,585** | $ 19,160 |
| Exempt from federal income taxes | **1,019** | 916 |
| Total interest and fees on loans and leases | **23,604** | 20,076 |
| Interest and dividends on investment securities: | | |
| Taxable | **3,684** | 2,446 |
| Exempt from federal income taxes | **948** | 967 |
| Other interest income | **64** | 63 |
| Total interest income | **28,300** | 23,552 |
| **Interest expense** | | |
| Interest on deposits | **10,395** | 6,697 |
| Interest on long-term borrowings | **1,466** | 1,156 |
| Interest on short-term debt | **994** | 707 |
| Total interest expense | **12,855** | 8,560 |
| Net interest income | **15,445** | 14,992 |
| Provision for loan and lease losses | **624** | 511 |
| Net interest income after provision for loan and lease losses | **14,821** | 14,481 |
| **Noninterest income** | | |
| Trust fee income | **1,487** | 1,551 |
| Service charges on deposit accounts | **1,650** | 1,672 |
| Investment advisory commission and fee income | **679** | 549 |
| Insurance commission and fee income | **1,875** | 1,377 |
| Life insurance income | **322** | 386 |
| Other service fee income | **866** | 754 |
| Net gain (loss) on sales of securities | **-** | - |
| Other | **37** | 156 |
| Total noninterest income | **6,916** | 6,445 |
| **Noninterest expense** | | |
| Salaries and benefits | **7,794** | 7,305 |
| Net occupancy | **1,251** | 1,068 |
| Equipment | **775** | 772 |
| Marketing and advertising | **165** | 535 |
| Other | **3,177** | 2,809 |
| Total noninterest expense | **13,162** | 12,489 |
| Income before income taxes | **8,575** | 8,437 |
| Applicable income taxes | **2,328** | 2,223 |
| Net income | $ **6,247** | $ 6,214 |
| **Net income per share:** | | |
| Basic | $ **0.48** | $ 0.48 |
| Diluted | **0.48** | 0.48 |
| Dividends declared | **0.20** | 0.19 |

Note: See accompanying notes to the unaudited condensed consolidated financial statements.

**UNIVEST CORPORATION OF PENNSYLVANIA**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(Unaudited)**

| | For the Three Months Ended March 31, | |
|---|---|---|
| | **2007** | 2006 |
| Cash flows from operating activities: | ($ in thousands) | |
| Net income | **$ 6,247** | $ 6,214 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan and lease losses | **624** | 511 |
| Depreciation of premises and equipment | **513** | 536 |
| Increase in cash surrender value of insurance policies | **(322)** | (386) |
| Other adjustments to reconcile net income to cash provided by operating activities | **(59)** | (8) |
| Decrease (increase) in accrued interest receivable and other assets | **1,257** | (3,082) |
| Increase (decrease) in accrued expenses and other liabilities | **5,441** | (2,686) |
| Net cash provided by operating activities | **13,701** | 1,099 |
| Cash flows from investing activities: | | |
| Net cash paid due to acquisitions, net of cash acquired | **(198)** | (152) |
| Net capital expenditures | **(467)** | (991) |
| Proceeds from maturing securities held-to-maturity | **226** | 308 |
| Proceeds from maturing securities available-for-sale | **16,267** | 11,975 |
| Proceeds from sales of securities available-for-sale | **8,380** | 7,470 |
| Purchases of investment securities available-for-sale | **(21,115)** | (7,827) |
| Proceeds from sales of loans and leases | **246** | 449 |
| Purchases of financing leases | **(6,478)** | |
| Net increase in loans and leases | **(13,034)** | (38,252) |
| Net decrease (increase) in interest-bearing deposits | **104** | (58) |
| Net decrease in federal funds sold | **7,397** | 5,528 |
| Net cash used in investing activities | **(8,672)** | (21,550) |
| Cash flows from financing activities: | | |
| Net increase in deposits | **32,741** | 38,391 |
| Net decrease in short-term borrowings | **(33,835)** | (17,463) |
| Repayment of long-term debt | **(1,000)** | |
| Repayment of subordinated debt | **(375)** | (375) |
| Purchases of treasury stock | **(1,273)** | (1,029) |
| Stock issued under dividend reinvestment and employee stock purchase plans | **492** | 552 |
| Proceeds from exercise of stock options | **151** | 158 |
| Cash dividends paid | **(2,595)** | (2,462) |
| Net cash (used in) provided by financing activities | **(5,694)** | 17,772 |
| Net decrease in cash and due from banks | **(665)** | (2,679) |
| Cash and due from banks at beginning of year | **46,956** | 46,226 |

| | | | | |
|---|---|---|---|---|
| Cash and due from banks at end of period | **$** | **46,291** | $ | 43,547 |
| | | | | |
| Supplemental disclosures of cash flow information | | | | |
| Cash paid (received) during the year for: | | | | |
| Interest expense | **$** | **13,623** | $ | 8,275 |
| Income taxes, net of refunds received | | **(2)** | | 23 |

Note: See accompanying notes to the unaudited condensed consolidated financial statements.

**UNIVEST CORPORATION OF PENNSYLVANIA AND SUBSIDIARIES**

**Notes to the Unaudited Condensed Consolidated Financial Statements**

**Note 1. Financial Information**

The accompanying unaudited condensed consolidated financial statements include the accounts of Univest Corporation of Pennsylvania (the "Corporation") and its wholly owned subsidiaries; the Corporation's primary subsidiary is Univest National Bank and Trust Co. (the "Bank"). The unaudited condensed consolidated financial statements included herein have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States have been condensed or omitted pursuant to such rules and regulations. The accompanying unaudited condensed consolidated financial statements reflect all adjustments which are of a normal recurring nature and are, in the opinion of management, necessary to present a fair statement of the results and condition for the interim periods presented. Operating results for the three-month period ended March 31, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. It is suggested that these unaudited condensed consolidated financial statements be read in conjunction with the financial statements and the notes thereto included in the registrant's Annual Report on Form 10-K for the year ended December 31, 2006, which has been filed with the SEC on March 8, 2007.

**Note 2. Loan and Leases**

The following is a summary of the major loan and lease categories:

| ($ in thousands) | | **At March 31, 2007** | | At December 31, 2006 |
|---|---|---|---|---|
| Commercial, financial and agricultural | **$** | **445,422** | $ | 442,182 |
| Real estate-commercial | | **355,627** | | 352,596 |
| Real estate-construction | | **144,143** | | 136,331 |
| Real estate-residential | | **305,767** | | 305,306 |
| Loans to individuals | | **84,866** | | 89,217 |
| Lease financings | | **39,810** | | 30,186 |
| Total gross loans and leases | | **1,375,635** | | 1,355,818 |
| Less: Unearned income | | **(3,112)** | | (2,137) |
| Total loans and leases | **$** | **1,372,523** | $ | 1,353,681 |

**Note 3. Reserve for Loan and Lease Losses**

A summary of the activity in the reserve for loan and lease losses is as follows:

| ($ in thousands) | | **Three Months Ended March 31, 2007** | | 2006 |
|---|---|---|---|---|
| Reserve for loan and lease losses at beginning of period | **$** | **13,283** | $ | 13,363 |
| Provision for loan and lease losses | | **624** | | 511 |
| Recoveries | | **159** | | 274 |
| Loans and leases charged off | | **(652)** | | (292) |
| Reserve for loan and lease losses at period end | **$** | **13,414** | $ | 13,856 |

Information with respect to loans and leases that are considered to be impaired under SFAS 114 at March 31, 2007 and December 31, 2006 is as follows:

| ($ in thousands) | **At March 31, 2007** Balance | Specific Reserve | At December 31, 2006 Balance | Specific Reserve |
|---|---|---|---|---|
| Recorded investment in impaired loans and leases at period-end subject to a specific reserve for loan and lease losses and corresponding specific reserve | **$ 4,451** | **$ 1,498** | $ 5,606 | $ 1,576 |
| Recorded investment in impaired loans and leases at period-end requiring no specific reserve for loan and lease losses | **3,301** | | 2,837 | |
| Recorded investment in impaired loans and leases at period-end | **$ 7,752** | | $ 8,443 | |
| Recorded investment in nonaccrual and restructured loans and leases | **$ 7,752** | | $ 8,443 | |

The following is an analysis of interest on nonaccrual and restructured loans and leases:

| ($ in thousands) | **Three Months Ended March 31, 2007** | 2006 |
|---|---|---|
| Nonaccrual and restructured loans and leases at period end | **$ 7,752** | $ 5,343 |
| Average recorded investment in impaired loans and leases | **8,186** | 4,321 |
| Interest income that would have been recognized under original terms | **198** | 118 |

No interest income was recognized on these loans for the three-month periods ended March 31, 2007 and 2006.

**Note 4. Earnings Per Share**

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

| (in thousands, except per share data) | Three Months Ended March 31, **2007** | 2006 |
|---|---|---|
| Numerator: | | |
| Numerator for basic and diluted earnings per share - Net income | **$ 6,247** | $ 6,214 |
| Denominator: | | |
| Denominator for basic earnings per share - weighted-average shares outstanding | **13,004** | 12,945 |
| Effect of dilutive securities: | | |
| Employee stock options | **49** | 74 |
| Denominator for diluted earnings per share - adjusted weighted-average shares outstanding | **13,053** | 13,019 |
| Basic earnings per share | **$ 0.48** | $ 0.48 |

| | | | | |
|---|---|---|---|---|
| Diluted earnings per share | **$** | **0.48** | $ | 0.48 |

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**Note 5. Accumulated Comprehensive Income**

The following shows the accumulated comprehensive income, net of income taxes, for the periods presented:

| ($ in thousands) | For the Three Months Ended March 31, **2007** | 2006 |
|---|---|---|
| Net Income | **$ 6,247** | $ 6,214 |
| Unrealized loss on cash flow hedges: | | |
| Unrealized holding losses arising during the period | | (11) |
| Unrealized gain (loss) on available-for-sale investment securities: | | |
| Unrealized gains (losses) arising during the period | **509** | (869) |
| Defined benefit pension plans: | | |
| Unrealized losses arising during the period | **(52)** | |
| Less: amortization of net gain included in net periodic pension costs | **(47)** | |
| Less: accretion of prior service cost included in net periodic pension costs | **15** | |
| Total comprehensive income | **$ 6,736** | $ 5,334 |

**Note 6. Pensions and Other Postretirement Benefits**

Components of net periodic benefit cost:

| ($ in thousands) | Three Months Ended March 31, 2007 | 2006 | 2007 | 2006 |
|---|---|---|---|---|
| | Retirement Plans | | Other Postretirement | |
| Service cost | $ 362 | $ 340 | $ 16 | $ 14 |
| Interest cost | 419 | 414 | 19 | 19 |
| Expected return on plan assets | (415) | (382) | | |
| Amortization of net gain | 70 | 70 | 3 | 3 |
| Accretion of prior service cost | (18) | (18) | (5) | (5) |
| Net periodic benefit cost | $ 418 | $ 424 | $ 33 | $ 31 |

The Corporation previously disclosed in its financial statements for the year ended December 31, 2006, that it expected to make payments of $1.7 million for its qualified and non-qualified retirement plans and $92 thousand for its other postretirement benefit plans in 2007. As of March 31, 2007, $401 thousand and $25 thousand have been paid from its retirement plans and other postretirement plans, respectively. During the three months ended March 31, 2007, the Corporation contributed $126 thousand and $25 thousand to its non-qualified retirement plans and other postretirement plans, respectively. The Corporation presently anticipates making essentially equal payments for the remaining quarters in 2007 to fund the non-qualified retirement plan and other postretirement plans.

**Note 7. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities."**

At March 31, 2006, the total notional amount of the "Pay Floating, Receive Fixed" swap outstanding was $20.0 million. The net payable or receivable from the interest-rate swap agreement was accrued as an adjustment to interest income. The $20.0 million notional amount of interest-rate swap outstanding expired on November 2, 2006. There were no swaps outstanding at March 31, 2007 or December 31, 2006.

**Note 8. Income Taxes**

Effective January 1, 2007 the Corporation adopted Financial Interpretation No. 48, “Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109” (“FIN 48”). FIN 48 provides guidance on financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. According to FIN 48, a tax position is recognized if it is more-likely-than-not that the tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. If the tax position meets the more-likely-than-not recognition threshold, the position is measured to determine the amount of benefit to recognize and should be measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

As of January 1, 2007, the Coporation had no material unrecognized tax benefits, accrued interest or penalties. Penalties are recorded in non-interest expense in the year they are assessed and are treated as a non-deductible expense for tax purposes. Interest is recorded in non-interest expense in the year it is assessed and is treated as a deductible expense for tax purposes. As of January 1, 2007, Tax Years 2003 through 2006 remain subject to Federal examination as well as examination by state taxing jurisdictions.

**Note 9. Recent Accounting Pronouncements**

In September 2006, the Emerging Issues Task Force (“EITF”) reached a conclusion on EITF No. 06-4, “Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements,” (“EITF 06-4.”) EITF 06-4 is effective for fiscal years beginning after December 15, 2007. Under EITF 06-4, if an agreement is to provide the employee with a death benefit in a postretirement/termination period, the employer should recognize a liability for the future death benefit in accordance with either Statement of Financial Accounting Standard (“SFAS”) No. 106 or Accounting Principles Board Opinion No. 12. EITF 06-4 requires that recognition of the effects of adoption should be either by (a) a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or (b) a change in accounting principle through retrospective application to all prior periods. The potential impact to the Corporation will be negative cumulative-effect adjustment to retained earnings of approximately $1.6 million and would not be tax affected.

In September 2006, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 157, “Fair Value Measurements” (“SFAS 157”). SFAS 157 establishes a framework for measuring fair value in GAAP, and enhances disclosures about fair value measurements. SFAS 157 applies when other accounting pronouncement require fair value measurements; it does not require new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and for interim periods within those years. The Corporation chose not to adopt SFAS 157 early. The Corporation does not anticipate the adoption of SFAS 157 in the Fiscal Year 2008 to have a material impact on its financial statements.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities (Including an amendment of FASB Statement No. 115)” (“SFAS 159.”) SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of SFAS 159 is to improve financial reporting by allowing entities to minimize volatility in reported earnings caused by related assets and liabilities being measured differently. Most of the provisions of SFAS 159 apply only to entities that elect the fair value option. However, SFAS 159 includes an amendment to SFAS 115 which applies to all entities with available-for-sale and trading securities. Entities electing the fair value option will report unrealized gains and losses in earnings and recognize upfront costs and fees related to those items in earnings as they are incurred, not deferred. The following items are eligible for the fair value measurement option established by SFAS 159: 1) Recognized financial assets and financial liabilities, except (a) an investment in a subsidiary that is required to be consolidated, (b) an interest in a variable interest entity that is required to be consolidated, (c) obligations (or assets representing net over funded positions) for pension plans, other postretirement benefits, post employment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, (d) financial assets and liabilities recognized under leases, (e) demand deposit liabilities of financial institutions, and (f) financial instruments classified by the issuer as a component of shareholder's equity; 2) firm commitments that would otherwise not be recognized at inception and that involve only financial instruments; 3) nonfinancial insurance contracts and warranties that the insurer can settle by paying a third party to provide those goods or services; and, 4) host financial instruments resulting from separation of an embedded nonfinancial derivative instrument from a nonfinancial hybrid instrument. The fair value option may be applied on an instrument-by-instrument basis, with a few exceptions, such as investments otherwise accounted for by the equity method or multiple advanced made to one borrower under a single contract. The fair value option is irrevocable unless a new election date occurs and applies only to entire instruments and not to portions of instruments. Entities are permitted to elect fair value option for any eligible item within the scope of SFAS 159 at the date they initially adopt the SFAS 159. The adjustment to reflect the difference between the fair value and the current carrying amount of the assets and liabilities for which an entity elects fair value option is reported as a cumulative-effect adjustment to the opening balance of retained earnings upon adoption. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS 157. The Corporation chose not to adopt SFAS 159 early. The Corporation does not anticipate the adoption of SFAS 159 in the Fiscal Year 2008 to have a material impact on its financial statements.

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

**Forward-Looking Statements**

The information contained in this report may contain forward-looking statements. When used or incorporated by reference in disclosure documents, the words "believe," "anticipate," "estimate," "expect," "project," "target," "goal" and similar expressions are intended to identify forward-looking statements within the meaning of section 27A of the Securities Act of 1933. Such forward-looking statements are subject to certain risks, uncertainties and assumptions, including those set forth below:

- Operating, legal and regulatory risks
- Economic, political and competitive forces impacting various lines of business
- The risk that our analysis of these risks and forces could be incorrect and/or that the strategies developed to address them could be unsuccessful
- Volatility in interest rates
- Other risks and uncertainties

Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, expected or projected. These forward-looking statements speak only as of the date of the report. The Corporation expressly disclaims any obligation to publicly release any updates or revisions to reflect any change in the Corporation's expectations with regard to any change in events, conditions or circumstances on which any such statement is based.

**General**

Univest Corporation of Pennsylvania, (the “Corporation”), is a Financial Holding Company. It owns all of the capital stock of Univest National Bank and Trust Co. (the “Bank”), Univest Realty Corporation, Univest Delaware, Inc., and Univest Reinsurance Corporation.

The Bank is engaged in the general commercial banking business and provides a full range of banking services and trust services to its customers. Vanguard Leasing, Inc., a wholly owned subsidiary of the Bank, provides lease financing. Delview, Inc., a wholly owned subsidiary of the Bank, provides various financial services including financial planning, investment management, insurance products and brokerage services to individuals and businesses through its subsidiaries Univest Investments, Inc. and Univest Insurance, Inc.

**Executive Overview**

The Corporation recorded net income of $6.2 million for both three-month periods ended March 31, 2007 and 2006.

Average earning assets increased $140.6 million and average interest-bearing liabilities increased $136.0 million when comparing the three-month periods ended March 31, 2007 and 2006. Increased volume and rates on commercial business loans and commercial and construction real estate loans, partially offset by increased volume and rates on money market savings and certificates of deposits, contributed to a $453 thousand increase in net interest income. The tax-equivalent net interest margin declined slightly to 3.81% for the three-month period ended March 31, 2007 compared to 4.01% for the same period in 2006.

Non-interest income grew 7.30%, when comparing the three-month periods ended March 31, 2007 to 2006, primarily due to increases in insurance commission and fee income.

Non-interest expense grew 5.38% primarily due to salary and employee benefit expense.

The Corporation earns its revenues primarily from the margins and fees it generates from the loan and depository services it provides as well as from trust, insurance and investment commissions and fees. The Corporation seeks to achieve adequate and reliable earnings by growing its business while maintaining adequate levels of capital and liquidity and limiting its exposure to credit and interest rate risk to Board approved levels. As interest rates increase, fixed-rate assets that banks hold will tend to decrease in value while the margin impact will vary from bank to bank based upon the structure of its balance sheet. The Corporation maintains a relatively low interest rate risk profile and does not anticipate that an increase in interest rates would be adverse to its net interest margin.

The Corporation seeks to establish itself as the financial provider of choice in the markets it serves. It plans to achieve this goal by offering a broad range of high quality financial products and services and by increasing market awareness of its brand and the benefits that can be derived from its products. The Corporation operates in an attractive market for financial services but also is in intense competition with domestic and international banking organizations and other insurance and investment providers for the financial services business. The Corporation has taken initiatives to achieve its business objective by acquiring banks and other financial service providers in strategic markets, by marketing, public relations and advertising, by establishing standards of service excellence for its customers, and by using technology to ensure that the needs of its customers are understood and satisfied.

**Results of Operations - Three Months Ended March 31, 2007 Versus 2006**

The Corporation's consolidated net income and earnings per share for the three months ended March 31, 2007 and 2006 were as follows:

| ($ in thousands, except per share data) | For the Three Months Ended March 31, 2007 | 2006 | Change Amount | Percent |
|---|---|---|---|---|
| Net income | $ 6,247 | $ 6,214 | $ 33 | 0.53% |
| Net income per share: | | | | |
| Basic | $ 0.48 | $ 0.48 | — | — |
| Diluted | 0.48 | 0.48 | — | — |

Return on average shareholders' equity was 13.33% and return on average assets was 1.31% for the three months ended March 31, 2007 compared to 14.24% and 1.41%, respectively, for the same period in 2006.

**Net Interest Income**

Net interest income is the difference between interest earned on loans, investments and other interest-earning assets and interest paid on deposits and other interest-bearing liabilities. Net interest income is the principal source of the Corporation's revenue. The following table presents a summary of the Corporation's average balances; the tax-equivalent yields earned on average assets, and the cost of average liabilities for the three months ended March 31, 2007 and 2006. Sensitivities associated with the mix of assets and liabilities are numerous and complex. The Asset/Liability Management and Investment committees work to maintain an adequate and reliable net interest margin for the Corporation.

Net interest income increased $453 thousand for the three months ended March 31, 2007 compared to the same period in 2006 primarily due to increased volume and rates on commercial loans and commercial real estate and construction loans, partially offset by increased volume and rates on money market savings deposits and certificates of deposit. The tax-equivalent net interest margin, which is tax-equivalent net interest income as a percentage of average interest-earning assets, was 3.81% and 4.01% for the three-month period ended March 31, 2007 and 2006, respectively. The tax-equivalent net interest spread, which represents the difference between the weighted average tax-equivalent yield on interest-earning assets and the weighted average cost of interest-bearing liabilities, was 3.24% for the three months ended March 31, 2007 compared to 3.56% for the same period in 2006. The effect of net interest free funding sources increased to 0.57% for the three months ended March 31, 2007 compared to 0.45% for the same period in 2006; this represents the effect on the net interest margin of net funding provided by noninterest-earning assets, noninterest-bearing liabilities and shareholders' equity.

**Table 1 — Distribution of Assets, Liabilities and Stockholders' Equity; Interest Rates and Interest Differential**

| | For the Three Months Ended March 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | | 2006 | | |
| | Average Balance | Income/ Expense | Avg. Rate | Average Balance | Income/ Expense | Avg. Rate |
| **Assets:** | | | | | | |
| Interest-earning deposits with other banks | $ **594** | $ **7** | **4.78%** | $ 610 | $ 6 | 3.99% |
| U.S. Government obligations | **123,249** | **1,351** | **4.45** | 152,557 | 1,297 | 3.45 |
| Obligations of states & political subdivisions | **82,983** | **1,458** | **7.13** | 84,612 | 1,486 | 7.12 |
| Other securities | **175,961** | **2,308** | **5.32** | 97,494 | 1,124 | 4.68 |
| Federal Reserve bank stock | **1,687** | **25** | **6.01** | 1,687 | 25 | 6.01 |
| Federal funds sold | **5,197** | **57** | **4.45** | 5,439 | 57 | 4.25 |
| Total interest-earning deposits, investments and federal funds sold | **389,671** | **5,206** | **5.42** | 342,399 | 3,995 | 4.73 |
| Commercial, financial and agricultural loans | **407,934** | **7,967** | **7.92** | 365,210 | 6,402 | 7.11 |
| Real estate commercial and construction loans | **432,734** | **8,334** | **7.81** | 401,242 | 7,102 | 7.18 |
| Real estate residential loans | **305,199** | **4,112** | **5.46** | 303,119 | 4,007 | 5.36 |
| Loans to individuals | **85,702** | **1,485** | **7.03** | 105,786 | 1,638 | 6.28 |
| Municipal loans | **92,839** | **1,469** | **6.42** | 86,748 | 1,275 | 5.96 |
| Lease financings | **31,386** | **687** | **8.88** | 323 | 11 | 13.81 |
| Gross loans and leases | **1,355,794** | **24,054** | **7.20** | 1,262,428 | 20,435 | 6.56 |
| Total interest-earning assets | **1,745,465** | **29,260** | **6.80** | 1,604,827 | 24,430 | 6.17 |
| Cash and due from banks | **39,075** | | | 39,173 | | |
| Reserve for loan losses | **(13,315)** | | | (13,572) | | |
| Premises and equipment, net | **21,888** | | | 21,571 | | |
| Other assets | **108,845** | | | 104,650 | | |
| Total assets | **$ 1,901,958** | | | $ 1,756,649 | | |
| **Liabilities:** | | | | | | |
| Interest-bearing checking deposits | $ **136,634** | $ **91** | **0.27%** | $ 140,787 | $ 37 | 0.11% |
| Money market savings | **365,947** | **3,685** | **4.08** | 284,009 | 2,110 | 3.01 |
| Regular savings | **198,145** | **717** | **1.47** | 196,136 | 202 | 0.42 |
| Certificates of deposit | **515,957** | **5,705** | **4.48** | 485,671 | 4,181 | 3.49 |
| Time open & club accounts | **17,164** | **197** | **4.65** | 19,272 | 167 | 3.51 |
| Total time and interest-bearing deposits | **1,233,847** | **10,395** | **3.42** | 1,125,875 | 6,697 | 2.41 |
| Federal funds purchased | **16,297** | **218** | **5.42** | 559 | 6 | 4.35 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Securities sold under agreements to repurchase | **91,450** | **537** | **2.38** | 98,624 | 506 | 2.08 |
| Short-term borrowings | **17,794** | **239** | **5.45** | 17,176 | 195 | 4.60 |
| Long-term debt | **76,883** | **884** | **4.66** | 56,525 | 606 | 4.35 |
| Subordinated notes and capital securities | **29,998** | **582** | **7.87** | 31,502 | 550 | 7.08 |
| Total borrowings | **232,422** | **2,460** | **4.29** | 204,386 | 1,863 | 3.70 |
| Total interest-bearing liabilities | **1,466,269** | **12,855** | **3.56** | 1,330,261 | 8,560 | 2.61 |
| Demand deposits, non-interest bearing | **218,933** | | | 228,003 | | |
| Accrued expenses & other liabilities | **29,306** | | | 23,841 | | |
| Total liabilities | **1,714,508** | | | 1,582,105 | | |
| **Shareholders' Equity:** | | | | | | |
| Common stock | **74,370** | | | 74,370 | | |
| Additional paid-in capital | **22,485** | | | 22,053 | | |
| Retained earnings and other equity | **90,595** | | | 78,121 | | |
| Total shareholders' equity | **187,450** | | | 174,544 | | |
| Total liabilities and shareholders' equity | **$ 1,901,958** | | | $ 1,756,649 | | |
| | | | | | | |
| Net interest income | | **$ 16,405** | | | $ 15,870 | |
| Net interest spread | | | **3.24** | | | 3.56 |
| Effect of net interest-free funding sources | | | **0.57** | | | 0.45 |
| Net interest margin | | | **3.81%** | | | 4.01% |
| Ratio of average interest-earning assets to average interest-bearing liabilities | **119.04%** | | | 120.64% | | |

Notes: Tax-equivalent amounts have been calculated using the Corporation's federal applicable rate of 35 percent.
For rate calculation purposes, average loan categories include unearned discount.
Nonaccrual loans have been included in the average loan balances.
Certain amounts have been reclassified to conform to the current-year presentation.

**Analysis of Changes in Net Interest Income**

The rate-volume variance analysis set forth in the table below compares changes in tax-equivalent net interest for the periods indicated by their rate and volume components. The change in interest income/expense due to both volume and rate has been allocated to change in volume.

| | The Three Months Ended March 31, 2007 Versus 2006 | | |
|---|---|---|---|
| | Volume Change | Rate Change | Total |
| Interest income: | | | |
| Interest-bearing deposits with other banks | $ | $ 1 | $ 1 |
| U.S. Government obligations | (322) | 376 | 54 |
| Obligations of states & political subdivisions | (30) | 2 | (28) |
| Other securities | 1,030 | | |