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COMMERCE BANCORP INC /NJ/
Form 10-Q
May 10, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 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, 2004

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 #0-12069

COMMERCE BANCORP
[GRAPHIC OMITTED]

(Exact name of registrant as specified in its charter)

New Jersey

22-2433468

(State or other jurisdiction of
incorporation or organization)

(IRS Employer Identification
Number)

Commerce Atrium, 1701 Route 70 East, Cherry Hill, New Jersey 08034-5400

(Address of Principal Executive Offices) (Zip Code)

(856) 751-9000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such report(s), and (2) has been subject to such filing requirements for the past 90 days.

Yes X

No ___

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes X

No ___

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Common Stock

77,915,974

(Title of Class)

(No. of Shares Outstanding
as of May 3, 2004)

COMMERCE BANCORP, INC. AND SUBSIDIARIES
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COMMERCE BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(unaudited)

March 31,

(dollars in thousands) 2004

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Assets	Cash and due from banks	\$ 971,897
	Federal funds sold	56,000

	Cash and cash equivalents	1,027,897
	Loans held for sale	34,934
	Trading securities	234,359
	Securities available for sale	11,972,943
	Securities held to maturity	2,871,593
	(market value 03/04-\$2,884,803; 12/03-\$2,467,192)	
	Loans	7,788,139
	Less allowance for loan losses	117,329

		7,670,810
	Bank premises and equipment, net	856,634
	Other assets	286,081

		\$ 24,955,251
		=====
Liabilities	Deposits:	
	Demand:	
	Noninterest-bearing	\$ 5,092,813
	Interest-bearing	9,313,838
	Savings	4,995,245
	Time	3,480,782

	Total deposits	22,882,678
	Other borrowed money	137,978
	Other liabilities	282,039
	Long-term debt	200,000

		23,502,695
Stockholders' Equity	Common stock, 78,120,321 shares issued (76,869,415 shares in 2003)	78,120
	Capital in excess of par value	912,905
	Retained earnings	394,794
	Accumulated other comprehensive income (loss)	78,076

		1,463,895
	Less treasury stock, at cost, 397,859 shares issued (363,076 shares in 2003)	11,339

	Total stockholders' equity	1,452,556

		\$ 24,955,251
		=====

See accompanying notes.

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COMMERCE BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

		Three Month March 31
		2004
		(dollars in thousands, except per share amounts)
Interest income	Interest and fees on loans	\$ 108,213
	Interest on investments	163,499
	Other interest	340
	Total interest income	272,052
Interest expense	Interest on deposits:	
	Demand	15,943
	Savings	7,786
	Time	14,643
	Total interest on deposits	38,372
	Interest on other borrowed money	448
	Interest on long-term debt	3,020
	Total interest expense	41,840
	Net interest income	230,212
	Provision for loan losses	9,500
	Net interest income after provision for loan losses	220,712
Noninterest income	Deposit charges and service fees	45,481
	Other operating income	40,327
	Net investment securities gains (losses)	424
	Total noninterest income	86,232
Noninterest expense	Salaries and benefits	97,340
	Occupancy	28,110
	Furniture and equipment	24,179
	Office	10,920
	Marketing	8,696
	Other	43,005
	Total noninterest expenses	212,250
	Income before income taxes	94,694
	Provision for federal and state income taxes	32,719
	Net income	\$61,975
	Net income per common and common equivalent share:	
	Basic	\$ 0.80

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Diluted	\$ 0.75
Average common and common equivalent shares outstanding:	
Basic	77,164
Diluted	85,532
Cash dividends, common stock	\$ 0.19

See accompanying notes.

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COMMERCE BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	(dollars in thousands)	20
Operating activities	Net income	\$ 61,
	Adjustments to reconcile net income to net cash provided by operating activities:	
	Provision for loan losses	9,
	Provision for depreciation, amortization and accretion	27,
	(Gain) loss on sales of securities available for sale	(
	Proceeds from sales of loans held for sale	146,
	Originations of loans held for sale	(152,
	Net (increase) decrease in trading securities	(63,
	Increase in other assets, net	(25,
	Increase (decrease) in other liabilities	62,
	Net cash provided by operating activities	65,
Investing activities	Proceeds from the sales of securities available for sale	1,561,
	Proceeds from the maturity of securities available for sale	758,
	Proceeds from the maturity of securities held to maturity	167,
	Purchase of securities available for sale	(3,519,
	Purchase of securities held to maturity	(548,
	Net increase in loans	(383,
	Proceeds from sales of loans	45,
	Capital expenditures	(65,
	Net cash used by investing activities	(1,984,
Financing activities	Net increase in demand and savings deposits	2,030,
	Net increase in time deposits	150,
	Net decrease in other borrowed money	(173,
	Dividends paid	(14,5
	Proceeds from issuance of common stock under dividend reinvestment and other stock plans	45,
	Other	(1,

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Net cash provided by financing activities	2,036,
Increase in cash and cash equivalents	117,
Cash and cash equivalents at beginning of year	910,
<hr/>	
Cash and cash equivalents at end of period	\$ 1,027,
<hr/>	

Supplemental disclosures of cash flow information: Cash paid during the period for:

Interest	\$ 40,
Income taxes	5,

See accompanying notes.

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COMMERCE BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(unaudited)

Three months ended March 31, 2004
(in thousands)

	Common Stock	Capital in Excess of Par or Stated Value	Retained Earnings	Treasu Stoc
Balances at December 31, 2003	\$76,869	\$866,095	\$347,365	\$ (9,3
Net income			61,975	
Other comprehensive income, net of tax				
Unrealized gain on securities (pre-tax \$96,281)				
Reclassification adjustment (pre-tax \$32,786)				
Other comprehensive income				
Total comprehensive income				
Cash dividends paid			(14,547)	
Shares issued under dividend reinvestment				
and compensation and benefit plans (1,251 shares)	1,251	44,010		
Other		2,800	1	(2,0
<hr/>				
Balances at March 31, 2004	\$78,120	\$912,905	\$394,794	\$ (11,3
<hr/>				

See accompanying notes.

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COMMERCE BANCORP, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

A. Consolidated Financial Statements

The consolidated financial statements included herein have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations. These consolidated financial statements were compiled in accordance with the accounting policies set forth in note 1 (Significant Accounting Policies) of the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003. The accompanying consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary to reflect a fair statement of the results for the interim periods presented. Such adjustments are of a normal recurring nature.

These consolidated financial statements should be read in conjunction with the audited financial statements and the notes thereto included in the registrant's Annual Report on Form 10-K for the year ended December 31, 2003. The results for the three months ended March 31, 2004 are not necessarily indicative of the results that may be expected for the year ended December 31, 2004.

The consolidated financial statements include the accounts of Commerce Bancorp, Inc. and its consolidated subsidiaries. All material intercompany transactions have been eliminated. Certain amounts from prior years have been reclassified to conform with 2004 presentation.

B. Long Term Debt

On April 1, 2004, the Company's \$200.0 million of 5.95% Convertible Trust Capital Securities, recorded on the consolidated balance sheet as long term debt, became convertible at the option of the holder. The holders of the Convertible Trust Capital Securities may convert each security into 0.9478 shares of Company common stock. The Company has calculated the effect of these securities on diluted net income per share by using the if-converted method. Under the if-converted method, the related interest charges on the Convertible Trust Capital Securities, adjusted for income taxes, have been added back to the numerator and the common shares to be issued upon conversion have been added to the denominator.

The Convertible Trust Capital Securities were issued on March 11, 2002 through Commerce Capital Trust II, a Delaware business trust. The Convertible Trust Capital Securities mature in 2032. The net proceeds of this offering were used for general corporate purposes, including the redemption of the Company's \$57.5 million of 8.75% Trust Capital Securities on July 1, 2002 and the repayment of the Company's \$23.0 million of 8 3/8% subordinated notes on May 20, 2002.

C. Bank Premises and Equipment

In accordance with accounting principles generally accepted in the United States, when capitalizing costs for branch construction, the Company includes the costs of purchasing the land, developing the site, constructing the building (or leasehold improvements if the property is leased), and furniture, fixtures and equipment necessary to equip the branch. All other pre-opening and post-opening costs related to branches are expensed as incurred. As of March 31, 2004 and December 31, 2003, Bank premises and equipment in progress was \$96.9 million and \$87.2 million, respectively.

D. Commitments

In the normal course of business, there are various outstanding commitments to extend credit, such as letters of credit and unadvanced loan commitments. Management does not anticipate any material losses as a result of these transactions.

E. Comprehensive Income

Total comprehensive income, which for the Company included net income and changes in unrealized gains and losses on the Company's available for sale securities, amounted to \$143.8 million and \$22.5 million, respectively, for the three months ended March 31, 2004 and 2003.

F. New Accounting Standards

In January 2003, the FASB issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). In December 2003, the FASB deferred the implementation date of FIN 46 to periods ending after March 15, 2004 for all variable interest entities with the exception of special-purpose entities, which were subject to adoption in periods ending after December 15, 2003. This interpretation provides guidance on how to identify a variable interest entity (VIE) and determine when the assets, liabilities, noncontrolling interests, and results of operations of a VIE need to be included in a company's consolidated financial statements. The adoption of FIN 46 did not have a material impact on the Company's financial condition or operating results.

The Company makes investments directly in low-income housing tax credit (LIHTC) operating partnerships, private venture capital funds and Small Business Investment Companies (SBIC). The Company has determined these entities do not meet the consolidation criteria of FIN 46. At March 31, 2004, the Company's investment in these entities totaled \$38.8 million.

G. Stock-Based Compensation

The Company follows APB Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations to account for its stock-based compensation plans. If the Company had accounted for stock options under the fair value provisions of FAS 123, "Accounting for Stock-Based Compensation", net income and net income per share would have been as follows (in thousands, except per share amounts):

	Three Months Ended March 31,	
	2004	2003
Reported net income	\$61,975	\$42,890
Less: Stock option compensation expense		

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determined under fair value method, net of tax	(3,420)	(2,380)
	-----	-----
Pro forma net income, basic	\$58,555	\$40,510
Add: Interest expense on Convertible Trust Capital Securities, net of tax	1,963	

Pro forma net income, diluted	\$60,518	\$40,510
Reported net income per share:		
Basic	\$ 0.80	\$ 0.63
Diluted	0.75	0.60
Pro forma net income per share:		
Basic	\$ 0.76	\$ 0.59
Diluted	0.71	0.57

The fair value of options granted in 2004 and 2003 was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions: risk-free interest rates of 3.09% to 3.00%, dividend yields of 1.33% to 1.50%, volatility factors of the expected market price of the Company's common stock of .255 to .304 and weighted average expected lives of the options of 5.27 and 5.22 years.

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The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its stock options.

H. Segment Information

The Company operates one reportable segment of business, Community Banks, which includes all of the Company's banking subsidiaries. Through its Community Banks, the Company provides a broad range of retail and commercial banking services, and corporate trust services. Parent/Other includes the holding company, Commerce Insurance Services, Inc. and Commerce Capital Markets, Inc.

Selected segment information is as follows (in thousands):

	Three Months Ended March 31, 2004			Three Months Ended March 31, 2003	
	Community Banks	Parent/ Other	Total	Community Banks	Parent/ Other
Net interest income	\$ 231,836	\$ (1,624)	\$ 230,212	\$ 168,229	\$ 168,229

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Provision for loan losses	9,500	-	9,500	6,900
Net interest income after provision	222,336	(1,624)	220,712	161,329
Noninterest income	58,133	28,099	86,232	49,995
Noninterest expense	189,353	22,897	212,250	149,450
Income before income taxes	91,116	3,578	94,694	61,874
Income tax expense	31,207	1,512	32,719	20,975
Net income	\$ 59,909	\$ 2,066	\$ 61,975	\$ 40,899
Average assets (in millions)	\$ 21,416	\$ 2,076	\$ 23,492	\$ 14,993

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I. Net income Per Share

The calculation of net income per share follows (in thousands, except for per share amounts):

	Three Months Ended March 31,	
	2004	2003
Basic:		
Net income available to common shareholders - basic	\$61,975	\$42,899
Average common shares outstanding	77,164	68,993
Net income per common share - basic	\$ 0.80	\$ 0.62
Diluted:		
Net income	\$61,975	\$42,899
Add interest expense on Convertible Trust Capital Securities, net of tax	1,963	
Net income available to common shareholders - diluted	\$63,938	\$42,899
Average common shares outstanding	77,164	68,993

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Additional shares considered in diluted computation assuming:		
Exercise of stock options	4,577	3
Conversion of Convertible Trust Capital Securities	3,791	
	-----	-----
Average common shares outstanding - diluted	85,532	71
	=====	=====
Net income per common share - diluted	\$ 0.75	\$
	=====	=====

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

Results of Operation

Executive Summary

During the first quarter of 2004, the Company experienced strong deposit growth and positive operating leverage as year over year revenue growth of 30% exceeded non-interest expense growth of 23%. Total assets grew to \$25.0 billion, an increase of 40% over March 31, 2003, while total deposits grew 41%. Net income increased 44% to \$62.0 million and diluted net income per share increased 25% to \$.75 during the first quarter of 2004 as compared to the first quarter of 2003. The net income per share calculation for the first quarter of 2004 includes 5.0 million shares issued in connection with the Company's September 2003 secondary offering and an additional 3.8 million shares assuming the conversion of the Company's Convertible Trust Capital Securities, neither of which were included in the calculation for the first quarter of 2003.

The Company has identified two critical accounting policies: the policies related to the allowance for loan losses and capitalization of branch costs. The foregoing critical accounting policies are more fully described in the Company's annual report on Form 10-K for the year ended December 31, 2003. During the current quarter, there were no material changes to the estimates or methods by which estimates are derived with regard to the critical accounting policies.

Capital Resources

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At March 31, 2004, stockholders' equity totaled \$1.5 billion or 5.82% of total assets, compared to \$1.3 billion or 5.62% of total assets at December 31, 2003.

The Company and its subsidiaries are subject to risk-based capital standards issued by bank regulatory authorities. Under these standards, Tier 1 capital includes stockholders' equity, as adjusted for certain items. The Company makes two significant adjustments in calculating regulatory capital. The first adjustment is to exclude from capital the unrealized appreciation or depreciation in its available for sale securities portfolio. The second adjustment is to add to capital the Convertible Trust Capital Securities. Total capital is comprised of all the components of Tier 1 capital plus the allowance for loan losses.

The table below presents the Commerce Bancorp and Commerce N.A.'s risk-based and leverage ratios at March 31, 2004 and 2003:

	Actual		Per Regulatory Guide		"We Amo
	Amount	Ratio	Amount	Ratio	
March 31, 2004:					

Commerce Bancorp					
Risk based capital ratios:					
Tier 1	\$1,564,769	12.70%	\$493,027	4.00%	\$7
Total capital	1,682,098	13.65	986,053	8.00	1,2
Leverage ratio	1,564,769	6.68	937,630	4.00	1,1
Commerce N.A.					
Risk based capital ratios:					
Tier 1	\$808,896	10.73%	\$301,573	4.00%	\$4
Total capital	887,959	11.78	603,146	8.00	7
Leverage ratio	808,896	6.03	536,607	4.00	6

	Actual		Per Regulatory Guide		"We Amo
	Amount	Ratio	Amount	Ratio	

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March 31, 2003:

Commerce Bancorp

Risk based capital ratios:

Tier 1	\$1,050,051	11.25%	\$373,411	4.00%	\$5
Total capital	1,144,782	12.26	746,823	8.00	9
Leverage ratio	1,050,051	6.28	668,655	4.00	8

Commerce N.A.

Risk based capital ratios:

Tier 1	\$567,037	9.83%	\$230,644	4.00%	\$3
Total capital	630,037	10.93	461,288	8.00	5
Leverage ratio	567,037	5.53	410,116	4.00	5

At March 31, 2004, the Company's consolidated capital levels and each of the Company's bank subsidiaries met the regulatory definition of a "well capitalized" financial institution, i.e., a leverage capital ratio exceeding 5%, a Tier 1 risk-based capital ratio exceeding 6%, and a total risk-based capital ratio exceeding 10%. Management believes that as of March 31, 2004, the Company and its subsidiaries meet all capital adequacy requirements to which they are subject. As a result of the issuance of FIN 46, the Federal Reserve Board is evaluating whether deconsolidation of Commerce Capital Trust II will affect the qualification of the Convertible Trust Capital Securities as Tier 1 capital. On May 6, 2004 the Federal Reserve Board issued a proposed ruling that would retain trust preferred securities in the Tier 1 capital of bank holding companies, subject to certain limitations. Based on the proposed ruling, the Convertible Trust Capital Securities will retain the qualification as Tier 1 capital. If it is determined that the Convertible Trust Capital Securities no longer qualify as Tier 1 capital, the Company will remain "well capitalized."

Deposits

Total deposits at March 31, 2004 were \$22.9 billion, up \$6.7 billion, or 41.4% over total deposits of \$16.2 billion at March 31, 2003, and up by \$2.2 billion, or 10.6% from year-end 2003. Deposit growth during the first three months of 2004 included core deposit growth in all categories as well as growth from the public sector. Same-store core deposit growth is measured as the year over year percentage increase in core deposits for branches open two years or more at the balance sheet date. The Company experienced same-store core deposit growth of 24% at March 31, 2004.

Interest Rate Sensitivity and Liquidity

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

Management considers the simulation of net interest income in different interest rate environments to be the best indicator of the Company's interest rate risk. Income simulation analysis captures not only the potential of all assets and liabilities to mature or reprice, but also the probability that they will do so. Income simulation also attends to the relative interest rate sensitivities of

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these items, and projects their behavior over an extended period of time. Finally, income simulation permits management to assess the probable effects on the balance sheet not only of changes in interest rates, but also of proposed strategies for responding to them.

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The Company's income simulation model analyzes interest rate sensitivity by projecting net income over the next 24 months in a flat rate scenario versus net income in alternative interest rate scenarios. Management continually reviews and refines its interest rate risk management process in response to the changing economic climate. Currently, the Company's model projects a proportionate plus 200 and minus 100 basis point change during the next year, with rates remaining constant in the second year. The Company's ALCO policy has established that interest income sensitivity will be considered acceptable if net income in the above interest rate scenario is within 10% of net income in the flat rate scenario in the first year and within 15% over the two year time frame. Net income in the flat rate scenario is projected to increase by approximately 25% per year. The following table illustrates the impact on projected net income at March 31, 2004 and 2003 of a plus 200 and minus 100 basis point change in interest rates.

	Basis Point Change	
	Plus 200	Minus 100
March 31, 2004:		
Twelve Months	0.98%	(7.81)%
Twenty Four Months	10.22%	(7.15)%
March 31, 2003:		
Twelve Months	7.78%	(2.35)%
Twenty Four Months	13.83%	(4.65)%

All of these net income projections are within an acceptable level of interest rate risk pursuant to the policy established by ALCO.

In the event the Company's interest rate risk models indicate an unacceptable level of risk, the Company could undertake a number of actions that would reduce this risk, including the sale of a portion of its available for sale portfolio, the use of risk management strategies such as interest rate swaps and caps, or the extension of the maturities of its short-term borrowings.

Management also monitors interest rate risk by utilizing a market value of equity model (MVE). The model assesses the impact of a change in interest rates on the market value of all the Company's assets and liabilities, as well as any off balance sheet items. The model calculates the market value of the Company's assets and liabilities in excess of book value in the current rate scenario, and then compares the excess of market value over book value given an immediate plus 200 and minus 100 basis point change in rates. The Company's ALCO policy indicates that the level of interest rate risk is unacceptable if the immediate plus 200 and minus 100 basis point change would result in the loss of 45% or more of the excess of market value over book value in the current rate scenario. At March 31, 2004, the market value of equity model indicates an acceptable

level of interest rate risk.

The MVE reflects certain estimates and assumptions regarding the impact on the market value of the Company's assets and liabilities given an immediate plus 200 or minus 100 basis point change in interest rates. One of the key assumptions is the market value assigned to the Company's core deposits, or the core deposit premium. Utilizing an independent consultant, the Company has completed and updated comprehensive core deposit studies in order to assign its own core deposit premiums as permitted by the Company's regulatory authorities. The studies have consistently confirmed management's assertion that the Company's core deposits have stable balances over long periods of time, are generally insensitive to changes in interest rates and have significantly longer average lives and durations than the Company's loans and investment securities. At March 31, 2004, the average life of the Company's deposits was 13.5 years. Thus, these core deposit balances provide an internal hedge to market value fluctuations in the Company's fixed rate assets.

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The MVE analyzes both sides of the balance sheet and, as indicated below, demonstrates the inherent value of the Company's core deposits in a rising rate environment. As rates rise, the value of the Company's core deposits increases which offsets the decrease in value of the Company's fixed rate assets. The following table summarizes the market value of equity at March 31, 2004 (in millions, except for per share amounts):

	Market Value Of Equity	Per Share
Plus 200 basis point	\$4,934	\$63.17
Current Rate	\$4,918	\$62.96
Minus 100 basis point	\$3,890	\$49.80

Liquidity involves the Company's ability to raise funds to support asset growth or decrease assets to meet deposit withdrawals and other borrowing needs, to maintain reserve requirements and to otherwise operate the Company on an ongoing basis. The Company's liquidity needs are primarily met by growth in core deposits, its cash and federal funds sold position, cash flow from its amortizing investment and loan portfolios, as well as the use of short-term borrowings, as required. If necessary, the Company has the ability to raise liquidity through collateralized borrowings, FHLB advances, or the sale of its available for sale investment portfolio. As of March 31, 2004 the Company had in excess of \$11.5 billion in immediately available liquidity which includes securities that could be sold or used for collateralized borrowings, cash on hand, and borrowing capacities under existing lines of credit. During the first three months of 2004, deposit growth was used to fund growth in the loan portfolio and purchase additional investment securities.

Short-Term Borrowings

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Short-term borrowings, or other borrowed money, consist primarily of securities sold under agreements to repurchase and overnight lines of credit, and are used to meet short term funding needs. During the first three months of 2004, the Company reduced its short-term borrowings, primarily through increased deposits. At March 31, 2004, short-term borrowings aggregated \$138.0 million and had an average rate of 0.76%, as compared to \$311.5 million at an average rate of 0.77% at December 31, 2003.

Interest Earning Assets

The Company's cash flow from deposit growth and repayments from its investment portfolio totaled approximately \$3.1 billion for the first three months of 2004. This significant cash flow provides the Company with ongoing reinvestment opportunities as interest rates change. For the three month period ended March 31, 2004, interest earning assets increased \$2.2 billion from \$20.8 billion to \$23.0 billion. This increase was primarily in investment securities and the loan portfolio as described below.

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Loans

During the first three months of 2004, loans increased \$347.6 million from \$7.4 billion to \$7.8 billion. All segments of the loan portfolio experienced growth in the first three months of 2004, including loans secured by commercial real estate properties, commercial loans, and consumer loans.

The following table summarizes the loan portfolio of the Company by type of loan as of the dates shown.

	March 31,	December 31,
	2004	2003
	(in thousands)	
Commercial:		
Term	\$1,071,736	\$ 1,027,526
Line of credit	960,080	959,158
Demand	1,080	1,077
	-----	-----
	2,032,896	1,987,761
Owner-occupied	1,710,098	1,619,079
	-----	-----
	3,742,994	3,606,840
Consumer:		
Mortgages (1-4 family residential)	984,415	918,686
Installment	135,406	138,437
Home equity	1,485,055	1,405,795
Credit lines	59,081	60,579

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	2,663,957	2,523,497
Real estate:		
Investor developer	1,236,862	1,167,672
Construction	144,326	142,567
	1,381,188	1,310,239
Total loans	\$7,788,139	\$ 7,440,576

Investments

In total, for the first three months of 2004, securities increased \$1.8 billion from \$13.3 billion to \$15.1 billion. The available for sale portfolio increased \$1.3 billion to \$12.0 billion at March 31, 2004 from \$10.7 billion at December 31, 2003, and the securities held to maturity portfolio increased \$381.1 million to \$2.9 billion at March 31, 2004 from \$2.5 billion at year-end 2003. The portfolio of trading securities increased \$63.9 million from year-end 2003 to \$234.4 million at March 31, 2004.

The portfolio is comprised primarily of high quality US Government agency and mortgage-backed obligations. During the first quarter of 2004, the Company continued its ongoing review and repositioning of the portfolio to adjust for current and anticipated interest rate and yield curve levels. This repositioning of the portfolio involved sales of approximately \$1.6 billion for the first quarter. This repositioning helped reduce the duration of the total portfolio to 2.74 years at March 31, 2004 from 3.93 years at December 31, 2003. The duration of the available for sale portfolio was reduced to 2.55 years at March 31, 2004 from 3.78 years at December 31, 2003. The yield on the total portfolio decreased slightly from 4.86% at December 31, 2003 to 4.81% at March 31, 2004.

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The following table summarizes the book value of securities available for sale and securities held to maturity by the Company as of the dates shown.

	March 31, 2004	December 31, 2003
	(dollars in thousands)	
U.S. Government agency and mortgage backed obligations	\$11,736,718	\$10,511,545
Obligations of state and political subdivisions	33,415	30,927
Other	202,810	108,183
Securities available for sale	\$11,972,943	\$10,650,655
U.S. Government agency and mortgage backed obligations	\$2,545,263	\$2,193,577
Obligations of state and political subdivisions	252,081	227,199

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Other	74,249	69,708
	-----	-----
Securities held to maturity	\$2,871,593	\$2,490,484
	=====	=====

Detailed below is information regarding the composition and characteristics of the Company's investment portfolio, excluding trading securities, as of March 31, 2004.

Product Description	Amount	Average Yield	Average Book Price	Average Duration
	(in millions)			(i)
Mortgage-backed Securities:				
Federal Agencies Pass Through Certificates (AAA Rated)	\$ 4,412	5.04%	\$101.2	2.87
Collateralized Mortgage Obligations (AAA Rated)	9,161	4.80	101.0	2.46
U.S. Government agencies/Other	1,271	4.00	99.6	4.57
	-----	-----	-----	-----
Total	\$ 14,844	4.81%	\$101.0	2.74
	=====	=====	=====	=====

The Company's mortgage-backed securities (MBS) portfolio comprises 91% of the total investment portfolio. The MBS portfolio consists of Federal Agencies Pass-Through Certificates and Collateralized Mortgage Obligations (CMO's) which are issued by federal agencies and other private sponsors. The Company's investment policy does not permit investments in inverse floaters, IO's, PO's and other similar issues.

Net Income

Net income for the first quarter of 2004 was \$62.0 million, an increase of \$19.1 million or 44.5% over the \$42.9 million recorded for the first quarter of 2003. On a per share basis, diluted net income for the first quarter of 2004 was \$0.75 per common share compared to \$0.60 per common share for the first quarter of 2003. Net income per share in the first quarter of 2004 reflects the addition of 5.0 million shares from the secondary offering in September 2003 and 3.8 million shares assuming conversion of the Convertible Trust Capital Securities.

Return on average assets (ROA) and return on average equity (ROE) for the first quarter of 2004 were 1.06% and 17.91%, respectively, compared to 1.02% and 17.94%, respectively, for the same 2003 period.

Net Interest Income

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Net interest income totaled \$230.2 million for the first quarter of 2004, an increase of \$62.9 million or 37.6% from \$167.3 million in the first quarter of 2003. The increase in net interest income was due primarily to the Company's continued ability to grow deposits and its loan and investment portfolios.

As shown below, the increase in net interest income on a tax equivalent basis was due to volume increases in the Company's earning assets, which were fueled by the Company's continued growth of low-cost core deposits (in millions).

Quarter Ended March 31	Net Interest Income		
	Volume Increase	Rate Change	Total Increase
2004 vs. 2003	\$69.7	(\$6.4)	\$ 63.3

The net interest margin for the first quarter of 2004 was 4.39%, down 20 basis points from the margin for the first quarter of 2003 and up 12 basis points from the margin for the fourth quarter of 2003. The increase in the net interest margin over the fourth quarter of 2003 was due primarily to an increase in the yield on interest earning assets of 10 basis points.

The following table sets forth balance sheet items on a daily average basis for the three months ended March 31, 2004, December 31, 2003 and March 31, 2003 and presents the daily average interest earned on assets and paid on liabilities for such periods.

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Average Balances and Net Interest Income

(dollars in thousands)	March 2004			December 2003		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Earning Assets						
Investment securities						
Taxable	\$13,295,903	\$ 159,648	4.83%	\$12,743,163	\$148,537	4.62%
Tax-exempt	256,628	3,860	6.05	242,901	3,829	6.25
Trading	161,701	2,065	5.14	190,658	1,917	3.99

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Total investment securities	13,714,232	165,573	4.86	13,176,722	154,283	4.65
Federal funds sold	144,297	340	0.95	20,435	50	0.97
Loans						
Commercial mortgages	2,793,159	42,782	6.16	2,655,510	41,172	6.15
Commercial	1,878,353	24,535	5.25	1,760,615	23,285	5.25
Consumer	2,603,037	36,936	5.71	2,444,764	35,773	5.81
Tax-exempt	337,313	6,092	7.26	283,291	5,497	7.70
	-----	-----	-----	-----	-----	-----
Total loans	7,611,862	110,345	5.83	7,144,180	105,727	5.87
	-----	-----	-----	-----	-----	-----
Total earning assets	\$21,470,391	\$ 276,258	5.17%	\$20,341,337	\$260,060	5.07%
	=====	=====	=====	=====	=====	=====
Sources of Funds						

Interest-bearing liabilities						
Regular savings	\$4,492,847	\$ 7,786	0.70%	\$4,251,627	\$ 7,597	0.71%
N.O.W. accounts	607,603	1,052	0.70	546,350	937	0.68
Money market plus	8,378,467	14,891	0.71	7,684,235	13,326	0.69
Time deposits	2,430,589	11,323	1.87	2,403,680	12,049	1.99
Public funds	968,513	3,320	1.38	923,561	3,151	1.35
	-----	-----	-----	-----	-----	-----
Total deposits	16,878,019	38,372	0.91	15,809,453	37,060	0.93
Other borrowed money	174,746	448	1.03	411,079	921	0.89
Long-term debt	200,000	3,020	6.07	200,000	3,020	5.99
	-----	-----	-----	-----	-----	-----
Total deposits and interest-bearing liabilities	17,252,765	41,840	0.98	16,420,532	41,001	0.99
Noninterest-bearing funds (net)	4,217,626			3,920,805		
	-----	-----	-----	-----	-----	-----
Total sources to fund earning assets	\$21,470,391	41,840	0.78	\$20,341,337	41,001	0.80
	=====	-----	-----	=====	-----	-----
Net interest income and margin tax-equivalent basis		\$234,418	4.39%		\$219,059	4.27%
		=====	=====		=====	=====
Other Balances						

Cash and due from banks	\$1,007,182			\$ 905,464		
Other assets	1,129,880			1,101,329		
Total assets	23,491,544			22,241,356		
Total deposits	21,478,730			20,171,403		
Demand deposits (noninterest-bearing)	4,600,711			4,361,950		
Other liabilities	253,890			232,037		
Stockholders' equity	1,384,178			1,226,837		

Notes

- Weighted average yields on tax-exempt obligations have been computed on a tax-equivalent basis assuming a federal tax rate of 35%.
- Non-accrual loans have been included in the average loan balance
- Investment securities includes investments available for sale.
- Consumer loans include mortgage loans held for sale.

Noninterest Income

Noninterest income totaled \$86.2 million for the first quarter of 2004, an increase of \$10.1 million or 13.3% from \$76.1 million in the first quarter of 2003. The increase was primarily due to increased deposit charges and service fees, which rose \$10.6 million over the first quarter of 2003 primarily due to higher transaction volumes. The decrease in loan brokerage fees of \$4.9 million resulted from a decline in mortgage refinancing activity.

(dollars in thousands)	Three Months Ended	
	March 31, 2004	March 31, 2003
Deposit charges & service fees	\$45,481	\$34,842
Other operating income:		
Insurance	18,336	16,055
Capital markets	9,727	10,003
Loan brokerage fees	3,053	7,923
Other	9,211	7,379
Total other	40,327	41,360
Net investment securities gains/(losses)	424	(136)
Total non-interest income	\$86,232	\$76,066

Noninterest Expense

For the first quarter of 2004, noninterest expense totaled \$212.3 million, an increase of \$40.1 million or 23.3% over the same period in 2003. Contributing to this increase was new branch activity over the past twelve months, with the number of branches increasing from 226 at March 31, 2003 to 278 at March 31, 2004. With the addition of these new offices, staff, facilities, and related expenses rose accordingly. Other noninterest expenses rose \$9.1 million over the first quarter of 2003. This increase resulted primarily from higher bank card-related service charges, increased business development expenses, and increased provisions for non-credit-related losses.

The Company experienced positive operating leverage in the first quarter, as year over year revenue growth of 30% exceeded non-interest expense growth of 23%. Non-interest expense growth during the first quarter of 2004 was 3% compared to the fourth quarter of 2003. One important factor influencing the growth in non-interest expenses is that the Company absorbed significant start-up expenses related to the New York City and Long Island markets in prior years. As a result, the impact of growth in non-interest expenses in these markets is expected to decline throughout 2004.

The Company's operating efficiency ratio (noninterest expenses, less other real estate expense, divided by net interest income plus noninterest income excluding non-recurring gains) was 67.12% for the first three months of 2004 as compared to 70.58% for the same 2003 period. The Company's efficiency ratio remains above its peer group primarily due to its aggressive growth expansion activities.

Loan and Asset Quality

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 Total non-performing assets (non-performing loans and other real estate, excluding loans past due 90 days or more and still accruing interest) at March 31, 2004 were \$32.4 million, or 0.13% of total assets compared to \$23.6 million or 0.10% of total assets at December 31, 2003 and \$22.5 million or 0.13% of total assets at March 31, 2003.

Total non-performing loans (non-accrual loans and restructured loans, excluding loans past due 90 days or more and still accruing interest) at March 31, 2004 were \$30.5 million or 0.39% of total loans compared to \$21.7 million or 0.29% of total loans at December 31, 2003 and \$19.0 million or 0.32% of total loans at March 31, 2003. At March 31, 2004, loans past due 90 days or more and still accruing interest amounted to \$696 thousand compared to \$538 thousand at December 31, 2003 and \$376 thousand at March 31, 2003. Additional loans considered as potential problem loans by the Company's internal loan review department (\$35.8 million at March 31, 2004) have been evaluated as to risk exposure in determining the adequacy of the allowance for loan losses.

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The following summary presents information regarding non-performing loans and assets as of March 31, 2004 and the preceding four quarters (dollar amounts in thousands).

	March 31, 2004	December 31, 2003	September 30, 2003	June 30, 2003
Non-accrual loans:				
Commercial	\$19,701	\$ 6,867	\$ 7,295	\$ 7,295
Consumer	9,984	9,242	8,295	9,242
Real estate:				
Construction		138		
Mortgage	810	5,494	7,502	5,494
Total non-accrual loans	30,495	21,741	23,092	22,736
Restructured loans:				
Commercial	1	1	2	1
Consumer				
Real estate:				
Construction				
Mortgage				
Total restructured loans	1	1	2	1
Total non-performing loans	30,496	21,742	23,094	22,737
Other real estate	1,890	1,831	1,670	1,670
Total non-performing assets	32,386	23,573	24,764	24,407

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Loans past due 90 days or more and still accruing	696	538	649	
Total non-performing assets and loans past due 90 days or more	\$33,082	\$24,111	\$25,413	\$24
Total non-performing loans as a percentage of total period-end loans	0.39%	0.29%	0.34%	0
Total non-performing assets as a percentage of total period-end assets	0.13%	0.10%	0.12%	0
Total non-performing assets and loans past due 90 days or more as a percentage of total period-end assets	0.13%	0.11%	0.12%	0
Allowance for loan losses as a percentage of total non-performing loans	385%	515%	449%	
Allowance for loan losses as a percentage of total period-end loans	1.51%	1.51%	1.52%	1
Total non-performing assets and loans past due 90 days or more as a percentage of stockholders' equity and allowance for loan losses	2%	2%	2%	

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The following table presents, for the periods indicated, an analysis of the allowance for loan losses and other related data: (dollar amounts in thousands)

	Three Months Ended	
	March 31, 2004	March 31, 2003
Balance at beginning of period	\$112,057	\$90,733
Provisions charged to operating expenses	9,500	6,900
	121,557	97,633
Recoveries on loans charged-off:		
Commercial	156	204
Consumer	270	131
Real estate	47	
Total recoveries	473	335

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Loans charged-off:		
Commercial	(2,293)	(1,868)
Consumer	(772)	(1,365)
Real estate	(1,636)	(4)
	-----	-----
Total charge-offs	(4,701)	(3,237)
	-----	-----
Net charge-offs	(4,228)	(2,902)
	-----	-----
 Balance at end of period	 \$117,329	 \$94,731
	=====	=====
 Net charge-offs as a percentage of average loans outstanding	 0.22%	 0.19%
 Net Reserve Additions	 \$ 5,272	 \$ 3,998

The Company considers the allowance for loan losses of \$117.3 million adequate to cover probable losses inherent in the loan portfolio at March 31, 2004. The Company's determination of the level of the allowance for loan losses rests upon various judgments and assumptions surrounding the risk characteristics included in the loan portfolio. Such risk characteristics include changes in levels and trends of charge-offs, delinquencies, and nonaccrual loans, trends in volume and terms of loans, changes in underwriting standards and practices, portfolio mix, tenure of loan officers and management, entrance into new geographic markets, changes in credit concentrations, and national and local economic trends and conditions, and other relevant factors, all of which may be susceptible to significant change.

Forward-Looking Statements

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

These forward-looking statements include statements with respect to the Company's beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties and are subject to change based on various factors (some of which are beyond the Company's control). The words "may", "could", "should", "would", "believe", "anticipate", "estimate", "expect", "intend", "plan" and similar expressions are intended to identify forward-looking statements. The following factors, among others, could cause the Company's financial performance to differ materially from that expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies, including interest rate policies of the Board of Governors of the Federal Reserve System (the "FRB"); inflation; interest rates, market and monetary fluctuations; the timely development of competitive new

products and services by the Company and the acceptance of such products and services by customers; the willingness of customers to substitute competitors' products and services for the Company's products and services and vice versa; the impact of changes in financial services' laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes; future acquisitions; the expense savings and revenue enhancements from acquisitions being less than expected; the growth and profitability of the Company's noninterest or fee income being less than expected; unanticipated regulatory or judicial proceedings; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

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

Item 3: Quantitative and Qualitative Disclosures About Market Risk

See Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operation, Interest Rate Sensitivity and Liquidity.

Item 4. Controls and Procedures

Quarterly evaluation of the Company's Disclosure Controls and Internal Controls. As of the end of the period covered by this quarterly report, the Company has evaluated the effectiveness of the design and operation of its "disclosure controls and procedures" ("Disclosure Controls"). This evaluation ("Controls Evaluation") was done under the supervision and with the participation of management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO").

Limitations on the Effectiveness of Controls. The Company's management, including the CEO and CFO, does not expect that its Disclosure Controls or its "internal controls and procedures for financial reporting" ("Internal Controls") will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. The Company

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conducts periodic evaluations of its internal controls to enhance, where necessary, its procedures and controls.

Conclusions. Based upon the Controls Evaluation, the CEO and CFO have concluded that, subject to the limitations noted above, the Disclosure Controls are effective in reaching a reasonable level of assurance that management is timely alerted to material information relating to the Company during the period when its periodic reports are being prepared.

In accordance with SEC requirements, the CEO and CFO note that, since the date of the Controls Evaluation to the date of this Quarterly Report, there have been no significant changes in Internal Controls or in other factors that could significantly affect Internal Controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

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PART II. OTHER INFORMATION

Item 2. Purchases of Certain Equity Securities by the Issuer and Others

Period	(a) Total Number of Shares Purchased (1)	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs
January 1 to January 31, 2004	34,783	\$57.50	
February 1 to February 29, 2004			
March 1 to March 31, 2004			
Total	34,783	\$57.50	

Item 6. Exhibits and Reports on Form 8-K

Exhibits

- Exhibit 3.1 Restated Certificate of Incorporation of the Company, as amended (incorporated by reference from the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002).
- Exhibit 3.2 By-laws of the Company, as amended (incorporated by reference from the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002).

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- Exhibit 31.1 Certification of the Company's Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- Exhibit 31.2 Certification of the Company's Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- Exhibit 32 Certification of the Company's Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Reports on Form 8-K

On January 15, 2004, we filed a Current Report on Form 8-K which included as exhibits a press release, issued by us on January 15, 2004, announcing our results for the fourth quarter of 2004 and certain supplemental information.

On March 3, 2004, we filed a Current Report on Form 8-K, which included certain questions and answers regarding corporate information.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMMERCE BANCORP, INC.

(Registrant)

May 10, 2004

(Date)

/s/ DOUGLAS J. PAULS

DOUGLAS J. PAULS
SENIOR VICE PRESIDENT AND
CHIEF FINANCIAL OFFICER
(PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER)

