

Popular Securities, Inc.
(a wholly-owned subsidiary of Popular, Inc.)
Unaudited Statement of Financial Condition
June 30, 2008

Popular Securities, Inc.
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Statement of Financial Condition
June 30, 2008

(dollars in thousands, except share data)

Assets

Cash	\$ 4,477
Securities purchased under agreements to resell	184,155
Securities owned, at fair value	
Pledged securities with creditors' rights to repledge	73,669
Other securities owned	37,555
Held in segregation	274
Receivables from broker-dealers and counterparties	15,064
Accrued interest receivable	813
Fixed assets, net of accumulated depreciation and amortization of \$2,209	1,624
Deferred tax asset, net	1,817
Goodwill	4,019
Other assets	5,692
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Total assets	\$ 329,159

Liabilities and Stockholder's Equity

Securities sold under agreements to repurchase	\$ 260,214
Payables to broker-dealers and counterparties	5,478
Accrued interest payable	215
Accounts payable to affiliates	279
Accrued employee compensation and benefits	3,652
Deferred compensation	2,280
Other liabilities	3,010
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Total liabilities	275,128
Commitments (Note 14)	
Stockholder's equity	
Capital stock, \$25 stated value; 10,000 shares authorized; 1,000 shares issued and outstanding	25
Treasury stock, at cost	(492)
Additional paid-in capital	15,713
Retained earnings	38,785
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Total stockholder's equity	54,031
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Total liabilities and stockholder's equity	\$ 329,159

The accompanying notes are an integral part of these financial statements.

Popular Securities, Inc.
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1. Nature of Business and Summary of Significant Accounting Policies

Popular Securities, Inc. (the "Company") is engaged in investment banking, brokerage and financial advisory services and is a member of the Financial Industry Regulatory Authority (FINRA). The Company operates principally in the Commonwealth of Puerto Rico and is a wholly-owned subsidiary of Popular, Inc.

The Company is a registered broker-dealer pursuant to section 15(b) of the Securities Exchange Act of 1934. In addition, the Company is licensed by the Office of the Commissioner of Financial Institutions of the Commonwealth of Puerto Rico as a registered broker-dealer and as an eligible similar institution under Regulation 5105.

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (GAAP) and industry practices. Following is a description of the more significant accounting policies followed by the Company:

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management believes that these estimates are adequate. Actual results could differ from those estimates.

Income Recognition

Securities owned transactions are recorded on the trade date, as if they had settled. Customers' securities transactions are recorded on a settlement-date basis with related commission income and expenses recorded on a trade-date basis for the institutional division and on a settlement-date basis for the retail division. The difference between the settlement date basis used for the retail division and the trade date basis required by GAAP is not material. Investment banking revenue is recorded as follows: 1) underwriting fees at the time the underwriting is completed and income is reasonably determinable, 2) corporate finance advisory fees as earned, according to the terms of the specific contracts and 3) sales concessions on a trade-date basis.

Securities Owned

Financial instruments owned and financial instruments sold but not yet purchased are recorded on a trade date basis and are carried at fair value. Fair value is based on quoted market prices or dealer quotes where those are available and considered reliable. Additionally, other factors may be considered where appropriate such as market prices for related or similar financial instruments and upon yield, credit quality, prepayment terms, volatility, and other economic factors. Unrealized gains and losses on securities, forward, future and option contracts, if any, are reflected in the Statement of Income.

The Company self clears its proprietary transactions. Non-proprietary transactions are cleared by its clearing broker.

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Securities Purchased/Sold Under Agreements to Resale/Repurchase

Repurchase and resale agreements are treated as collateralized financing transactions and are carried at the amounts at which the securities will be reacquired or resold as specified in the respective agreements. Interest income and expense related to these agreements is recorded on the accrual basis.

It is the Company's policy to take possession of securities purchased under resale agreements and such collateral is not reflected in the financial statements. The Company monitors the market value of the securities received as collateral under the resale agreements as compared to the related receivable, including accrued interest, and requests additional collateral when deemed appropriate.

The Company maintains control over the securities sold under repurchase agreements. The securities pledged as collateral under such agreements are included in the financial statements.

Receivables and Payables to Broker-Dealers and Counterparties

At June 30, 2008, receivables and payables to broker dealers and counterparties consist of the following:

Receivables

Clearing broker	\$	2,072
Investment banking fees		554
Securities failed to deliver		362
Net Unsettled Transactions		8,087
Other		3,989
	\$	<u>15,064</u>

Payables

Securities failed to receive	\$	1,518
Other		3,960
	\$	<u>5,478</u>

Fixed Assets

Fixed assets are composed of furniture, equipment and leasehold improvements. Furniture and equipment, are initially recorded at cost and depreciated using the straight-line method over the estimated useful life of the related assets (between 3 and 10 years). Leasehold improvements are amortized over the lesser of the economic useful life of the improvement or the term of the lease.

Other Assets

Included in Other Assets are forgivable loans made to financial consultants, typically in connection with their recruitment. These loans are forgivable based on continued employment and are amortized over the terms specified in each agreement, which is generally four to nine years, using the straight-line method.

Income Taxes

A deferred tax asset or liability is recognized for the estimated future tax effects attributable to temporary differences. A related valuation allowance is recognized when it is more likely than not that

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the deferred tax asset will not be realized. A temporary difference is the difference between the tax basis of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible amounts in future years when the reported amount of the asset or liability is recovered or settled.

Temporary differences giving rise to deferred tax assets and liabilities are attributable to deferred compensation, and other revenues and expenses which are reported for tax purposes in different years than for financial reporting purposes.

Goodwill and Other Intangibles

Goodwill represents the excess of the purchase price and related costs over the value assigned to net assets acquired. Other intangible assets are recognized separately from goodwill when they arise from contractual or other legal rights or are separable and their fair value can be measured reliably. Goodwill will not be amortized but rather will be tested at least annually for impairment. Other intangible assets that have a finite useful life are amortized over a period based on the expected useful life.

Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a consistent framework for measurement of fair value. Additionally, SFAS 157 eliminates the requirement to defer calculated profit or loss on transaction values that include unobservable inputs "Day 1 profit or loss" and eliminates the use of block discounts for securities traded in an active market. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The provisions of SFAS 157 should be applied prospectively upon initial adoption, except for the provisions that eliminate prior measurement guidance regarding block discounts and Day 1 profit or loss. Those changes should be applied retrospectively as an adjustment to the opening balance of retained earnings in the period of adoption. The Company believes the adoption of SFAS 157 will not have a significant impact on the statement of Financial Condition.

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 irrevocably choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. For any eligible items that exist at the effective date for which an entity chooses to elect the fair value option, the effect of the first remeasurement to fair value shall be reported as a cumulative-effect adjustment to the opening balance of retained earnings. The Company is currently assessing the impact SFAS 159 will have on its Statement of Financial Condition.

In June 2006, the FASB issued FASB interpretation No. 48 Accounting for Uncertainty in Income Taxes- an interpretation of SFAS No. 109, ("FIN 48"), which prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of uncertain tax positions. The Company adopted the provisions of FIN 48 on January 1, 2007. The implementation of FIN 48 did not have a significant impact on the Company.

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2. Securities Owned

Securities owned, at fair value, as of June 30, 2008 were as follows:

United States Government and its agencies	\$ 5,539
State and municipal governments	27,217
Mortgage-backed securities	41,789
Corporate and other securities	36,953
	<u>\$ 111,498</u>

During the year ended November 30, 2004, the Company transferred approximately \$61 million of GNMA mortgage-backed securities to an irrevocable trust in exchange for collateralized mortgage obligation (CMO) certificates. The Company derecognized the mortgage-backed securities transferred given that it relinquished control over such securities. The mortgage-backed securities transferred were accounted for at fair value prior to securitization. The Company subsequently retained approximately \$25 million of such certificates including a residual interest certificate (interest only). Such residual interests are accounted for at fair value and included in the "Mortgage-backed securities" caption above. Cash flows received on the residual retained interest were approximately \$393 for the six months ended June 30, 2008.

The following table sets forth the weighted average key economic assumptions used in measuring the fair value of the residual retained interest, for which fair value is based on discounted cash flows, and the sensitivity of those fair values to immediate adverse changes of 10% and 20% in those assumptions:

Fair value of residual retained interest	\$ 1,946
Weighted-average life (in years)	4.33
Prepayment speed assumption (annual rate)	13.50%
Impact on fair value of 10% adverse change	\$ (103)
Impact on fair value of 20% adverse change	\$ (189)
Discount rate (annual)	14.77%
Impact on fair value of 10% adverse change	\$ (73)
Impact on fair value of 20% adverse change	\$ (142)

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a 10 and 20 percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the residual retained interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments, which might magnify or counteract the sensitivities).

3. Securities Owned Held in Segregation

U.S. Treasury Bills with a market value of \$274 have been segregated in a special reserve bank account for the benefit of customers under Rule 15c3-3 of the Securities and Exchange Commission.

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4. Securities Purchased Under Agreements to Resell

The securities underlying the agreements to resell were delivered to, and are held by the Company. The counterparties to such agreements maintain effective control over such securities. Although the Company is permitted by contract or custom to repledge the securities, it has agreed to resell to the counterparties the same or substantially similar securities at the maturity of the agreements.

The fair value of the collateral securities received by the Company on these transactions as of June 30, 2008 was as follows:

Repledged	\$ 200,602
Not repledged	<u>4,084</u>
	<u>\$ 204,686</u>

The repledged securities were used as underlying collateral for securities sold under agreements to repurchase.

5. Goodwill and Other Intangible Assets

On December 7, 2007, the Company acquired from Citigroup Global Markets, Inc. the Puerto Rico operations of the broker-dealer Smith Barney in order to expand the Company's retail business. This transaction was accounted under the purchase method of accounting. The purchase price was allocated between goodwill and other intangible assets.

6. Securities Sold Under Agreements to Repurchase

The following table summarizes certain information on securities sold under agreements to repurchase as of June 30, 2008.

Securities sold under agreements to repurchase	<u>\$ 260,214</u>
Maximum aggregate balance outstanding at any month-end	<u>\$ 410,390</u>
Average monthly aggregate balance outstanding	<u>\$ 296,550</u>
Weighted average interest rate	
At June 30, 2008	<u>2.74%</u>
For the period	<u>2.79%</u>

7. Subordinated Borrowings

The Company has a revolving subordinated loan agreement with Popular, Inc. maturing on November 15, 2012. Under the agreement, the Company may borrow up to \$50,000. The interest rate on this loan is adjusted quarterly to the comparable floating spread for three-months LIBOR plus 12.5 basis points. All borrowings under this agreement qualify as regulatory capital and the agreement includes all statutory restrictions specified by the Uniform Net Capital Rule. The Company had no borrowings outstanding during the year under this agreement.

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8. Deferred Compensation

Plan A

Under the deferred compensation plan for the institutional division employees, participants are required to defer a portion of their incentive performance bonus. The amount deferred and interest thereon are paid to participants as follows: (a) 50% on or before January 31 of the second fiscal year following the fiscal year for which such amounts were contributed and (b) 50% on or before January 31 of the third fiscal year following the fiscal year for which such amounts were contributed.

Total amount deferred related to this plan included in deferred compensation as of June 30, 2008 amounted to \$492.

Total liability under this plan not deferred, included in accrued employee compensation and benefits, amounted to \$2,102.

Plan Trust

On October 22, 1999 the Company created a trust (the "Trust") to invest the amount deferred under Plan A, if so elected by the participant. The Trust's assets are subject to the claims of the Company's creditors in the event of the Company's insolvency until paid to each Plan's participants at such times as specified above.

The principal balance held by the Trust and any realized and unrealized appreciation are exclusively for the benefit of each Plan's participants. As of June 30, 2008, the Trust had 40,610 shares of common stock of Popular, Inc. related to Plan A. These shares are carried at cost, as treasury stock in the Statement of Financial Condition.

Plan C

Under the deferred compensation plan for the retail division employees, the participants' deferred compensation must be deferred completely. The principal and interest thereon have a vesting period of five years. The deferred compensation expense related to this plan is recognized over the vesting period. The interest on the principal amount deferred is the result of earnings of the investment of such principal in certain financial instruments as defined by Plan C.

Total plan liability as of June 30, 2008 amounted to \$1,439 included as deferred compensation in the Statement of Financial Condition.

9. Employee Benefit Plan

The Company maintains a contributory savings plan which is available to employees with more than three months of service. Company contributions include a matching contribution and an additional discretionary profit sharing contribution. Employees are fully vested on these contributions after five years of service. The plan's trustee is an affiliated company.

10. Income Taxes

Temporary differences which give rise to the deferred tax asset at June 30, 2008, are as follows:

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Deferred tax asset	
Deferred compensation	\$ 868
Other	949
Net deferred tax asset	<u>\$ 1,817</u>

11. Financial Instruments

The financial instruments of the Company are reported in the Statement of Financial Condition at market or estimated fair value or at carrying values that approximate fair values, because of their short-term nature.

Fair values for financial instruments are based on quoted market prices, quoted prices for similar financial instruments or various pricing models based on discounted anticipated cash flows.

Transactions involving financial instruments sold, not yet purchased, entail an obligation to purchase a financial instrument at a future date. The Company may incur a loss if the market value of the financial instrument subsequently increases prior to the purchase of the instrument.

12. Derivatives

Derivative contracts are financial instruments, such as future, forward, swap or option contracts, that derive their value from underlying assets, indices, reference rates or a combination of these factors. Derivatives may involve future commitments to purchase or sell financial instruments. The amounts exchanged are based on the specific terms of the contract with reference to specified rates, securities or indices.

Most of the Company's derivative transactions are entered into for trading purposes. The Company uses derivatives in its trading activities to facilitate customer transactions, to take proprietary positions and as means of risk management. Gains and losses on derivatives used for trading purposes are generally included as "trading gain or loss" in the Statement of Income.

By using derivative instruments, the Company exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligation under a derivative contract, the Company's credit risk will equal the fair-value gain in a derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the Company, thus creating a repayment risk for the Company. The repayment risk is minimized by requiring posting of collateral within certain thresholds. When the fair value of a derivative contract is negative, the Company owes the counterparty and, therefore, assumes no repayment risk.

Options are contracts that grant the purchaser the right to buy or sell the underlying asset by a certain date at a specified price. The risk involved with purchased option contracts is normally limited to the price of the options. Interest rate future contracts are commitments to either purchase or sell designated instruments, such as U.S. Treasury securities, at a future date for a specified price. Future contracts are generally traded on an exchange, and are marked to market daily, and are subject to margin requirements.

The notional amounts of derivative financial instruments represent the volume of these transactions and not the amounts potentially subject to market risk. In addition, measurement of market risk is meaningful only when all related and offsetting transactions are taken into consideration.

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The Company entered into mortgage-backed securities (TBAs) for trading purposes. The gross notional amounts of these forward commitments to sell as of June 30, 2008 amounted to \$8,000 and the gross notional amount of the commitments to purchase amounted to \$8,000. The fair value of these derivative financial instruments at June 30, 2008 amounted to \$52 and \$50, respectively.

13. Concentration of Credit Risk

The Company is engaged in various trading and brokerage activities in which counterparties primarily include broker-dealers, banks, and other financial institutions. In the event counterparties do not fulfill their obligations, the Company may be exposed to risk. The risk of default depends on the creditworthiness of the counterparty or issuer of the instrument. It is the Company's policy to review, as necessary, the credit standing of each counterparty. Also, the Company's main business is with individual customers and corporations in Puerto Rico.

14. Commitments and Contingent Liabilities

At June 30, 2008, the Company has obligations under a number of noncancelable leases, for office space which require rental payments as follows:

Year	<u>Minimum Payments</u>
2009	636
2010	664
2011	240
	<u>\$ 1,540</u>

Certain lease agreements contain provisions for future rent increases. The total amount of rental payments due over the lease term is being charged to rent expense on the straight-line method over the term of the lease. The difference between rent expense recorded and the amount paid is charged to "Deferred rent obligation", which is included in "Accounts payable to affiliates" in the accompanying Statement of Financial Condition. Total Deferred rent obligation as of June 30, 2008 amounted to \$217.

In the ordinary course of business, the nature of the Company's business subjects it to claims, lawsuits, regulatory examinations and other proceedings. The results of these matters cannot be predicted with certainty. There can be no assurance that these matters will not have a material adverse effect on the Company's results of operations in any future period and a material judgment could have a material adverse impact on the Company's financial condition and results of operations. However, it is the opinion of management, after consultation with legal counsel that, based on information currently available, the ultimate outcome of these matters will not have a material adverse impact on the business, financial condition, operating results or liquidity of the Company although those might be material to operating result for any particular period, depending, in part, upon operating results for that period.

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15. Clearance Agreements

The Company has clearing and custody agreements with National Financial Services, Inc. ("NFS"), for its retail brokerage operation. The Company's institutional division self-clears its transactions through Bank of New York. NFS is a member of various stock exchanges and subject to the rules and regulations of such organizations as well as those of the Securities and Exchange Commission. Under the terms of the agreement, NFS clears and executes the brokerage transactions of the Company's customers on a fully disclosed basis.

16. Guarantees

Under the terms of the clearance agreements with NFS, the clearing broker has the right to charge us for losses that result from a counterparty's, introduced by the Company, failure to fulfill its contractual obligations which default could have material effect on our business, financial condition and operating results. The Company is unable to develop an estimate of the maximum assumptions under these agreements and the probable exposures, however, the exposure at June 30, 2008 was immaterial.

17. Related Party Transactions

In the normal course of business, the Company enters into transactions with affiliated companies. The Statement of Financial Condition at June 30, 2008, included \$24,890 and \$13,658 in repurchase and resale agreements, respectively, with affiliates. Accrued interest payable and receivable related to these transactions amounted to \$4 and \$20, respectively.

At June 30, 2008, the Company owned securities issued by affiliates and affiliated funds with a fair value of approximately \$14,534.

18. Stock Option Plan

The Company participates in Popular, Inc.'s stock option plan, which permits the granting of incentive awards in the form of qualified stock options, incentive stock options, or non-statutory stock options of Popular, Inc. This plan provides for the issuance of Popular Inc.'s common stock at a price equal to its fair market value at the grant date, subject to certain plan provisions. The maximum option term is generally ten years from the date of grant.

Popular, Inc. uses the fair value method of recording stock options as described in Statement of Financial Accounting Standards No. 123 "Accounting for Stock-Based Compensation". All future stock option grants will be expensed over the stock option vesting period based on the fair value at the date the options are granted.

19. Net Capital Requirements

As a registered broker-dealer, the Company is subject to the Uniform Net Capital Rule 15c3-1 (the "Rule") under the Securities Exchange Act of 1934 and has elected to compute its net capital in accordance with the alternative method of the Rule. Under the alternative method, the Company is required to maintain at all times a net capital equal to the greater of \$250 or 2% of aggregate debit items computed in accordance with the Rule. At June 30, 2008, the Company's net capital of \$12,480 was \$12,099 in excess of required net capital of \$381. The Company's ratio of debt to equity was 0%, which is below the maximum requirement specified by the Rule.

